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Checklist supplement for investment companies and illustrative financial statements : a financial accounting and reporting practice aid, April 1990 edition

American Institute of Certified Public Accountants. Technical Information Division

Neil Selden

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April 1990 Edition

**Checklist Supplement for
Investment Companies and
Illustrative Financial Statements**
A FINANCIAL ACCOUNTING AND REPORTING
PRACTICE AID

To be used in conjunction with *Disclosure Checklists
and Illustrative Financial Statements for Corporations*

Edited by:

Neil Selden, CPA
Technical Manager
Technical Information Division

The Disclosure Supplement and Illustrative Financial Statements for Investment Companies have not been approved, disapproved, or otherwise acted upon by any senior technical committees of the American Institute of Certified Public Accountants, or the Financial Accounting Standards Board and have no official or authoritative status.

AICPA

American Institute of Certified Public Accountants

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CHECKLIST SUPPLEMENT FOR INVESTMENT COMPANIES
AND ILLUSTRATIVE FINANCIAL STATEMENTS

The checklist and illustrative financial statements included in this booklet have been developed as a nonauthoritative technical practice aid. Readers should be aware of the following:

- o The checklist and illustrative financial statements are to be used in conjunction with the "Disclosure Checklists and Illustrative Financial Statements for Corporations," and have been updated to include relevant FASB Statements, Accounting Principles Board Opinions and AICPA Statements of Position. In addition, suggested guidance has been provided from various accounting textbooks where no specific authoritative literature exists. The checklist and illustrative financial statements should be modified, as appropriate, for subsequent pronouncements. To determine the applicability of a pronouncement, its effective date should be considered.
- o The checklist and illustrative financial statements are a "tool" and in no way represent official positions or pronouncements of the AICPA.
- o The checklist and illustrative financial statements should be used by or under the supervision of persons having adequate technical training and proficiency in the application of generally accepted accounting principles and generally accepted auditing standards.
- o The checklist and illustrative financial statements do not represent minimum requirements and do not purport to be all-inclusive. The referenced standards should be reviewed if clarification is desired as to whether the disclosures indicated are required or suggested and to what extent each disclosure is relevant to the statements.

Users of this checklist and illustrative financial statements are urged to refer directly to applicable authoritative pronouncements when appropriate. If you have further questions, call the AICPA Technical Hotline (see back cover).

John Graves
Director
Technical Services

NOTICE

This checklist is updated through FASB Statement No. 104. At the time of this checklist's publication the FASB was in the final stages of issuing a Statement of Financial Accounting Standards that would require all entities to disclose information about (1) financial instruments with off-balance-sheet risk and (2) financial instruments with concentrations of credit risk. Those disclosures would be required for financial statements issued for fiscal years ending after June 15, 1990, and will be reflected in Section _____ of the AICPA Financial Statement Preparation Manual, which will be mailed to subscribers before June 1990.

CHECKLIST SUPPLEMENT FOR INVESTMENT COMPANIES
AND ILLUSTRATIVE FINANCIAL STATEMENTS

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Introduction

Investment companies generally are companies that pool shareholders' funds and invest the proceeds for the benefits of shareholders under the supervision of professional investment management. The investments generally are in securities that are intended to meet the investment objectives of the entity. The entity distributes the net income and realized net gains to its shareholders.

The industry is subject to extensive governmental regulation by the Securities and Exchange Commission ("SEC"). The industry also is the subject of special tax treatment. The investment company industry usually is categorized by the type of security or the investment objective.

There are many types of investment companies: management investment companies, unit investment trusts, collective trust funds, investment partnerships, certain separate accounts of life insurance companies, and offshore funds. Management investment companies are further divided into many sub-classifications, the most predominant of which is open-end funds, also called mutual funds. There also are closed-end funds and Small Business Investment Companies.

This checklist has been designed primarily for auditors of mutual funds and closed-end investment companies that register with the SEC under the Investment Company Act of 1940. However, this checklist generally would apply to all types of investment companies.

Investment companies covered by this checklist are required to report their investment assets at value and have the following attributes: (not applicable to real estate investment trusts)

- a. Investment activity - The primary activity is the investment in securities of non-affiliates or entities not under common management for current income, appreciation or both.
- b. Unit ownership - Ownership in the investment company is evidenced by units of investments, such as shares of stock or partnership interests to which proportionate shares of net assets can be attributed.
- c. Pooling of funds - The funds of the owners are pooled to avail owners of professional investment management.
- d. Reporting entity - The investment company is the primary reporting entity.

The major accounting and auditing literature and applicable regulations for investment companies are as follows:

- a. Audit and Accounting Guide - AICPA - Audits of Investment Companies (Third Edition, Revised)
- b. SOP 89-2 - Reports on Audited Financial Statements of Investment Companies
- c. Article 6 of Regulation S-X of the Securities and Exchange Commission
- d. The Securities Act of 1933
- e. Investment Company Act of 1940

Checklist Questionnaire For Investment Companies

- .01 This checklist has been developed by the staff of the Technical Information Division of the AICPA as a nonauthoritative practice aid and is to be used in conjunction with Section 2000 of the "Disclosure Checklist for Corporations".
- .02 The form and content of the investment companies financial statements required in SEC filings are governed by Regulation S-X Article 6, which deals specifically with investment companies. (SBIC's are covered in article 5)
- .03 Explanation of references:
- ICG = AICPA Audit and Accounting Guide, Audits of Investment Companies
- Reg S-K = Securities and Exchange Commission Regulation S-K
- Reg S-X = Securities and Exchange Commission Regulation S-X
- .04 Checklist Questionnaire

General

A. Financial Statements Presented

- | 1. Are the following Financial Statements Presented?
[ICG5.1] | <u>Yes</u> | <u>No</u> | <u>N/A</u> |
|---|------------|-----------|------------|
| a. Statement of assets and liabilities or a statement of net assets as of the close of the latest period? | ___ | ___ | ___ |
| (1) Does it include a detailed list of investment in securities? | ___ | ___ | ___ |
| (2) Covered call options written? | ___ | ___ | ___ |
| (3) Securities sold short? | ___ | ___ | ___ |
| (4) Other investments? | ___ | ___ | ___ |
| b. Statement of operations for the latest period? | ___ | ___ | ___ |
| c. Statement of changes in net assets for the latest two years? | ___ | ___ | ___ |

	<u>Yes</u>	<u>No</u>	<u>N/A</u>
d. Selected per share data and ratios for the latest five years? [ICG5.1]	—	—	—
 B. Reporting Financial Position			
1. Is a statement of net assets omitted because less than 95% of total assets is invested in securities of non-affiliated issuers? (ICG5.5) (Reg. S-X)	—	—	—
2. If a statement of assets and liabilities is used, does it list assets and liabilities in sufficient detail, and an amount for net assets? (ICG5.6)	—	—	—
3. Does the statement of net assets present a detailed list of portfolio securities and a net amount for all other assets and liabilities? (ICG5.7)	—	—	—

Statement of Assets and Liabilities

A. Assets

1. Investments

a. Are investments in securities the first item in the asset section? (ICG5.9)	—	—	—
b. Are securities reported at value with acquisition cost shown parenthetically by major classification of securities? (ICG5.10)	—	—	—
c. Are investments in foreign securities reported at value by converting their foreign currency value into U.S. dollars using current exchange rates? (ICG5.10)	—	—	—
d. If a statement of assets and liabilities is used, are individual securities held by the fund listed in the statement or in an accompanying list			

	<u>Yes</u>	<u>No</u>	<u>N/A</u>
by major classifications of the investments in the portfolio? (ICG5.10)	—	—	—
e. Are significant investments in foreign securities disclosed and presented separately in a representative grouping? (ICG5.10)	—	—	—
f. Are securities arranged in the most meaningful manner within each classification by industry or group with disclosure of the percentage of assets in each group? (ICG5.10)	—	—	—
g. Does the portfolio listing indicate the number of shares or principal amount and value of each security issue? (ICG5.11)	—	—	—
h. Are short-term investments summarized by issuers (other than money market mutual funds who should present in detail) disclosing their ranges of interest rates and maturity dates? (ICG5.11)	—	—	—
i. Is specific disclosure made of investments in restricted securities non-income producing, affiliated companies and securities subject to call options? (ICG5.11)	—	—	—
 2. Cash			
a. Is cash on hand and demand deposits included under the general caption, cash?	—	—	—
b. Are foreign currencies, if material, disclosed separately?	—	—	—
c. Are time deposits and other funds subject to withdrawal presented separately with disclosure of applicable interest rates and maturity dates? (ICG5.12)	—	—	—

	<u>Yes</u>	<u>No</u>	<u>N/A</u>
3. Receivables			
a. Are the following receivables listed separately?			
(1) Dividends and interest?	___	___	___
(2) Investment securities sold?	___	___	___
(3) Capital stock sold?	___	___	___
(4) Repurchase agreements including accrual interest? (ICG2.75)	___	___	___
(5) Other accounts receivable such as receivables from related parties or expense reimbursements from affiliates? (ICG5.13)	___	___	___
4. Other Assets			
a. Do other assets include items such as deferred organization expense, prepaid taxes, and furniture and fixtures with only significant items separately disclosed? (ICG5.14)	___	___	___
B. Liabilities			
1. Accounts Payable			
a. Have accounts payable been listed separately for investment securities purchased and for capital stock re-acquired? (ICG5.16)	___	___	___
b. Have call or put options written, future contracts sold, and securities sold short been disclosed? (ICG5.17)	___	___	___
(1) Are call options written and securities sold short at the end of the period presented separately?	___	___	___

	<u>Yes</u>	<u>No</u>	<u>N/A</u>
(2) Does the information for covered call options include the number of shares subject to call for each option written, the value of each option, stock price and exercise date?	_____	_____	_____
(3) Does the information presented for other securities sold short, other options written and futures contracts sold include data about quantities, value and proceeds?	_____	_____	_____
 2. Taxes			
a. Does the entity meet the provisions of subchapter M of the Internal Revenue Code and distribute all taxable income and realized gains? (ICG1.37)	_____	_____	_____
b. Are there any non-distributed realized taxable long-term gains for which election has been made to pay the federal income tax for their shareholders? (ICG1.37)	_____	_____	_____
c. Are state, local and foreign taxes, current and deferred, reported on the accrual basis? Are such taxes recorded on unrealized appreciation or depreciation of investments? (ICG1.38)	_____	_____	_____
d. If the entity does not qualify under Subchapter M of the Internal Revenue Code, has a provision for deferred federal taxes on unrealized appreciation or depreciation been recorded in addition to federal income taxes on net investment income and realized gains or losses? (ICG1.39)	_____	_____	_____
 3. Accrued Liabilities			
a. Are accounts payable separately reported for securities purchased and reported stock reacquired?	_____	_____	_____

	<u>Yes</u>	<u>No</u>	<u>N/A</u>
b. Are call options written, securities sold short and futures contracts sold presented separately including details such as quantities, values and proceeds? (ICG5.1)	—	—	—
c. Are accrued liabilities disclosed including taxes, management fees, interest, compensation expenses, and other expenses with separate disclosure of related party amounts? (ICG5.18)	—	—	—
d. Are notes payable to banks and to others and other funded debt reported separately with separate disclosure of related party amounts? (ICG5.19)	—	—	—
e. Do other liabilities include amounts payable to affiliates for collateral on return of securities loaned, for deferred income, and for dividends? (ICG5.20)	—	—	—
f. Are reverse repurchase agreements presented?	—	—	—
4. Net Assets			
a. If not required to be disclosed separately in the statement of assets and liabilities, does the statement or notes disclose the following? (ICG5.21)			
(1) Units of capital, including the title of each class, the number authorized and outstanding and the dollar amount?	—	—	—
(2) Paid-in capital which includes the net proceeds received on sale of capital shares less the cost of reacquired shares, adjusted for amounts apportioned to the equalization accounts, if that accounting procedure is followed?	—	—	—

	<u>Yes</u>	<u>No</u>	<u>N/A</u>
(3) Undistributed investment income, which includes cumulative investment income or loss, equalization apportionments, if necessary, less dividends from net investment income (amounts at the end of the periods presented are normally disclosed in the statement of changes in net assets)?	_____	_____	_____
(4) Cumulative amounts of gains and losses realized from security transactions, net of actual or deemed dividends to shareholders?	_____	_____	_____
(5) Unrealized appreciation or depreciation of investments (value of securities owned at the end of the period compared to acquisition price less applicable deferred income taxes on unrealized appreciation)?	_____	_____	_____
b. As to tax-managed funds:			
(1) For tax-managed funds, have the undistributed investment income, realized gains and losses, and changes in unrealized appreciation or depreciation been combined? (ICG5.22)	_____	_____	_____
(2) Have current and accrued taxes been recorded? (ICG4.76)	_____	_____	_____
c. Net asset value per share? (ICG5.23)	_____	_____	_____

Statement of Operations

A. Income

1. Is dividend income recorded as of the ex-dividend date? (ICG5.25)	_____	_____	_____
2. Are dividends from affiliates and controlled companies reported and disclosed separately? (ICG5.25)	_____	_____	_____

	<u>Yes</u>	<u>No</u>	<u>N/A</u>
3. Is interest income generally accrued on all debt securities? (ICG5.26)	—	—	—
4. Has the interest received on bonds that were in default or that were delinquent in the payment of interest when acquired been accounted for as:			
a. Interest income for the amount earned from the date of acquisition through the current period, or	—	—	—
b. A reduction in the cost of the investment in terms of the amount relative to arrearages at the date of the acquisition? (ICG2.108, ICG5.26)	—	—	—
5. Has income from securities loaned and from miscellaneous sources been included as other income? (ICG5.27)	—	—	—

B. Expenses

1. Are the following expenses reported separately? (ICG5.28)			
a. Investment advisory (management) fees (or compensation)?	—	—	—
b. Shareholder service costs including fees and expenses for the transfer agent and distribution expenses?	—	—	—
c. Dividend disbursing agent fees?	—	—	—
d. Custodian fees?	—	—	—
e. Reports to shareholders?	—	—	—
f. Federal income taxes?	—	—	—
g. Other taxes?	—	—	—
h. Interest?	—	—	—
i. Dividends on securities sold short?	—	—	—
j. Professional fees?	—	—	—

	<u>Yes</u>	<u>No</u>	<u>N/A</u>
k. Director's fees?	—	—	—
l. Registration fees and expenses?	—	—	—
2. Based on SEC requirements, are expenses that represent 5% or more of total expenses disclosed? (ICG5.28)	—	—	—
3. Are amounts paid to affiliates or related parties disclosed in accordance with FASB Statement No. 57? Does the disclosure include the basis for determining management, advisory fees, and other amounts paid to related parties (including expense reimbursement)? (ICG5.29)	—	—	—
4. Are sales and payments to affiliates under a 12b-1 distribution plan disclosed? (ICG5.29)	—	—	—
5. Is the excess of investment income over total expenses shown as investment income-net? (ICG5.30)	—	—	—
C. Realized Gains or Losses on Investments			
1. Are significant net realized gains or losses disclosed by major types of security transactions such as long transactions, short sale transactions, and covered call option transactions? (ICG5.31)	—	—	—
2. Are net gains or losses from sales or other disposals reported net of brokerage commissions? (ICG5.31)	—	—	—
3. Are income tax provisions charged against realized gains disclosed separately? (ICG5.31)	—	—	—
4. Are gains arising from in-kind redemptions disclosed? (ICG5.31)	—	—	—

	<u>Yes</u>	<u>No</u>	<u>N/A</u>
5. Has disclosure been made of the proceeds from sales and the cost of securities bought separately for U.S. Government obligations and other than U.S. Government Securities? (ICG5.32)	---	---	---
6. Has consideration been given to separate disclosures of the proceeds and costs pertaining to common stocks, preferred and bonds? (ICG5.32)	---	---	---
7. For a money market fund, have net realized gains or losses (usually insignificant), been combined with interest income? (ICG5.32)	---	---	---
D. Changes in Unrealized Appreciation or Depreciation of Investments			
1. Have changes in unrealized appreciation or depreciation of investments together with related disclosure of deferred taxes, if any, been reported in the statement of operations? (ICG5.33)	---	---	---
E. Net Gain or Loss on Investments			
1. Has the sum of realized and unrealized net gain or loss on investments been presented in the statement of operations as a net gain or loss on investments?	---	---	---
2. Are the significant effects of futures or options trading activities, disclosed separately? (ICG5.34)	---	---	---
F. Net Increase or Decrease in Net Assets Resulting from Operations			
1. Is the sum of investment income-net and net gain or loss on investment, shown as a net increase or decrease in net assets resulting from operations? (ICG5.35)	---	---	---

	<u>Yes</u>	<u>No</u>	<u>N/A</u>
Statement of Changes in Net Assets			
A. Does the increase or decrease in net assets include the following categories?			
1. Operations			
a. Net investment income or loss?	___	___	___
b. Net realized gains and losses?	___	___	___
c. Changes in unrealized gains or losses on investments?	___	___	___
2. If equalization accounting is followed, is undistributed investment income included in the price of capital shares issued or reacquired?	___	___	___
3. Distributions to shareholders			
a. Distribution from undistributed investment income?	___	___	___
b. Distribution from undistributed realized gains from investment transaction.	___	___	___
c. Distributions from other sources (e.g., return of capital)?	___	___	___
d. Has per share amounts of distributions been included? (ICG5.37)	___	___	___
B. Has disclosure of declared but undistributed amounts been disclosed in the notes? (ICG5.37)	___	___	___
C. Have the following components of capital share transactions been disclosed on the face of this statement or in the notes as follows:			
1. The number and value of shares sold?	___	___	___
2. The number and value of shares issued in reinvestment of distributions?	___	___	___

	<u>Yes</u>	<u>No</u>	<u>N/A</u>
3. The number and value of shares reacquired?	___	___	___
4. The net change? (ICG5.37)	___	___	___
D. Have net assets been disclosed at the beginning and end of the year including an indication (usually parenthetically) of undistributed investment income? (This amount should agree with the comparable amount in the statement of assets and liabilities) (ICG5.37)	___	___	___

Supplementary Information

A. Does the information include selected per share data and ratios for a period of at least five years? (ICG5.38)	___	___	___
B. Are per share amounts presented based on a share outstanding throughout the period? (ICG5.38)	___	___	___
C. Has the following per share information been presented? (ICG5.39)	___	___	___
1. Investment income?	___	___	___
2. Expenses?	___	___	___
3. Income taxes and interest on borrowed funds, if material?	___	___	___
4. Per share investment income?	___	___	___
5. Distributions from undistributed investment income, undistributed net realized gain through investment transactions, and from other sources?	___	___	___
6. Realized and unrealized gains and losses per share that are balancing amounts necessary to reconcile the changes in net asset value per share with other per share information presented?	___	___	___

	<u>Yes</u>	<u>No</u>	<u>N/A</u>
7. The increase or decrease in net asset value per share?	___	___	___
8. The net asset value at the beginning and end of each period? (ICG5.39)	___	___	___
D. Are the ratios of investment of investment income-net and expenses to average net assets presented? (ICG5.40)	___	___	___
E. Have additional ratios such as turnover rates, number of shares outstanding at the end of each period and the total return or yield information for money market investment companies, been presented? (ICG5.40)	___	___	___
F. Have the per share amounts of distributions from undistributed net investment income of municipal bond funds, been stated separately for amounts applicable to taxable and tax-exempt dividends? (ICG5.41)	___	___	___

Interim Financial Statements

A. Is quarterly financial information complete and based upon GAAP in a manner that conforms to principles used in preparing annual financial statements? (ICG5.42)	___	___	___
B. Does the statement of changes in net assets present information on the latest interim period and the preceding fiscal year? (ICG5.43)	___	___	___
C. Has unaudited interim financial data been marked accordingly?	___	___	___
D. Has data summarized in condensed form been labeled as unaudited?	___	___	___
E. If the independent accountant has not performed an audit or review, but is identified in the interim report, has he or she insisted the reference be deleted or that a disclaimer of opinion be included? (ICG5.44)	___	___	___

Yes No N/A

SEC Compliance Disclosures Per Regulations S-X

- | | | | | |
|----|---|-----|-----|-----|
| A. | Has the total cost, for federal income tax purposes, of the portfolio been disclosed? (S-X Rule 12-2, Note 8) | ___ | ___ | ___ |
| B. | Have the additional disclosures been made as required by: | | | |
| 1. | S-X Rule 12-22 [note 2] pertaining to collateral for repurchase agreements? | ___ | ___ | ___ |
| 2. | S-X Rule of 4-08(m) pertaining to carrying amounts of repurchase or reverse repurchase which exceed 10% of total assets? | ___ | ___ | ___ |
| 3. | Disclosure of the average amount of borrowings outstanding during the period, the weighted average interest rate, and the maximum amount of debt outstanding during the period, according to rule 6-.04.13(b), referring to rules 5.02.19(b) and 5.02.22(b), of S-X. | ___ | ___ | ___ |
| 4. | The additional disclosure about restricted securities required by the SEC's Codification of Financial Reporting Policies, section 404, and rule 12-12 (note 6) of S-X. | ___ | ___ | ___ |
| 5. | S-X Rule 12-12 (note 8) dealing with gross unrealized appreciation for all securities in which there is an excess of value over tax cost and gross unrealized depreciation for all securities in which there is an excess of value over tax cost and gross unrealized depreciation for all securities in which there is an excess of tax cost over value, as well as net unrealized appreciation or depreciation. | ___ | ___ | ___ |
| 6. | Disclosure of the elements of net assets as required in regulation 210.6-.04.16, 210.6-04.17 and 210.6-04.18 as part of the statement of assets and liabilities rather than in the notes to the financial statements. | ___ | ___ | ___ |
| 7. | Disclosure of non-income producing securities as required by S-X rule 12-12 (note 5). | ___ | ___ | ___ |

	<u>Yes</u>	<u>No</u>	<u>N/A</u>
C. Are additional disclosures made about restricted securities, in accordance with the SEC's Codification of Financial Reporting Policies, section 404 and rule 12-12 (Note 6)?	_____	_____	_____
D. Has the gross unrealized appreciation for all securities been disclosed in the following areas:			
1. Excess of value over tax cost?	_____	_____	_____
2. Gross unrealized depreciation for all securities in which there is an excess of tax cost over value?	_____	_____	_____
3. Net unrealized appreciation or depreciation for all securities in which there is an excess of tax cost over value?	_____	_____	_____
4. Aggregate cost of securities for federal income tax purposes?	_____	_____	_____
E. If a statement of net assets was presented in place of a statement of assets and liabilities, is 95% of the amount of the investment company's total assets represented by investments in securities of unaffiliated issuers (S-X article 6)?	_____	_____	_____

Illustrative Financial Statements

Independent Auditor's Report

To the Shareholders and Board of Directors:
XYZ Management Investment Company

We have audited the accompanying statement of assets and liabilities of XYZ Management Investment Company (or Statement of Net Assets), including the schedule of investments in securities, covered call options written, and securities sold short as of December 31, 19X4, 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 the selected per share data and ratios for each of the five years in the period then ended. These financial statements and selected per share data and ratios are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and per share data and ratios based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements and per share data and ratios are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. Our procedures included confirmation of securities owned as of December 31, 19X4 by correspondence with the custodian and brokers. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements and selected per share data and ratios referred to above present fairly, in all material respects, the financial position of XYZ Management Investment Company as of December 31, 19X4, 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 selected per share data and ratios for each of the five years in the period then ended, in conformity with generally accepted accounting principles.

[Signature]
[City]
[Date]

XYZ Management Investment Company
Statement of Assets and Liabilities
December 31, 19X4
(000's omitted)

Assets	
Investments in securities, at value—identified cost \$19,294	\$21,721
Cash	199
Deposits with brokers for securities sold short	1,555
Receivables	
Dividends and interest	46
Investment securities sold	24
Capital stock sold	54
Other assets	<u>26</u>
Total assets	<u>23,625</u>
 Liabilities	
Covered call options written, at value—premiums received \$110	230
Securities sold short at value—proceeds \$1,535	1,673
Demand loan payable to bank (Note 5)	2,000
Payable upon return of securities loaned (Note 9)	620
Payables	
Investment securities purchased	52
Capital stock reacquired	8
Other	4
Accrued taxes	8
Distribution payable	<u>168</u>
Total liabilities	<u>4,763</u>
 Net Assets	
Net assets (equivalent to \$4.47 per share based on 4,216 shares of capital stock outstanding) (Note 6)	<u>\$18,862</u>

The accompanying notes are an integral part of these financial statements.

Note: A statement of assets and liabilities is an alternative presentation to a statement of net assets. The reader should be aware, however, that SEC rules do not always consider the two statement formats to be alternative presentation. (ICG5.47)

XYZ Management Investment Company
Schedule of Investments in Securities
December 31, 19X4
(000's omitted)

[Note: Securities may be arranged by industry groupings or other groupings (showing percentage of total portfolio or of net assets invested in each grouping) that the company believes are most meaningful to users. The basis of the computation of percentages shown (which in this illustration is based on the ratio of the specific category of securities to the total portfolio owned) should be disclosed.]

	Principal Amount or Shares	Value
Common Stocks—54%		
Consumers' durable goods—5%		
Allied Manufacturing Corporation	25	\$ 620
Baker Industries, Inc.	15	150
Etc. (other common stocks)		316
Consumers' nondurable goods—2%		
Amalgamated Buggy Whips, Inc. (Note 2)	10	280
Etc. (Other common stocks)		155
Service industries—4%		
Service Company, Inc.	10	465
Etc. (other common stocks)		404
Etc. (other industry groupings)—43%		<u>9,351</u>
Total common stocks (cost \$10,294)		<u>11,741</u>
Convertible bonds—25%		
American Retailing Inc.—5.5% debentures due 19XX	\$500	525
Etc. (other convertible bonds)		<u>4,875</u>
Total convertible securities (cost \$4,400)		<u>5,400</u>
U.S. government obligations—16%		
U.S. Treasury 6% notes due 20XX	\$500	\$ 490
Etc. (other long-term government obligations)		<u>2,985</u>
Total U.S. government obligations (cost \$3,500)		<u>3,475</u>
Short-term notes—3%		
Commercial Paper, Inc. due 2/5/X5	\$500	505
U.S. Treasury bills, due 1/20/X5	\$100	100
Total short-term notes (cost \$600)		<u>605</u>
Repurchase agreements collateralized by U.S. government obligations—2%		
Money Center Bank of Large City, 11% due 1/3/X5 (cost \$500)	\$500	500
Total—100% (cost \$19,294)		<u><u>\$21,721</u></u>

The accompanying notes are an integral part of these financial statements.

XYZ Management Investment Company
Statement of Operations
Year Ended December 31, 19X4
(000's omitted)

Investment income

Income		
Dividends	\$742	
Interest	<u>259</u>	
Total income		\$ 1,001

Expenses

Investment advisory fee (Note 8)	90	
Interest	55	
Professional fees (Note 8)	29	
Custodian and transfer agent fees	12	
Distribution expenses (Note 8)	4	
State and local taxes other than income taxes	15	
Directors' fees	12	
Dividends on securities sold short	<u>9</u>	
Total expenses		<u>226</u>
Investment income—net		<u>775</u>

Realized and unrealized gain (loss) on investments (Note 7)

Net realized gain on investments	1,089
Change in unrealized appreciation of investments for the year	<u>(1,649)</u>
Net loss on investments	<u>(560)</u>
 Net increase in net assets resulting from operations	 <u><u>\$ 215</u></u>

The accompanying notes are an integral part of these financial statements.

XYZ Management Investment Company
Statement of Net Assets
December 31, 19X4
(000's omitted)

	<u>Shares or Principal Amount</u>	<u>Value</u>
Assets		
Investments in securities—115% of net assets		
[Note: Securities may be arranged by industry or other groupings (showing the percentage of total portfolio or of net assets invested in each grouping) that the company believes will be most meaningful to the user.]		
Common stocks—62%		
Consumers' durable goods—6%		
Allied Manufacturing Corporation	25	\$ 620
Baker Industries, Inc.	15	150
Etc. (other common stocks)		316
Consumers' nondurable goods—2%		
Amalgamated Buggy Whips, Inc. (Note 2)	10	280
Etc. (other common stocks)		155
Service industries—5%		
Service Company Inc.	10	465
Etc. (other common stocks)		404
Etc. (other industry groupings)—49%		<u>9,351</u>
Total common stocks (cost \$10,294)		<u>11,741</u>
Convertible bonds—29%		
American Retailing Inc.—5.5% debentures due 19XX	\$500	525
Etc. (other convertible bonds)		<u>4,875</u>
Total convertible bonds (cost \$4,400)		5,400
U.S. government obligations—18%		
U.S. Treasury—6% notes due 20XX	\$500	490
Etc. (other long-term obligations)		<u>2,985</u>
Total U.S. government obligations (cost \$3,500)		<u>3,475</u>
Short-term notes—3%		
Commercial Paper, Inc. due 2/5/X5	\$500	505
U.S. Treasury bills, 1/20/X5	\$100	100
Total short-term notes (cost \$600)		<u>605</u>
Repurchase agreement collateralized by U.S. government obligations—3%		
Money Center Bank of Large City—11% due 1/3/X5 (cost \$500)	\$500	500
Total investments in securities (cost \$19,294)		<u>21,721</u>
Other assets—10%		<u>1,904</u>
Total assets		<u><u>23,625</u></u>

	<u>Shares or Principal Amount</u>	<u>Value</u>
Liabilities		
Demand loans payable to bank—10% (Note 5)		2,000
Securities sold short—9%		1,673
Other liabilities—6%		<u>1,090</u>
Total liabilities		<u>4,763</u>
Net Assets		
Net assets (equivalent to \$4.47 per share based on 4,216 shares of capital stock outstanding) (Note 6)		<u>\$18,862</u>

The accompanying notes are an integral part of these financial statements.

Note: A statement of assets and liabilities is an alternative presentation to a statement of net assets. The reader should be aware, however, that SEC rules do not always consider the two statement formats to be alternative presentations. (ICG5.47)

XYZ Management Investment Company
Statement of Changes in Net Assets
Years Ended December 31, 19X4 and 19X3

	<u>19X4</u>	<u>19X3</u>
Increase (decrease) in net assets from operations		
Investment income—net	\$ 755	\$ 492
Net realized gain on investments	1,089	1,000
Change in unrealized appreciation	<u>(1,649)</u>	<u>1,551</u>
Net increase in net assets resulting from operations	215	3,043
Net equalization credits	9	6
Distributions to shareholders from—		
Investment income—net	(525)	(350)
Net realized gain on investments	(1,350)	(1,066)
Capital share transactions	<u>2,721</u>	<u>1,749</u>
Total increase	1,070	3,382
Net assets		
Beginning of year	<u>17,792</u>	<u>14,410</u>
End of year (including undistributed investment income of \$639,000 and \$380,000, respectively)	<u>\$18,862</u>	<u>\$17,792</u>

The accompanying notes are an integral part of these financial statements.

**XYZ Management Investment Company
Covered Call Options Written
December 31, 19X4**

<u>Common Stocks/Expiration Date/Exercise Price</u>	<u>Shares Subject to Call</u>	<u>Value</u>
Allied Manufacturing Corporation/July/25	10	\$ 50
Allied Manufacturing Corporation/October/30	5	3
Etc. (other options written)		<u>177</u>
Total (premiums received \$110) (Note 3)		<u><u>\$ 230</u></u>

**XYZ Management Investment Company
Securities Sold Short
December 31, 19X4**

<u>Common Stock</u>	<u>Shares</u>	<u>Value</u>
International Widgets, Inc.	40	\$ 425
Paper Airplane Corporation	25	265
Etc. (other common stocks)		<u>983</u>
Total (proceeds \$1,555)		<u><u>\$1,673</u></u>

The accompanying notes are an integral part of these financial statements.

XYZ Management Investment Company Notes to Financial Statements

The following notes to the financial statements are illustrative only. In some circumstances, the information may be better presented within the financial statements; in other circumstances, information not required by regulation may not be sufficiently material to be disclosed.

1. Significant Accounting Policies

The Company is registered under the Investment Company Act of 1940 as a diversified, open-end management investment company.

Security valuation. Investments in securities traded on a national securities exchange (or reported on the NASDAQ national market) are stated at the last reported sales price on the day of valuation; other securities traded in the over-the-counter market and listed securities for which no sale was reported on that date are stated at the last quoted bid price, except for short positions and call options written, for which the last quoted asked price is used. Short-term notes are stated at amortized cost, which is equivalent to value. Restricted securities and other securities for which quotations are not readily available are valued at fair value as determined by the board of directors.

Federal income taxes. The Company's policy is to comply with the requirements of the Internal Revenue Code that are applicable to regulated investment companies and to distribute all its taxable income to its shareholders. Therefore, no federal income tax provision is required.

Equalization. The Company uses the accounting practice of *equalization*, by which a portion of the proceeds from sales and costs of redemption of capital shares, equivalent on a per share basis to the amount of undistributed net investment income on the date of the transactions, is credited or charged to undistributed income. As a result, undistributed net investment income per share is unaffected by sales or redemptions of capital shares.

Distributions to shareholders. Dividends to shareholders are recorded on the ex-dividend date.

Other. The Company follows industry practice and records security transactions on the trade date. Dividend income is recognized on the ex-dividend date, and interest income is recognized on an accrual basis. Discounts and premiums on securities purchased are amortized over the life of the respective securities.

2. Restricted Securities

The investment in 10,000 shares of Amalgamated Buggy Whips, Inc. common stock, the sale of which is restricted, has been valued by the board of directors after considering certain pertinent factors, including the results of operations of Amalgamated since the date of purchase in 19X1 and the sales price of recent private placements in its common stock. There is no quoted market for Amalgamated shares.*

3. Covered Call Options Written

As of December 31, 19X4, portfolio securities valued at \$1,908,000 were held in escrow by the custodian in connection with covered call options written by the Company.

4. Distribution of Shareholders

On January 3, 19X5, a distribution of \$0.20 aggregating \$840,000 was declared from net realized gains from investment transactions (including \$0.02 applicable to short-term gains that are taxable to shareholders as ordinary income dividends) during 19X4. The dividend was paid on January 20, 19X5, to shareholders of record on January 10, 19X5.

As of December 31, 19X4, the Company had available for federal income tax purposes an unused capital loss carryover of approximately \$1,500,000, which will expire in 19X5.**

* If several restricted security investments are held, a general statement on the valuation methods may be given rather than individual descriptions.

** This would be disclosed if the Company has an available capital loss carryover as of December 31, 19X4.

XYZ Management Investment Company Notes to Financial Statements (Continued)

5. Bank Loans

The Company has an unsecured \$3,000,000 bank line of credit; borrowings under this arrangement bear interest at 110 percent of the bank's prime rate. As of December 31, 19X4, the Company was paying interest at 11 percent per year on its outstanding borrowings. No compensating balances are required.

6. Capital Share Transactions

As of December 31, 19X4, there were 25,000,000 shares of \$0.50 par value capital stock authorized and capital paid-in aggregated \$15,184,000.

Transactions in capital stock were as follows:

	Shares		Amount	
	19X4	19X3	19X4	19X3
Shares sold	452,000	329,000	\$2,177,000	\$1,434,000
Shares issued in reinvestment of dividends	<u>222,000</u>	<u>207,000</u>	<u>1,000,000</u>	<u>845,000</u>
	674,000	536,000	3,177,000	2,279,000
Shares redeemed	<u>104,000</u>	<u>121,000</u>	<u>456,000</u>	<u>530,000</u>
Net income	<u><u>570,000</u></u>	<u><u>415,000</u></u>	<u><u>\$2,721,000</u></u>	<u><u>\$1,749,000</u></u>

7. Investment Transactions

Purchases and sales of investment securities (excluding short-term securities) were \$32,000,000 and \$23,300,000, respectively, for common stocks and bonds; purchases and sales of U.S. government obligations were \$3,300,000 and \$2,000,000. Net loss on investments for the year ended December 31, 19X4, was \$560,000. That amount represents the net decrease in value of investments held during the year. The components are as follows:

Long transactions	\$(501,000)
Short sale transactions	(75,000)
Covered call options written	<u>16,000</u>
	<u><u>\$(560,000)</u></u>

As of December 31, 19X4, the unrealized appreciation of securities was \$2,189,000; accumulated undistributed net realized gains on investment transactions totaled \$850,000.

8. Investment Advisory Fees and Other Transactions with Affiliates

The Company pays advisory fees for investment management and advisory services under a management agreement (Agreement) that provides for fees to be computed at an annual rate of 0.5 percent of the Company's average daily net assets. Certain officers and directors of the Company are also officers and directors of the investment adviser. The Agreement provides for an expense reimbursement from the investment adviser if the Company's total expenses, exclusive of taxes, interest on borrowings, dividends on securities sold short, brokerage commissions, and extraordinary expenses, exceed 1.5 percent of the Company's average daily net assets for any full fiscal year. An expense reimbursement was not required for either 19X4 or 19X3. An expense reimbursement of \$0.01 per share was required in 19X0.

The investment adviser also received \$10,000 in 19X4 and \$15,000 in 19X3 from commissions earned on sales of XYZ Management Investment Company capital stock and \$5,000 in 19X4 and \$8,000 in 19X3 from brokerage fees on its executions of purchases and sales of portfolio investments.

During 19X4, the Company incurred legal fees of \$7,000 to Brown and Smith, counsel for the Company. John F. Smith, a partner of the firm, is a director of the Company. MNO Service Company, an affiliate of the investment adviser, received \$4,000 in expense reimbursements for shareholder-related distribution expenses undertaken pursuant to a shareholder-approved plan.

XYZ Management Investment Company
Notes to Financial Statements (Continued)

9. *Portfolio Securities Loaned*

As of December 31, 19X4, the Company loaned common stocks having a value of approximately \$570,000 and received cash collateral of \$620,000 for the loan.

Supplementary Information—Selected Per Share Data and Ratios*

	<u>19X4</u>	<u>19X3</u>	<u>19X2</u>	<u>19X1</u>	<u>19X0</u>
Per Share Data					
Investment income	\$.27	\$.30	\$.24	\$.20	\$.18
Expenses	<u>.06</u>	<u>.10</u>	<u>.05</u>	<u>.03</u>	<u>.03**</u>
Investment income—net	.21	.20	.19	.17	.15
Distributions from investment income net	(.16)	(.16)	(.17)	(.17)	(.15)
Net realized and unrealized gain (loss) on securities	(.12)	.71	.52	(.42)	.48
Distributions from realized gains on securities	<u>(.34)</u>	<u>(.33)</u>	<u>(.24)</u>	<u>(.23)</u>	<u>(.20)</u>
Net increase/decrease in net asset value	(.41)	.42	.30	(.65)	.28
Net asset value:					
Beginning of year	<u>4.88</u>	<u>4.46</u>	<u>4.16</u>	<u>4.81</u>	<u>4.53</u>
End of year	<u>\$4.47</u>	<u>\$4.88</u>	<u>\$4.46</u>	<u>\$4.16</u>	<u>\$4.81</u>
Ratios					
Ratio of expenses to average net assets (%)	1.33	1.31	.99	.82	.84
Ratio of investment income—net to average net assets (%)	4.56	2.82	4.22	5.42	5.10

* Selected data for a share of capital stock outstanding throughout the year.

** See Note 8 of the notes to financial statements.

Editor's note: Form N1-A requires disclosure of the portfolio turnover rate and number of shares at the end of each period in the condensed financial information. (ICG5.40)

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