INSIDE AIM

Issue 1- December 2009

WELCOME TO INSIDE AIM

Welcome to this first edition of Inside AIM, a periodic newsletter from the AIM Regulation team.

Inside AIM is designed to keep the AIM adviser community, in particular the nominated advisers ("nomads"), updated on key AIM policy and technical matters where we receive regular requests for clarification or explanation on the application of the AIM Rules. We hope that this will be helpful and we welcome views on other items that you would like to be addressed in future issues.

We expect Inside AIM to be published bi-annually, or as required.

Bob Beauchamp - Acting Head of AIM Regulation

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"Communicating with the AIM advisory community is a vital part of ensuring the continued success and growth of AIM and I hope Inside AIM helps to build further on our close working relationship.

Over £4.6bn has been raised on AIM this year, demonstrating its continuing critical role in providing finance to growing companies that are pivotal to future economic growth, and we continue to look at initiatives to promote AIM's benefits. These include supporting the wider take up of equity research, our regional investor roadshow programme, lobbying the Government to allow greater freedom for Venture Capital Trusts to invest in smaller quoted companies and working closely with the market making community to develop greater liquidity in AIM securities.

Looking to the future, the fundamentals of AIM remain strong and the market structure continues to create a compelling offering for companies seeking to raise funds and their profile via a public market. I look forward to continuing to work with you to ensure AIM retains its position as a leading global growth market."

Marcus Stuttard - Head of AIM

REGULATORY STATUS OF INSIDE AIM

The technical guidance provided in this newsletter should be regarded as illustrative only. It is intended to give an indication of how AIM Regulation expects certain aspects of the AIM Rules to be interpreted and is not definitive. AIM Regulation should be contacted by a company's nomad if clarification or a derogation from the rules is required.

As usual, AIM companies should continue to seek the guidance of their nomad when looking for assistance on the application of the AIM Rules.

Any amendments to existing AIM Rules will continue to be communicated via AIM Notices and will be subject to the usual public consultation process where appropriate. Amendments to our rules will not be introduced through Inside AIM.

TECHNICAL GUIDANCE

This section aims to provide detailed technical guidance on areas of the AIM Rules where we receive regular requests for additional clarification. Guidance on less complicated matters is included in the FAQs set out throughout this newsletter.

AIM RULE 13 - AGGREGATION OF DIRECTORS' PARTICIPATION IN A RELATED PARTY TRANSACTION

Where more than one director participates in the same transaction with an AIM company, for example in a share placing, it may be appropriate to aggregate their participation when calculating the class tests to assess whether AIM Rule 13 applies.

This treatment reflects the fact that the directors may be able, or viewed to be able, to act in concert when setting the terms of the transaction. As a result, it may be more likely that the provisions of AIM Rule 13, including the need for a 'fair and reasonable' statement, apply.

PURCHASE BY AN AIM COMPANY OF ITS OWN SECURITES

In the case of an AIM company contemplating the purchase of its own securities, AIM Rules 13, 17 and 21 may be applicable.

Tender offers

The AIM Rules do not deal specifically with tender offers, i.e. there is no requirement for one to be completed if the AIM company is purchasing more than 15% of its own securities. However, should an AIM company decide to complete a tender offer, we support the market practice of completing such an offer in accordance with the Listing Rule requirements.

A tender offer is defined as a corporate action in the London Stock Exchange's (the "Exchange") Admission and Disclosure Standards (7 September 2009). Whilst these Standards do not specifically apply to AIM companies, in practice any tender offer timetable will still require approval by the Stock Situations and Analysis team of the Exchange before any notification of the timetable is made in accordance with AIM Rule 24.

Contact details for Stock Situations are included at the end of this newsletter.

Share buy-backs

Similarly, the AIM Rules do not specifically refer to share buy-backs, with the exception that an AIM company cannot purchase its own securities during a close period (AIM Rule 21). As in the case of tender offers, we consider that in most circumstances compliance with the requirements of the Listing Rules, in particular Listing Rule 12.4.1, would represent best practice.

When a situation does arise where an AIM company wishes to complete a buy-back programme during a close period, a formal derogation request should be submitted in advance of the close period with full details of the programme. AIM Regulation will consider such derogation requests on a case-by-case basis, taking into account:

- the nature of the close period and any price sensitive information held;
- whether the dates and quantities of the securities to be purchased are fixed and announced in advance of the close period commencing; and
- whether the buy-back is being independently managed by a third party.

Other AIM Rule considerations

For tender offers and share buy-back programmes, the purchase and cancellation of an AIM company's shares will also require an announcement pursuant to AIM Rule 17.

The nomad should also consider whether AIM Rule 13 is applicable to the share purchases.

AIM RULE 14 - ENTERING INTO AN OPTION AGREEMENT TO COMPLETE A REVERSE TAKEOVER

This section applies to AIM companies that are considering entering into an option agreement that would on exercise be treated as a reverse takeover.

The guidance note to AIM Rule 14 requires suspension of trading in the AIM securities following the announcement of a proposed reverse takeover as there is a risk of insufficient information in the market for investors to accurately assess the impact of the transaction on the company's financial position.

Nomads should therefore contact us prior to the announcement of such an option to discuss whether suspension may be required. The exact terms of the option, together with the factors below, help determine this:

- Does the option agreement itself need disclosing as a substantial transaction due to the consideration being paid?
- How long is the exercise period of the option?
- Is the decision to exercise entirely at the company's discretion?
- Are there any conditions to the option agreement that need to be satisfied before exercise?

To prevent suspension, the negotiations concerning a reverse takeover should be conducted confidentially. A call option entered into by a company to purchase a target, which does not itself require disclosure as a substantial transaction, may, depending on the terms of the option and other circumstances, be viewed as a matter in the course of negotiation and not require notification until subsequent exercise. AIM Regulation should be contacted in these circumstances.

FAQ

Q. Can a Qualified Executive ("QE") applicant and an existing QE cite the same Relevant Transaction?

A. Subject to the certain conditions, yes.

We believe there is a common misunderstanding amongst the nomad community with regard to the citing of Relevant Transactions by more than one QE, particularly by new QE applicants and existing QEs.

Whilst it remains the case that only one existing QE may be regarded as lead QE on a Relevant Transaction for the purposes of ongoing eligibility, unless such a transaction has been agreed with us as being sufficiently complex, this transaction may also still be cited by a QE applicant. This recognises the importance of an applicant being able to shadow an existing QE to be able to qualify.

This is permitted where the role performed by the applicant is in a co-lead capacity with them having a material role in discharging the nomad responsibilities. In all circumstances, the existing QE should continue to have day to day involvement in the transaction and oversight of the work undertaken.

We place reliance on the nomad firm to assess the readiness of junior corporate finance executives for QE approval. We would expect this to be when an applicant is able to act as the lead adviser on a Relevant Transaction without the supervision of an existing QE.

COMPANIES ACT 2006 AND AIM RULE 19

Following the implementation of the provisions of the Companies Act 2006 ("CA 2006") we have received enquiries concerning the potential impact of the revised reporting deadlines.

In summary, the changes mean that public companies incorporated in England and Wales are now subject to a shorter deadline of six months (previously seven months) during which time they must present their accounts at their annual general meeting and file them with Companies House. These periods are calculated from the end of the relevant accounting reference period.

As a result of these changes, AIM companies incorporated in England and Wales will in practice have to send their annual accounts to shareholders before the six month deadline referred to in AIM Rule 19, to ensure that all the actions required by CA 2006 can be completed within the six month period.

We would like to confirm that there is currently no intention to make any changes to the AIM Rules as a result of the revised reporting timetable. The CA 2006 does not conflict with AIM Rule 19 and AIM companies should always be mindful of requirements contained in the relevant legal framework of their country of incorporation that may impose additional reporting requirements to those prescribed in the AIM Rules.

THE AIM NOTE FOR INVESTING COMPANIES

On 1 June 2009, a revised version of the AIM Rules and the AIM Note for Investing Companies (the "Note") were released. Full details of the rule changes were included in AIM Notices 30 and 33.

Based on queries received, we would like to clarify the following points.

Appropriate entities and security types for admission to AIM

We would normally expect an investing company to be a closed-ended entity of a similar structure to a UK plc and would expect its security structure to be straightforward, issuing primarily ordinary shares or equivalent.

The following, non-exhaustive list of security/company types generally fall outside of what is considered appropriate for admission to AIM:

- Open-ended investing companies, including unit trusts;
- Protected cell companies;
- Partly paid shares;
- Non-voting shares as a primary line of security;
- Shares redeemable on an open basis; and
- Stapled units.

AIM Regulation should be consulted at an early stage if there is any concern that the security type or company structure being proposed for admission is likely to fall in one of the above-mentioned categories.

FAQ

Q. The AIM company we represent is contemplating a disposal – do we need to apply the gross capital test?

A. No – the gross capital test is only required when the AIM company is making an acquisition.

Q. The AIM company for which we act is about to complete a significant fundraising, potentially in excess of 100% of the company's existing share capital. How should we apply AIM Rule 14, the reverse takeover rule?

A. AIM Rule 14 is only applicable if there is an acquisition; it will not be relevant when only a significant fundraising is taking place.

Implementation of an investing policy following a Rule 15 disposal

The assessment as to whether an investing company has implemented its investing policy is not necessarily the same for a company following a fundamental disposal under AIM Rule 15 as it is for a newly admitted investing company subject to the provisions of AIM Rule 8.

Under AIM Rule 8 an investing company has to substantially implement its investing policy within eighteen months of admission or otherwise continue to seek approval for its policy on an annual basis. Substantial implementation of a policy would usually be considered to mean that the company had invested at least 50% of all the funds available to it.

In order to avoid suspension of its securities from trading, AIM Rule 15 requires an investing company to make an acquisition which constitutes a reverse takeover under AIM Rule 14 or otherwise implement its investing policy to the satisfaction of the Exchange within twelve months of the disposal occurring.

The minimum fundraising requirement of £3m from independent shareholders allows for different treatment under AIM Rules 8 and 15. This fundraising requirement does not apply to investing companies resulting from the sale or discontinuation of their core trading business. As a consequence, we will not necessarily consider an AIM Rule 15 investing company to have implemented its policy if it invests 50% of the cash resources available to it.

In cases where a nomad considers an investing company to have implemented its policy for the purposes of AIM Rule 15, but where it has not completed a reverse takeover, a nomad should seek confirmation from us.

A commitment to invest funds in the future, or a commitment to make certain expenditure, is not considered equivalent to an actual investment in a target company or assets.

Inclusion of Annex XV information in an admission document

Paragraph 4.1 of the Note requires an investing company to disclose the information required by Annex XV of the Prospectus Rules in its AIM admission document. However, we retain the ability to derogate from the full requirements of Annex XV where appropriate. If a nomad considers that certain requirements of Annex XV may not need to be included in an admission document, a submission to AIM Regulation should be made setting out the reasons.

FAQ

Q. We are intending to change our accounting reference date ("ARD") – what do we need to do?

A. In accordance with the guidance to AIM Rules 18 and 19, the nomad should ensure that we are contacted before announcing an amendment to an ARD.

This is to ensure that shareholders continue to receive financial information on a timely basis and that information is also subject to regular independent audits.

As a result of a change in ARD, we may require:

- half-yearly reports and accounts to be notified/ published prior to the standard three and six month deadlines stated under AIM Rules 18 and 19;
- additional half-yearly reports to be notified;
- half-yearly reports to be subject to an accountant's report; and/or
- trading statements to be made by a specified date.

If possible, changes to ARDs should not be made in the period between the end of the financial year and the original expected results publication date.

DEPOSITARY RECEIPTS ('DRs')

Periodically we receive enquiries from AIM companies, via their nomads, that are seeking to establish a market for their shares via DRs, with the DRs being traded off-exchange, on an OTC basis.

Although the DRs will not be admitted to AIM, we may seek to restrict the percentage of AIM securities represented by the DRs to no more than 25%. This reflects the potential lack of visibility on the underlying trading.

More generally, DRs will only be considered appropriate for admission to AIM where the AIM company is incorporated in a jurisdiction which prohibits, or unduly restricts, the offering or admission of its securities outside of that country.

INVESTIGATIONS & ENFORCEMENT UPDATE

AIM Regulation has previously published details of its disciplinary actions via AIM Disciplinary Notices. This will remain the case in respect of any disciplinary actions resulting in a public censure but private disciplinary actions will be published via Inside AIM going forward.

The Exchange takes public action in the most serious cases, generally involving significant market impact. Private action is taken in other cases, which enables disciplinary action to be concluded in an effective and timely manner.

The purpose of publishing details of these private actions is to ensure that nomads understand our approach to the issues raised. We hope this provides a useful educational tool for both nomads and AIM companies.

DISCIPLINARY ACTIONS

In the twelve months to 30 October 2009, six AIM companies and two nomads have been privately censured and fined a total of £200,000 by the AIM Executive Panel. This is in addition to the public censures and/or fines imposed on Minmet plc (4/12/08), Astaire Securities plc (22/06/09), Regal Petroleum plc (17/11/09) and Environmental Recycling Technologies plc (23/11/09).

Our disciplinary actions against the six AIM companies all involved breaches of AIM Rules 10, 11 and/or 31, including delays in notifying price sensitive information and failure to liaise appropriately with the company's nomad. The fines imposed on those AIM companies ranged from £10,000 to £25,000.

AIM Regulation's disciplinary action against one of the nomads concerned a failure to implement appropriate systems, procedures and controls for the purpose of advising and guiding AIM companies, in respect of which a private censure and fine of £100,000 was imposed. In the other nomad disciplinary action, the nomad had failed to advise an AIM company appropriately in relation to its announcements and was privately censured and fined £15,000.

FAQ

Q. An AIM company has released its preliminary results via an RIS. At what stage should the AIM Rule 20 notification be released?

A. Whenever any document is sent by an AIM company to its shareholders, including the company's annual audited accounts, the AIM company is obliged to release the AIM Rule 20 announcement via an RIS at the same time. A copy of the document should also be placed on its website without delay.

This announcement can be combined with another disclosure that is also scheduled for release. However, the release of a preliminary announcement does not remove the need for an AIM Rule 20 announcement.

Given that electronic versions of annual audited accounts are available via a company's website, we no longer require electronic versions of annual audited accounts to be sent to us.

Actions against AIM companies have highlighted the following issues:

- In one recent disciplinary action, an AIM company's business was materially underperforming and its profit expectations for the year were significantly short of both the company's internal expectations and market expectations. In those circumstances, it is not permissible for a company to delay updating the market based on the possibility that the year-end figures may be affected by possible accounting or tax changes, or one-off exceptional items.

- In one case, two directors were aware of a material trading under performance in the AIM company's business, of which the rest of the board was unaware. There was a material delay in releasing this information to the market in accordance with AIM Rule 11. This case illustrates that, in appropriate circumstances, AIM Regulation will hold AIM companies responsible for the individual, as well as collective, actions of its directors.

- In another case, an AIM company announced that it had raised funds via a placing and wrongly implied that the majority of the funds would be applied for a particular purpose. AIM companies should ensure that fundraising announcements accurately convey the purpose for which the funds are raised and update the market as to any material change in their use.

- In one disciplinary action, following significant underperformance in Q1 of the financial year the AIM company breached its banking covenants. The company's management did not make an announcement on the basis that they believed the full year results would not be materially short of market expectations. However, given the circumstances of this case, the above events were considered price sensitive and the company was under an obligation to update the market and to provide it with the opportunity to assess the reasonableness of its belief in meeting full year expectations.

- During a number of disciplinary actions it has been suggested that a new development requiring notification under AIM Rule 11 would only be notifiable if it falls specifically within one or more of the four bullet points in that rule. In practice, we consider that any new development which is likely to lead to a substantial movement in the company's share will fall within one or more of the bullet points in AIM Rule 11, and therefore a narrow interpretation of the rule should be avoided.

Actions against nomads have highlighted that a nomad should take reasonable care to ensure:

- that its AIM clients appropriately update the market on or before the expiry of previously notified deadlines, especially in the context of operational deadlines regarding the company's core business. Any failure by an AIM company to update the market in these circumstances may constitute a breach of AIM Rule 11 depending on the materiality of the deadline. In any event we consider that best practice would be to update any deadlines previously announced by the AIM company to avoid uncertainty in the market.

- that an AIM company's management is appropriately challenged on the contents of announcements, especially where the nomad has information indicating that the announcement may be inaccurate or incomplete; and

- that, if acting as nomad and broker to an AIM company, the firm's nomad function is fully involved in the firm's relationship with that company and does not rely inappropriately on the broker function. In particular, the nomad should have in place sufficient internal systems and controls to ensure that any material information relating to the AIM company is provided to, and any consequent advice on the AIM Rules is given or reviewed by, an appropriately qualified person within the nomad function. The nomad should also ensure that its AIM company clients understand the different functions within the firm and who is the appropriate contact for AIM Rule issues.

AIM MARKET POLICY UPDATE

AIM VCT LOBBYING

The Exchange has been lobbying for two key recommendations to help boost SME access to finance via the VCT scheme. We are calling for a relaxation of the VCT investment criteria and for VCT participation in secondary market trading of quoted securities. Specifically:

- increasing investment criteria to qualifying companies with gross assets of £25m instead of £7m and 250 employees instead of 50 employees increases the reach of the VCT scheme; and

- allowing VCTs to buy shares on market to stimulate liquidity in qualifying AIM companies.

These changes, combined with the package of measures, such as PSQ Analytics, changes to the tariffs for market makers, and the pilot programme of regional roadshows, are all designed to help improve liquidity of AIM securities.

CURRENT CONSULTATIONS

Response to clarification of MiFID level 1 and 2

The Exchange has called for clarification that shares admitted to MTFs, including AIM, should be deemed non-complex as there is nothing inherently more complex about AIM shares than shares admitted to a regulated market.

Changes to the Prospectus Directive

Following the consultation on PD earlier this year, the EU Commission's proposals for change were released in September and are currently being discussed at the European Parliament level.

The Commission recognises the need to alleviate the burden of the PD on smallller companies. The proposals recommend that a "proportionate disclosure regime" should apply to smaller companies on regulated markets. They also recommend that the proportionate regime should apply to rights issues by all companies already admitted to trading on a regulated market.

We are actively lobbying to influence the proposals. We believe that any relaxations to the PD for smaller companies should be extended to issuers on growth markets like AIM. If you would like to provide comments or input into this process, please contact Umerah Akram at uakram@londonstockexchange.com.

Link to our response to PD consultation – March 2009: http://www.londonstockexchange.com/about-the-exchange/regulatory/review-directive.pdf

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Feedback

We would welcome any feedback on this edition of Inside AIM and any suggestions for issues that you would like us to address in future editions.

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