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The Association of Investment Companies

# Interim management statements

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## To discuss the issues raised in this paper please contact:

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## Background

In implementing the Transparency Directive, many of the regulations relating to financial reporting have been moved from the Listing Rules into a newly created Chapter 4 of the Disclosure Rules, now called the Disclosure and Transparency Rules (DTR). One of the new requirements in Chapter 4 is to produce a biannual 'interim management statement' (IMS).

***This commentary explores how investment companies might prepare an IMS and the issues that they will need to consider.***

### 1. Who needs to prepare an IMS?

[The requirement to prepare interim management statements] *applies to an issuer:*

- (1) whose shares are admitted to trading; and*
- (2) whose Home State is the United Kingdom. (DTR 4.3.1R)*

To be required to prepare an IMS, the company's shares must be admitted to trading on a regulated market. The term 'regulated market' includes the main market of the London Stock Exchange but does not include AIM. **Companies whose shares are only traded on AIM are therefore not required to produce an IMS, but may wish to do so on a voluntary basis. However, we anticipate that virtually all other AIC Members will have to produce an IMS. Our analysis is set out below.**

The FSA's Glossary defines Home State for the purposes of DTR as:

*"the Member State chosen by the issuer from among the Member State in which the issuer has its registered office and those Member States which have admitted its securities to trading on a regulated market on their territory. The issuer may choose only one Member State as its home Member State. Its choice shall remain valid for at least three years unless its securities are no longer admitted to trading on any regulated market in the Community."*

For the AIC's UK domiciled Members, it is likely that the UK will be their Home State by default, as this will be where their registered office is and their shares will normally only be admitted to trading on the London Stock Exchange.

For the AIC's non-UK domiciled Members, it is also likely that the UK will be their Home State by default. This is because the majority of the AIC's non-UK domiciled Members will have a registered office outside an EEA Member State (e.g. Guernsey, Jersey etc). Their choice of Member State will

therefore be limited to the Member State(s) where their shares are admitted to trading on a regulated market, which again is likely only to be the UK.

Some Members may, however, have a choice of Home State. This may be because their registered office is based in an EEA Member State other than the UK, or because their shares are admitted to trading on more than one regulated market in the EEA.

In such cases, it should be noted that choosing a Home State as anything other than the UK does not mean that the company will be exempt from the requirement to prepare an IMS – it simply means that the company does not have to comply with the requirements for the IMS as implemented by the FSA in DTR, including the timetable for introduction. It will instead have to comply with the requirement to prepare an IMS under a different jurisdiction's rulebook. **The AIC strongly recommends that, where a Member believes that its Home State could potentially be a state other than the UK, it seeks advice as to the practical implications of this. This commentary only applies to investment companies producing an IMS in accordance with the FSA's requirements.**

### Exemption for non-EEA State companies

DTR 4.4.8 and DTR 4.4.9 state:

*"An issuer whose registered office is in a non-EEA State whose relevant laws are considered equivalent by the FSA is exempted from the rules on....interim management statements.*

*The FSA maintains a published list of non-EEA States which....are judged to have laws which lay down requirements equivalent to those imposed upon issuers by this chapter."*

There are, at present, no non-EEA States which have been identified as having equivalent requirements by the FSA. This exemption is therefore of no practical relevance at the moment.

## 2. When should the IMS be published?

*An issuer must make public a statement by its management during the first six-month period of the financial year and another statement by its management during the second six month period of the financial year. (DTR 4.3.2R)*

*The statement required by DTR 4.3.2R must be made in a period between ten weeks after the beginning, and six weeks before, the end of the relevant six-month period. (DTR 4.3.3R)*

The requirement for an IMS applies to companies with an accounting period beginning on or after 20 January 2007.

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The table below shows the earliest and latest dates for publication of the IMS for each month year-end.

<b>Accounting period beginning</b>	<b>Earliest date of publication of 1<sup>st</sup> IMS</b>	<b>Latest date of publication of 1<sup>st</sup> IMS</b>	<b>Earliest date of publication of 2<sup>nd</sup> IMS</b>	<b>Latest date of publication of 2<sup>nd</sup> IMS</b>
<b>1 February 2007</b>	12 April 2007	19 June 2007	10 Oct 2007	20 Dec 2007
<b>1 March 2007</b>	10 May 2007	20 July 2007	10 Nov 2007	17 Jan 2008
<b>1 April 2007</b>	10 June 2007	19 Aug 2007	10 Dec 2007	18 Feb 2008
<b>1 May 2007</b>	10 July 2007	19 Sept 2007	10 Jan 2008	19 March 2008
<b>1 June 2007</b>	10 Aug 2007	19 Oct 2007	9 Feb 2008	19 April 2008
<b>1 July 2007</b>	9 Sept 2007	19 Nov 2007	11 March 2008	19 May 2008
<b>1 August 2007</b>	10 Oct 2007	20 Dec 2007	11 April 2008	19 June 2008
<b>1 September 2007</b>	10 Nov 2007	18 Jan 2008	10 May 2008	20 July 2008
<b>1 October 2007</b>	10 Dec 2007	18 Feb 2008	10 June 2008	19 Aug 2008
<b>1 November 2007</b>	10 Jan 2008	19 March 2008	10 July 2008	19 Sept 2008
<b>1 December 2007</b>	9 Feb 2008	19 April 2008	10 Aug 2008	19 Oct 2008
<b>1 January 2008</b>	11 March 2008	19 May 2008	9 Sept 2008	19 Nov 2008

### 3. What period should the information in the IMS cover?

*The interim management statement must contain information that covers the period between the beginning of the relevant six-month period and the date of publication of the statement. (DTR 4.3.4R)*

As explained above, an IMS can (depending on when it is issued) cover a reporting period, roughly speaking, ranging from two and a half months to four and a half months. It is for the board to determine where the end of each IMS reporting period should lie.

### 4. What should be disclosed in an IMS?

*The interim management statement must provide:*

- (1) an explanation of material events and transactions that have taken place during the relevant period and their impact on the financial position of the issuer and its controlled undertakings, and*
- (2) a general description of the financial position and performance of the issuer and its controlled undertakings during the relevant period. (DTR 4.3.5R)*

The requirements for the contents of an IMS are relatively high-level and open to interpretation. In the December 2006 issue of 'List!', the FSA stated that it wished to encourage a 'market-led solution' to determine the appropriate detail of IMS reporting. It also said that companies should use their professional judgement to decide what is important and what should be reported to shareholders.

The FSA has also been keen to clarify that the IMS is intended to be less demanding than producing quarterly reports (which were originally envisaged in the Transparency Directive) and that companies are not expected to apply the conventions currently required for annual and half-yearly reports. The AIC envisages that, for most investment companies, the IMS should not be a lengthy document, and that something of the length and level of detail often found in periodic factsheets commonly produced for investment companies (i.e. 1-2 pages) would be sufficient to meet the high-level requirements of an IMS.

In drafting their IMS reports, boards may wish to give consideration to the balance of narrative and numerical information provided. The DTR calls for an "explanation" of material events and transactions and a "general description" of the financial position and performance, which may be taken to suggest a predominantly narrative focus is required. However, in explaining the "impact" of material events and transactions on the financial position, the board may feel it is more appropriate to give more emphasis to numerical information.

We have set out below a range of information that an investment company board may wish to consider disclosing in its IMS. Clearly, there is a very long list of information that might be covered, and we have not attempted to be exhaustive. **It is up to each investment company board to decide what information should be disclosed to meet the requirements of the DTR.** In other words, the board needs to select information which shareholders would find of most interest and relevance in relation to explaining material events and transactions, their impact on the company's financial position, and a general description of the financial position and performance for the period under review.

**We would emphasise that there can be no 'one size fits all' model IMS - the range of material necessary to meet the DTR requirements would differ between investment companies and over time. Undoubtedly there are some items, like net asset value (NAV), which the AIC would expect to be included in most IMS. However it may still be legitimate for a board not to include this information if it was felt unnecessary or if the requirements of the IMS can be met by other disclosures.**

**Set out below are a range of issues that boards might want to address in an IMS. In some instances, the suggestions below may go further than the minimum required by the DTR. A board could therefore reasonably decide this information need not be disclosed, but it should always ensure that the information it does provide meets the minimum requirements.**

The IMS requires explanation of four distinct areas:

### **a) Material events and their impact on the financial position of the company**

Material events might include changes in the company's name, domicile, investment policy, benchmark, or board structure or members. It might also include the introduction of a discount control mechanism, or significant amendments to the terms of the management agreement, or indeed a change of manager, or management personnel.

The DTR also requires an explanation of the impact of material events on the financial position of the company. For example, where the board has concluded that amendments to the fee arrangements with the manager are a material event and as such must be disclosed in the IMS, this statement should be supported by an explanation of the impact of these amendments on, say, the amount and timing of management fee and/or performance fee payments.

### **b) Material transactions and their impact on the financial position of the company**

Material transactions are likely to include key portfolio changes. Where the investment company has made material portfolio acquisitions or disposals during the period, these changes, and the impact they have had on the financial position of the company (e.g. the increase in the amount of cash held as a result of a major disposal), will need to be explained.

The AIC does not consider that there is any requirement to provide a detailed analysis of the portfolio (as the IMS focuses on events and transactions “that have taken place during the relevant period”). However, we imagine that some investment companies will choose to provide a list of their top holdings and/or asset allocation etc. Such information is also useful in demonstrating the impact that major changes in the portfolio have had on the financial position of the investment company.

Other material transactions may include changes to the capital structure of the company, for example share buy-backs or sales from treasury, or changes to the level of gearing. It might also include the payment of dividends during the period.

### **c) General description of financial position**

As explained above, there is no formal requirement for the IMS to contain NAV information. However, it is likely that most investment companies would provide this as part of their general description of the financial performance of the company.

If a company chooses to provide an NAV, the AIC does not believe that it needs to be a ‘real-time’ NAV, i.e. calculated on the date of the publication of the IMS. A real-time NAV would go beyond “a general description” of the financial position and performance of the investment company. If an up-to-date NAV were an essential component of an IMS, then there would be difficulties as it is unlikely to be practical to produce a NAV on the date of publication and get the IMS signed off and distributed on the same day. This would be impossible for many investment companies, especially those with a significant unquoted or property element to their portfolios.

If a company chooses to include a NAV in its IMS, the AIC believes the company should use the most recent NAV it is practical to use. In this instance the IMS should make clear the date on which that NAV was produced. The board may also wish to consider making a statement in the IMS to confirm that it is not aware of any significant events or transactions which have occurred between the ‘as at’ date of the financial information and the date of publication of the IMS which would have a material impact on the financial position of the company.

Where the NAV has moved materially during this period, then the AIC suggests that the publication of the IMS should be delayed until such a point that the current financial position can be better reflected, bearing in mind the DTR publication deadlines.

It is also recommended that the IMS contains information on where current performance information (e.g. a daily NAV) can be obtained from, for example by providing a link through to the company’s or manager’s website.

For investment companies where there is a significant period of time between the date of the most recent NAV and the date of publication of the IMS (most likely to occur with private equity investment companies, property investment companies or venture capital trusts), the investment company will need to consider whether any further information on the valuation of the portfolio should be disclosed to adequately explain the financial position of the company. This might be best provided in narrative form.

Investment companies may also wish to publish a figure for total assets to provide further information.

The AIC also anticipates that most investment companies would seek to provide information on gearing. Where gearing is at a material level this will help investors to understand the financial position of the company, as well as providing information to help them assess the possible future performance of the company.

### **d) General description of financial performance**

Information on share price and discount movements is highly valued by investors and the AIC would anticipate most investment companies will choose to provide this.

The requirements for the IMS only refer to a “general description” of performance over the period under review. However, the AIC considers that most investment companies will provide statistical information. In addition, it might also choose to provide information covering other periods, over and above the requirements of the IMS to avoid encouraging too short-term a view of performance. This could be presented in a tabular or graphical format.

It is a matter of choice which measures of performance are shown. However, the AIC anticipates that the most likely measures which will be used are share price total return and NAV total return. The AIC also anticipates that performance of the benchmark in the same period(s) will be given.

## 5. How should IMS be distributed?

The IMS must be ‘made public’ in accordance with DTR 4.3.2 above. As the IMS is classed as ‘regulated information’ the investment company must also comply with the rules regarding the filing and dissemination of information as set out in DTR 6.2.3 and DTR 6.3. In practice, **we anticipate that most IMS will be announced to the market via a regulatory information service, as well as being made available on the company’s or manager’s website.**

## 6. Are there exemptions from publishing an IMS?

*An issuer which publishes quarterly financial reports:*

- (1) in accordance with national legislation; or*
- (2) in accordance with the rules of the regulated market; or*
- (3) of its own initiative,*

*will be taken as satisfying the requirement to make public the statements required by DTR 4.3.2R. (DTR 4.3.6R)*

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Where an investment company publishes quarterly financial reports, it may be able to rely on an exemption under DTR 4.3.6 from producing an IMS.

For example, UK investment companies which are required, under Sections 272 and 273 of the Companies Act 1985, to prepare interim or initial accounts to support the quarterly declaration of dividends, would be exempt from publishing an IMS.

The exemption also applies to a company which publishes a quarterly financial report 'of its own initiative'. The wording of this part of the exemption is unclear in terms of the manner in which a quarterly financial report would have to be prepared in order to obtain an exemption from producing an IMS. The FSA has confirmed that subsection (c) of DTR 4.3.6 should be read as 'of its own initiative in accordance with national legislation or the rules of the regulated market'. This wording more closely mirrors the IMS regulations which are contained in Article 6(2) of the Transparency Directive and the FSA is considering an amendment to the DTR in this regard.

Where an investment company produces quarterly financial reports which provide an exemption from publishing an IMS, the FSA has confirmed that the company does not need to follow the IMS reporting timetable for publishing its quarterly financial report. In other words, a quarterly financial report which is prepared instead of an IMS does not need to be published "*in a period between ten weeks after the beginning, and six weeks before, the end of the relevant six-month period*" (DTR 4.3.3R). There may, however, be other reporting deadlines which the company needs to be aware of.



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