

Savings From Audit Exemption - Who Will Benefit?

As of January 2004, 69,000 companies with a turnover between £1m and £5.6m will no longer need to have their accounts audited. (Check with your accountant to ensure you are not covered by exceptions to the rule).

Noel Duffy of Duffy Regan & Company explained the requirement for audit arose from the need to protect investors in limited liability companies. He confirmed, "The Government's decision to drop the requirement to audit companies, with low turnovers, stemmed from the Government's desire to cut red tape. After all owner managed businesses should be able to protect their own investments." He went on, "although it appears reasonable the Government has ignored the other groups that have an interest in a company's financial affairs such as banks, creditors and potential buyers of the business.

He adds, "claims by trade and industry secretary Patricia Hewitt that the move will save these firms £94m a year are at odds with a study commissioned by her own department as part of its "evidence-based" approach to policy making." A spokesperson for the DTI says the Government believes 69% of the new companies will seek the exemption.

But the study conducted by Dr. Jill Collis, a senior lecturer in the school of accounting and finance at Kingston University, shows that only 21% of the companies in the £1m-£5.6m turnover band are likely to seek audit exemption. Findings suggest the larger the company, the less likely it is to seek exemption.

In her report, available on DTI's website Collis says: "The fact that so few directors reported any savings from discontinuing the audit implies that it may not have been a significant saving or that it was offset by other charges". Those other charges could include the higher interest rates that companies unable to provide lenders with audited accounts have to pay for borrowing. Peter Rowe, director general of the Institute of Credit Management points out that when the audit exemption threshold was raised from £350,000 to £1m in 2000, some companies that took advantage had their credit rating reduced or cancelled.

Others found that borrowing became more expensive or that managers had to spend extra time providing references because lenders couldn't perform a satisfactory credit check on audited accounts at Companies House. It's perhaps not surprising then that the latest threshold rise has had a mixed reception. Stephen Alambritis of the Federation of Small Businesses says: "We have welcomed the move and we are hopeful that the money saved by not undertaking the statutory audit will be spent with accountants, but on more meaningful financial information for directors."

But Bryan Regan of Duffy Regan, is not convinced: "The move is meant to cut costs but I don't think it will cut much. In order to produce a proper set

of accounts for SME's that comply with the Companies Act and deal with the tax compliance issues, one has to go through the accounting records with a fine tooth comb."

Others are worried that a reduction in auditing could lead to a rise in fraud. The Association of Chartered Accountants point out that 45% of frauds- mostly involving managers manipulating financial records for personal gain are uncovered by external auditors.

Noel Duffy says, "ironically audits have never been so meaningful and predicts that within five years we will return to a system that had really begun to work. Besides providing a check on the numbers, the audit process critically examines whether assets such as stock and debtors are worth the value shown in the accounts. The audit process acts as a reality check and adjusts the accounts accordingly". Directors see a range of benefits from auditing. These include providing a check on accounting records and systems (65% of directors), improving the credibility of financial information (61%), providing assurance to the company's bank (58%) and improving the quality of information (43%). Despite the new exemption, for most £1m plus companies it is likely to be audit as usual.

The above advice is given in good faith. Individual circumstances differ, no action should be taken without regard to these personal circumstances. Accordingly, please consult your professional adviser. If you wish to talk to one of our partners or tax consultants, please do so. The first hour is free and without obligation.