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Our ref DLC/JP

30 December 2011

BIS
Spur 2, 3rd Floor
1 Victoria Street
London
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For the attention of: Rufus Rottenberg

Dear Sirs,

BIS Consultation on audit exemptions

We would like to make the following comments on the government's proposals regarding widening the scope of audit exemption.

Take up of audit exemption

We believe that certain companies – especially owner managed businesses – will take up the audit exemption. Where owners exercise a high level of day to day control and are also possibly engaging external accountants to assist with management accounts, payroll and so on, the year end statutory audit provides little additional assurance to the shareholders.

However, some owner managed and/or SME businesses, especially those with a wider shareholder base, are likely to continue to require some form of independent assurance to satisfy the requirements of other parties, mainly lenders, but in some cases suppliers and indeed non-management shareholders.

In addition, those businesses for which the owners are planning an exit strategy are also likely to continue to require an annual audit to demonstrate appropriate governance to potential buyers; as will those businesses planning to get involved in tendering situations where typically a history of audited accounts can be required.

As to whether lenders will continue to see a role for the traditional audit process to satisfy their ongoing assurance needs remains to be seen.

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Subsidiaries exemption

As to the audit exemption becoming available to subsidiaries provided, among other conditions, that the parent guarantees subsidiary debts, we do not believe this will be taken up widely. In our experience of privately owned group structures, subsidiaries often exist in order that the liabilities of one part of the business can be isolated from others. If the parent guaranteed the debts of a subsidiary, the liability isolation would be removed, defeating the purpose of the subsidiary.

Further, in some group structures, the directors of the parent are not necessarily directors of the subsidiaries, and consequently may still require audits of subsidiaries to provide them with the assurance they need on the stewardship of the other directors.

From the auditor's point of view, the audit of the group accounts will still mean a certain amount of audit work will need to be undertaken on the subsidiary irrespective of the subsidiary's own statutory audit requirements. And if a parent guarantee is in place, the parent auditors will need to undertake sufficient audit work at parent level to satisfy themselves as to unrecorded liabilities which may result from the guarantee; so an individual subsidiary's audit exemption is unlikely to reduce significantly the overall amount of audit work required for the group.

Benefits

As noted above, for those businesses for whom the annual audit provides little additional assurance or who don't need the assurance an audit provides, the audit cost saving will undoubtedly be welcome.

The alignment of the audit exemption criteria with those of the small company regime will reduce confusion. Some businesses do not always realise they require an audit until filing deadlines are imminent, so simplification in this regard will help businesses and auditors alike.

It will also be of benefit to those investment property holding businesses who only require an audit because, as a consequence of having to hold investment properties at valuation, they breach the balance sheet limit for audit exemption.

Impact on firm's business

There may be some loss of audit fee income from existing audit clients, but there may also be an opportunity to pick up audit work where other firms have decided to drop their audit registration. There may also be opportunities to get involved with businesses in a wider range of advisory or other capacities from which we may currently be ethically barred from undertaking.

Some statutory audits may be replaced by different assurance assignments.

Overall, the simplification in audit exemption criteria will be helpful. We are not convinced that the availability of the audit exemption to a larger group will result in a considerable reduction in either audits conducted or costs for businesses, but many businesses may welcome the opportunity to make the decision to have an audit – and incur the associated costs - for themselves.

Other implications

The increase in thresholds may reduce the number of audits and accordingly auditors' experience. Ultimately, if the number of audits overall is reduced significantly, there may come a point where either the quality of audits will reduce as a result of the decrease in auditors' experience, or audit experience will be concentrated within a smaller group of practitioners with a consequential risk to competition in the market.

Yours faithfully

Saffery Champness
Chartered Accountants & Registered Auditors