BIS Department for Business Innovation & Skills

AUDIT EXEMPTIONS AND CHANGE OF ACCOUNTING FRAMEWORK

Government Response to Consultation

6 SEPTEMBER 2012

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1. Executive Summary

1. Following consultation, the Government has decided to align mandatory audit thresholds for small companies with accounting thresholds for small companies meeting two out of three criteria for turnover, total assets and number of employees. This change will give 36,000 more companies the chance to be audit exempt.

2. It will also exempt from mandatory audit a further 83,000 subsidiary companies where a company fulfils all of the following conditions:

   (a) its parent undertaking is established under the law of an EEA state;
   (b) the company's shareholders must unanimously agree to dispense with an audit in the financial year in question;
   (c) the parent must give a statutory guarantee of all the outstanding liabilities to which the subsidiary is subject at the end of the financial year;
   (d) the company must be included in the consolidated accounts drawn up by the parent undertaking, which must be prepared in accordance with Directive 83/349/EEC (the Seventh Company Law Directive);
   (e) the use of the exemption by the subsidiary must be disclosed in the notes on the consolidated accounts drawn up by the parent;
   (f) the following documents must be filed by the directors of the subsidiary at Companies House on or before the date that they file the subsidiary's accounts:
      i. written notice of the agreement in (b);
      ii. a statement by the parent that it guarantees the subsidiary company under the particular section of the Act;
      iii. a copy of the consolidated report and accounts referred to in (d) and the auditor's report on those accounts;
   (g) the company is not quoted within s385(2) of the Companies Act ("the Act";
   (h) it is not an authorised insurance company, a banking company, an e-Money issuer, a MiFID investment firm or a UCITS management company, or carries on insurance market activity; and
   (i) it is not a trade union or an employer's association.

3. A further 67,000 dormant subsidiary companies will be exempted from the requirement to prepare and file accounts if they fulfil these conditions. An annual return will still be required to be filed at Companies House.

4. The Government will permit companies who currently prepare IAS accounts to change their accounting framework to UK GAAP for a reason other than a relevant change of circumstances, provided they have not moved to UK GAAP in the previous 5 years. In calculating the 5 year period, no account will be taken of a change due to a relevant change of circumstances. This will permit companies to take advantage of reduced disclosures under UK GAAP. Parent companies will also benefit from this new flexibility with respect to their group accounts, provided they are not

required under EU law to prepare their consolidated accounts using IFRS.

5. The departmental estimate for the audit exemption measure is a saving to business of less or equal to £390m per year. The Regulatory Policy Committee has confirmed that this measure would qualify as an “OUT”. The exact scale of the saving is to be finalised, but is likely to be at least £100m per year[1]. Final figures will be provided in Statement of New Regulation 5. The net benefit of the permitting companies more flexibility to change their accounting framework will be £2.4m per year.

6. It is intended that the changes will come into force for accounting periods ending on or after 1 October 2012 and will also be applied to LLPs.

2. Introduction

7. In the *Plan for Growth*[2] published in March 2011, the Government committed itself to reduce the regulatory burden on UK businesses and to improve corporate governance. Subsequently, on 6 October 2011, BIS published a consultation paper *Consultation on Audit Exemptions and Change of Accounting Framework* together with two Impact Assessments[3]. The consultation covered the whole of the UK. The consultation on increasing audit exemptions concerned the proposal to give more small companies and subsidiaries the ability to make a commercial decision about whether or not to have an audit. It also proposed allowing companies more flexibility to change their accounting framework.

8. 60 responses to the consultation were received, and a table setting out the categorised distribution of responses can be found in Annex A. Following receipt of the consultation responses, further discussions with several stakeholders were held, and a summary of responses to the consultation was published on 2 March 2012[4].

9. Respondents were broadly supportive of the proposals and welcomed the increased level of flexibility and the reduction in the regulatory burden offered by the proposals. To the extent that concerns were raised, they were with regard to the need to protect users of accounts and creditors; the proposed take-up rate of the audit exemption for qualifying non-dormant subsidiaries; and the proposed level of savings for subsidiaries.

10. The audit exemption policy options considered were:

1 HMGovernment One-in, One-out: Fourth Statement of New Regulation URN12/96B page 6 http://www.bis.gov.uk/assets/biscore/better-regulation/docs/o/12-p96b-one-in-one-out-fourth-statement-new-regulation.pdf

2 http://cdn.hm-treasury.gov.uk/2011budget_growth.pdf

3 Audit Exemptions and Change of Accounting Framework, Department for Business, URN 11/1193

4 Department for Business, URN 12/609

- Option A: take partial advantage of the exemptions available under Articles 51(2) and 57 of the 4th Company Law Directive to reduce the mandatory audit, preparation and publication of accounts (the Government's preferred option)
- Option B: take advantage of the full extent of the exemptions available under the above articles.
- Option C: do nothing

- Under the Government's preferred option, mandatory audit thresholds for small companies would be aligned with accounting thresholds for small companies and a subsidiary company would be exempt from mandatory statutory audit where it fulfilled the conditions imposed by the Directive. In addition the Government proposed excluding from the exemptions quoted companies as well as certain other companies, primarily those involved in financial services.

11. In light of the consultation by the Financial Reporting Council (FRC) on changes to UK GAAP[5], the Government also sought views on whether to allow companies who currently prepare accounts under IFRS, as adopted in the EU, more flexibility to change their accounting framework to UK GAAP. This would permit subsidiaries to take advantage of reduced disclosures under UK GAAP.

12. The Change of Accounting Framework policy options considered were:

    - Option A: permit companies to change their accounting framework no more than once every 5 years (the Government's preferred option)
    - Option B: add a change in the accounting standards to the list of relevant reasons for a permitted change in companies' accounting framework
    - Option C: permit companies to change their accounting framework no more than once every 3 years
    - Option D: permit companies to change their accounting framework every year
    - Option E: do nothing/status quo

    It was estimated that the Government's preferred option would result in a net benefit of £2.4m per year, and following consultation, we believe this is still a valid estimate.

13. For both audit exemptions and a change in accounting framework, it was proposed that the changes would apply for accounting years ending on or after 1 October 2012.

14. In light of responses received to the consultation and further consideration of our proposals, the Government has made the following key changes to the proposal:

5 http://www.frc.org.uk/images/uploaded/documents/CP%20Policy%20Proposal%20the%20future%20of%20UK%20GAAP.pdf

- With regard to exemptions for subsidiaries, the guarantee made by the parent undertaking will be a statutory guarantee and will be in respect of all liabilities of the subsidiary which are outstanding at the end of the financial year for which an exemption from audit is being sought.

- We have revised downwards our estimate of the take up rate for the audit exemption for non-dormant subsidiaries, and now estimate the level of take up to be in the range of 50%-75%. This has reduced the net benefit claimed in the Government's Impact Assessment from a range of £408m–£902m per year, to £306m–£608m per year. The departmental estimate for the audit exemption measure is a saving to business of less or equal to £390m per year. The Regulatory Policy Committee has confirmed that this measure would qualify as an "OUT". The exact scale of the saving is to be finalised, but is likely to be at least £100m per year[6]. Final figures will be provided in Statement of New Regulation 5.

- In addition to the ongoing annual cost of internal legal and tax advice, we now assume that parent companies may incur a one-off cost of external legal and tax advice per group holding company when a parent company guarantee is first made and valued. We estimate this one-off cost to be in the range of £2,000-£5,000 per group holding company, although this could be lower as a result of the statutory nature of the guarantee.

3. Government Response

Q1. What are your views on the overall principle of reducing audit requirements for unlisted companies?

Question 1: Government Response

15. As outlined in the March 2011 Plan for Growth[7], we seek to achieve our ambition of making the UK one of the best places in Europe to start, finance and grow a business, in part, through reducing the regulatory burden on UK businesses. Thus, we welcome the broad support received for the overall principle of reducing audit requirements for unquoted companies, and the support for proposals which promote flexibility and prevent UK businesses from being at a disadvantage to their European competitors.

16. We carefully considered the responses to the consultation and came to our decision for the reasons set out below:

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6 HMGovernment One-in, One-out: Fourth Statement of New Regulation URN12/96B page 6 http://www.bis.gov.uk/assets/biscore/better-regulation/docs/o/12-p96b-one-in-one-out-fourth-statement-new-regulation.pdf

7 http://cdn.hm-treasury.gov.uk/2011budget_growth.pdf

- We consider that any reduction in the availability, quality or reliability of financial information, resulting from the reduction in audit requirements, will not be significant.
- Companies can choose to have an audit should they feel it is in their commercial interests.
- Banks and other lending institutions will be able to request additional information or an audited set of accounts from companies seeking finance.
- Finance providers often require current financial information when making commercial decisions; information that is not contained in the statutory accounts.
- HMRC possess the power to request additional information, where they feel it is necessary.
- Companies which are considered more systemically important, such as quoted companies, banks and insurers, have been excluded from the scope of audit exemption proposals.
- The interests of shareholders are protected by safeguards existing in company law whereby, under section 476 of the Act, shareholders holding at least 10% of the share capital may require an audit.

17. Companies that are also charities will still be required to undergo an audit, even if they fall within the scope of the Companies Act exemptions, unless they also fall below the audit exemption thresholds laid out in section 144 of the Charities Act 2011. Further guidance on regulatory requirements for charities can be found on the Charity Commission's website.

Q2.

A. Do you agree with the underlying assumptions in our Impact Assessment that at least 60% of small companies now eligible will take up the audit exemption?

B. Do you agree that the whole audit fee will be saved?

C. Do you agree that there is no saving of management time for small companies taking up the audit exemption?

Question 2: Government Response

18. In our Impact Assessment, we have retained our estimate of a 60% take-up rate for companies now eligible for the audit exemption, and our estimate of the cost of audit. These estimates are based on our analysis of information provided by companies themselves to the FAME[8] database and information provided in the Collis report[9]. In light of

[8] FAME – Financial Analysis Made Easy – Database of company information www.bvd.co.uk
[9] Collis, Jill *Directors' views on accounting and auditing requirements for SMEs* April 2008 http://www.bis.gov.uk/files/file50491.pdf

responses received to the consultation, we recognise that potential savings in management time for small companies availing themselves of the audit exemption may have been underestimated. Therefore, the Final Impact Assessment makes the revised estimate of a 2 hour saving in management time per company for small companies availing themselves of the audit exemption. The departmental estimate for this audit exemption measure is a saving to business of less or equal to £390m per year. The Regulatory Policy Committee has confirmed that this measure would qualify as an "OUT". The exact scale of the saving is to be finalised, but is likely to be at least £100m per year. Final figures will be provided in Statement of New Regulation 5.

Q3. Do you agree that the audit and accounting exemption for small companies should be aligned and a small company should be able to obtain the audit exemption if it meets two out of the three criteria?

Question 3: Government Response

19. Through aligning the audit and accounting thresholds for small companies, we seek to simplify the operation of thresholds and to enable 36,000 more small companies to take advantage of audit exemptions. At the same time we are amending section 479 of the Act so that where a company is a member of a group that qualifies as small for accounting purposes, it will also be eligible for the audit exemption. We do not believe that this alignment will significantly negatively impact on the amount and quality of publicly available financial information for reasons set out in response to question 1. Companies deemed systemically important or of public interest, such as any public company, and banking and insurance companies, will continue to be excluded from the scope of the small companies audit exemption, as will members of an ineligible group.

20. In accordance with section 382(2) of the Act, if a company fails to meet two out of the three qualifying criteria in a particular financial year, it can still avail itself of the audit exemption in that year providing it satisfied two out of the three criteria and qualified as small in the preceding financial year.

Q4. Do you agree that qualifying non-dormant subsidiaries should be exempted from mandatory audit of their accounts?

Question 4: Government Response

21. With regard to concerns raised over the potential level of savings, our estimates of the potential savings in the Impact Assessment are based on analysis of information provided in the FAME database, and take into account any increase in the workload and costs of auditors incurred at group level, where subsidiaries have taken up these exemptions. However, following our consultation, we have revised downwards the

level of potential savings in view of doubts raised by consultees over the assumed level of take-up of the audit exemption by qualifying non-dormant subsidiaries. Please see our response to questions 10-12 for further details of the revised estimates.

22. Our proposals aim to provide a further 83,000 UK subsidiaries with greater flexibility in meeting assurance requirements, and large corporate firms responding to the consultation indicated strong support for these proposals. It will be for each qualifying company and its parent to assess the costs and benefits of availing themselves of the audit exemption, and to determine the best option for their situation.

23. We do not believe our proposals will result in a significant loss in the quality of publicly available financial information as the exemption from the preparation and filing of accounts will only apply to dormant subsidiaries.

24. We do not intend to introduce a limitation on the size of a subsidiary eligible to qualify for audit exemptions, as we believe the potential risks to be mitigated by the qualifying conditions we have imposed additional to those already imposed by Article 57 of the Directive. As subsidiaries will be required to file the consolidated parent accounts at Companies House, stakeholders and potential creditors will have the opportunity to assess the potential level of risk. Furthermore, the required provision of a parent guarantee reduces the level of risk for creditors of the subsidiary.

25. The Government will not be extending the scope of the exemption to companies with parents outside the EEA: having a parent within the EEA makes the parents subject to the EU regime of preparation, filing and audit of accounts to the standard required by EU law. This would not be the case for all parents subject to the laws of 3rd countries.

Q5. What would be the effect of exempting qualifying non-dormant subsidiaries from mandatory preparation of accounts, mandatory filing of accounts and mandatory audit of accounts?

Question 5: Government Response

26. We share the concerns raised by respondents to the consultation, and agree that the risks of exempting non-dormant subsidiaries from the preparation and filing of accounts would outweigh the benefits. Such an exemption would result in a significant reduction in the amount and quality of financial information in the public domain, and this is not in the public interest.

Q6. Do you agree that the Government should exempt qualifying dormant subsidiaries of whatever size from mandatory preparation, mandatory filing and mandatory audit of accounts? What difference would this make to your business and to the wider economy?

Question 6: Government Response

27. Owing to a lack of trading activity and a lack of significant accounting transactions, the preparation and filing of dormant company accounts provides little additional information for the public record. Dormant companies can currently take advantage of an exemption from audit should they fulfill the conditions of section 480 of the Companies Act. We believe there is minimal risk associated with taking advantage of the exemptions available under Article 57 and extending the scope of the exemptions for dormant subsidiaries to include the preparation and filing of accounts.

28. All dormant subsidiaries will still be required to file an Annual Return with Companies House, and those taking advantage of the exemptions will need to file the documents required under the conditions of Article 57 with Companies House. These documents include a written notice of the shareholder's unanimous consent to avail themselves of the exemption or exemptions, the statement of guarantee by the parent and the consolidated accounts of the parent. We do not believe the ability of dormant subsidiaries to hold material assets or liabilities poses a significant threat to financial transparency. The last set of accounts of the dormant company prior to it becoming dormant will continue to be available at Companies House. Dormant subsidiaries will continue to be subject to the group audit, and therefore those holding material assets and/or liabilities will remain subject to independent review.

29. The 67,000 qualifying dormant subsidiaries wishing to take advantage of any of the exemptions available will only be able to do so if they file the documents relating to the exemption at Companies House within the statutory period for the filing of accounts. Therefore, if a qualifying dormant subsidiary, wishing to avail itself of the exemption from the mandatory filing of accounts, fails to file the documents required within the statutory period for the filing of accounts, the subsidiary and its directors will be subject to the normal penalties for the late filing of accounts or the failure to file accounts as set out in the Act.

Q7.

A. Do you agree that in addition to the Article 57 exemptions, in order to qualify, a subsidiary company should be unquoted, not involved in financial services or insurance and not fall into the category of certain other companies under industrial relations legislation, in line with the existing exclusions for the audit exemption in UK company law?

B. Why? What difference would this make to your business and to the wider economy?

Q8. What would be the consequences (e.g. to investors, depositors or lenders or to the wider economy) of allowing financial services subsidiaries to take advantage of this exemption?

Questions 7 and 8: Government Response

30. We believe the conditions we have imposed in addition to those of Article 57 are necessary in order to protect the UK economy. Subsidiaries excluded by virtue of their involvement in financial services, or by being quoted (within the definition of s385(2) of the Act), are potentially systemically important, and therefore should continue to be subject to mandatory audit.

31. In the case where there is an FSA regulated entity in a group, other qualifying subsidiaries within the group will still be eligible to avail themselves of the exemption from audit provided both the group and the FSA regulated entity are still subject to statutory audit, and provided that the auditor of the group and regulated entity reports certain matters that come to their attention during the statutory audit to the FSA (as set out in the Financial Services and Markets Act 2000 (Communications by Auditors Regulations 2001 SI 2001/2587).

Q9. Should the same rules on exemptions for qualifying subsidiaries broadly apply to LLPs and unregistered companies?

Question 9: Government Response

32. We are extending the exemptions for qualifying subsidiaries to LLPs and to unregistered companies.

Q10. Do you agree with our estimate of the savings of the cost of the audit as detailed in the Impact Assessment, and in particular the underlying assumptions:

A. That the average cost of audit is in the range of £8,000 to £83,000 per subsidiary?

B. That 75% to 100% of qualifying subsidiaries will take up the exemption?

C. That 10 to 25% of the audit cost of each qualifying subsidiary will be saved?

Question 10: Government Response

33. Our estimate of the average audit cost is based on analysis of information provided by companies to the FAME database and this remains unchanged in our Final Impact Assessment. We have already recognised that the entire audit cost would most likely not be saved by qualifying subsidiaries availing themselves of the exemption owing to additional audit costs at group level. We have taken this into account in the Final Impact Assessment in estimating the level of potential audit cost savings for subsidiaries taking advantage of the exemption, and have based our estimate of a potential saving of 10-25% of the audit cost on informal discussions with stakeholders. Other issues relating to the Impact Assessment are set out in our response to question 2.

34. Taking concerns expressed by respondents to the consultation into consideration, we have revised downwards our estimate of the take up rate for subsidiaries qualified to use the audit exemptions. We now estimate the take up rate to be in the range of 50% to 75%. As the level of potential savings will vary according to company size and structure, it will be for each qualifying subsidiary to assess the costs and benefits of availing themselves of an exemption from audit, and to decide whether to use such an exemption. Our aim is to provide greater flexibility with respect to audit requirements and to reduce the regulatory burden on companies.

Q11. Do you agree with our estimate of the saving of management time interacting with the auditor and in particular, with our underlying assumptions that for subsidiary companies the saving will be 5 hours of senior management time, which gives rise to £60 to £273 saving per company, depending on size of company?

Q12. Do you agree with our estimate of the saving of the cost of management time to prepare and file dormant subsidiary accounts and in particular the underlying assumption of £280 per dormant subsidiary?

Questions 11 and 12: Government Response

35. We have used the most detailed information available to estimate savings relating to management time. Savings in senior management time for qualifying non-dormant subsidiaries availing themselves of the audit exemption have been estimated using ASHE[10] data for hourly costs for corporate managers. Potential savings in management time arising from the exemption of dormant subsidiaries from the mandatory preparation and filing of accounts have been estimated using the PWC administrative burdens data[11] uprated in line with inflation to 2011 prices. Savings will of course vary depending on the size and nature of the company taking advantage of the exemptions available.

Q13. Do you agree with our estimate of the cost of legal advice of £110 per subsidiary in the first year only, but that if the Government provided guidance on an acceptable form of the guarantee, this cost of legal advice would be zero?

Question 13: Government Response

36. In view of both the level of disagreement expressed in the consultation with respect to our estimate of the cost of legal advice, we have significantly increased our estimate of the cost of obtaining legal and accounting advice with regard to the parent company guarantee. The Impact Assessment anticipates there may be a one-off cost for external legal and accounting advice in the range of £2,000–£5,000 per group holding company when the guarantee is first made and valued, and a subsequent ongoing annual cost for internal legal advice regarding the continued provision of the guarantee.

37. However, in accordance with responses from consultees for more clarity as to the guarantee, the legislation implementing the policy provides that the parent guarantee is given under statute. This should make it more straightforward for parents and creditors, and reduce the legal advice necessary.

38. In terms of ongoing costs, the Impact Assessment estimates that each group will require 4-10 hours of internal legal advice, and based on ASHE data for hourly professional legal services, this will result in an ongoing annual cost of £102–£256 per group. These too may be lower because of the statutory guarantee.

10 ASHE- Annual Survey of Hours and Earning
http://www.statistics.gov.uk/downloads/theme_labour/ashe-2010/2010-occupation.pdf
11 https://www.abcalculator.berr.gov.uk/login_register.php

Q14. Have views of stakeholders expressed to the Company Law Review changed since 2000?

Q15. Do you agree with the Government's conclusions on the likely impacts that would have been involved in exempting non-dormant qualifying subsidiaries from either preparation or filing of accounts and that the costs of such a proposal would be likely to exceed the benefits?

Questions 14 and 15: Government Response

39. We share concerns expressed by stakeholders to the Company Law Review relating to the potential loss of public information resulting from the exemption of qualifying non-dormant subsidiaries from the preparation and filing of accounts, and believe these concerns to be still valid.

Q16. Do you agree with the assumption that it is unlikely that the Government's proposals will have a significantly adverse impact on the number of small audit firms?

Question 16: Government Response

40. While we recognise that some small audit firms may not seek to maintain registration as a statutory auditor, we do not believe that this will significantly adversely impact on the number of small audit firms. Small audit firms will continue to be able to provide business services such as accounts preparation and taxation advice, and those no longer registered as statutory auditors will be able to provide services which they are currently prevented from providing by their position as auditor in accordance with the Ethical Standards of the Financial Reporting Council.

41. We do not believe that levels of audit expertise and training will be significantly adversely affected by our proposals. Companies will, in many cases, still require the expert advice and services of auditors and accountants, thereby encouraging opportunities for training and development.

Q17. Do you agree with Government's assessment of the risks of the proposal?

Question 17: Government Response

42. We believe the risks of this proposal to be largely mitigated by existing provisions in the Act, by the conditions for qualification as outlined in Article 57, and by the additional conditions we have imposed to protect the UK economy. A more detailed description of our position on the risks associated with a potential loss of financial information can be found in

our response to question 1.

43. Should a qualifying subsidiary wish to take advantage of the audit exemption, the parent must make a statement under the particular section of the legislation guaranteeing all outstanding liabilities to which the subsidiary is subject at the end of the financial year to which the statement of guarantee relates. A guarantee given in accordance with the legislation is enforceable against the parent undertaking by any person to whom the subsidiary company is liable in respect of those liabilities. A creditor who has obtained a judgment against the parent guarantor in the courts of England and Wales, Scotland or Northern Ireland will, as a general principle, be able to enforce that judgment in another EEA jurisdiction, without issuing separate proceedings there either by virtue of the Brussels Regulation (Council Regulation (EC) No 44/2001 on the jurisdiction and the recognition and enforcement of judgments in civil and commercial matters) or the 2007 Lugano Convention (Lugano Convention on Jurisdiction and the Recognition and Enforcement of Judgments in Civil and Commercial Matters).

44. We do not foresee any significant difficulties arising with regard to issues of accessibility. If a parent company's audited consolidated accounts filed at Companies House pursuant to this exemption are delivered in a foreign language, they will need to be accompanied by a certified translation into English. The other exemption documents to be filed at Companies House will need to be in English, in accordance with s1103 of the Act. There is an exemption for certain Welsh companies which allows them to file all the exemption documents in Welsh without a translation. Further information can be found in Companies House guidance (GP2, Chapter 13[12]).

45. We believe that the benefits of the flexibility offered to companies by allowing them to use this exemption outweigh the potential cost of enforcement of any guarantee.

[12] http://www.companieshouse.gov.uk/about/gbhtml/gp2.shtml#ch13

Q18. Do you agree that the guarantee should be irrevocable and in respect of all debts in respect of that financial year? Until an audited set of accounts for the subsidiary is filed it will also be in respect of future debts incurred by the subsidiary.

Q19. Do you agree that the guarantee should cover "debts" of the subsidiary and not extend to its "liabilities"?

Q20.

A. Do you agree with the proposals for the Guarantee?

B. Do you think the form of the proposed guarantee will encourage its take-up in line with our assumptions above (75-90%)? If not, why not?

C. Do you have alternative proposals that would not gold plate the Directive, provide adequate protection for those to whom the subsidiary owes a debt, but do not make it unlikely that the parent would issue such a guarantee?

Questions 18-20: Government Response

46. In light of views expressed in both responses to the consultation and in further discussions with stakeholders, we reconsidered the guarantee and have provided that it should be given in statutory form, as discussed above. It will cover all outstanding liabilities to which the subsidiary is subject at the end of the financial year, until they are satisfied in full.

47. The documents required must be filed at Companies House on or before the date that accounts are filed (or within the filing period, if the subsidiary is dormant and proposing to avail itself of the exemptions from the preparation and filing of accounts).

48. In accordance with the existing section 475(2) of the Companies Act, the directors of a subsidiary availing itself of an exemption from audit must also make a statement to that effect on the balance sheet. No declaration of solvency by the directors of the parent company will be required.

49. The filing of the consolidated accounts of the parent company at Companies House will allow creditors to assess potential levels of liability. Further discussion on the legal implementation and enforceability of a guarantee can be found in our response to question 17.

50. Strong support for these proposals was indicated by all large corporate firms responding to the consultation. However, taking the extension of the scope of the guarantee into consideration, along with the significant level of disagreement expressed by respondents to the consultation

regarding our estimate of the likely scale of the take up, we have reduced our estimate of the take-up rate to 50%–75%. Our proposals seek to provide companies with greater flexibility in meeting assurance requirements. Qualifying companies will need to assess the potential benefits of taking advantage of exemptions available, and will need to determine whether these benefits would exceed the risks and costs involved.

51. With regard to concerns raised over the impact of the guarantee on matters such as a company's distributable reserves, dividend payments, cross guarantees, and limited liability status, companies and parents considering taking advantage of exemptions available will have to seek legal advice.

52. The position of charities with respect to audit exemptions is discussed in our response to question 1.

Q21. Do you agree that no new penalties should be proposed in conjunction with the introduction of these proposals?

Question 21: Government Response

53. No new penalties or offences will be introduced in conjunction with the implementation of these proposals. Companies wishing to take advantage of the qualifying subsidiary exemptions will have to file the documents required to claim the exemption within the time period for filing their accounts. If they fail to do so they and their directors will be subject to the normal penalties and offences for the late filing or the failure to file accounts and reports as set out in the Act.

Q22. Do you agree that the Government should impose restrictions on companies' ability to move from IFRS to UK GAAP?

Q23. How frequently should a company be able to move from IFRS to UK GAAP, unless there is a relevant change of circumstances? Every year, every 3 years, every 5 years, or never?

Questions 22 and 23: Government Response

54. The Government has decided to allow companies that prepare their accounts under IFRS to move to UK GAAP for any reason, provided they have not changed to UK GAAP in the previous 5 years. In calculating the 5 year period, no account will be taken of a change due to a relevant change of circumstances under sections 395 and 403 of the Act. This will promote flexibility while maintaining an appropriate level of consistency and comparability. Parent companies will also benefit from this new flexibility with respect to their group accounts, provided they are not required under EU law to prepare their consolidated accounts using IFRS.

55. We consider the risk of misrepresentation to be largely mitigated by
    - the similarities between IFRS and the new accounting framework proposed by the FRC for UK Financial Reporting Standards;
    - by the requirement of company directors, under section 393 of the Act, to approve the accounts only if they are satisfied the accounts give a true and fair view of the company's results and financial position; and
    - by the existing transitional rules in accounting standards which minimise the risk of a lack of comparability between accounts when a change of accounting framework occurs.

56. We recognise that companies will most likely not change their accounting framework on a frequent basis, unless the benefits of doing so outweigh the costs.

Q24.

A. Do you agree with the Government's estimate that 90% of eligible subsidiary companies will take up the option?

B. Do you agree that the saving for each company will be £569?

Q25.
Do you agree that the one-off cost per company will by £390?

Questions 24 and 25: Government Response

57. Following the consultation and informal discussions with stakeholders, we have continued to use the range of 75%–90% as our estimate of the take-up rate for subsidiary companies in our Final Impact Assessment.

58. Our estimate of £569 for the potential saving available to each company taking up this option was based on informal discussions with stakeholders and ASHE data. The uplift for overhead costs relating to staff time has since been revised downwards from 24% to 16%, and in line with this we have reduced our estimate to £533 per company. While we acknowledge the significant level of uncertainty existing over the original estimate of £569, no further significant data is available to contradict our revised estimate of £533. Our estimate of £390 for the one-off cost of switching was based on views of both stakeholders and industry experts. Similarly, this estimate has been revised downwards to £377 in line with the reduction in the uplift for overhead costs to 16%. We recognise that potential savings arising from switching from IFRS to UK GAAP will vary according to company size and nature. It will be for each company to consider the costs and benefits of availing themselves of this option, and to decide on the most appropriate accounting framework. This proposal aims to provide companies with greater flexibility in making this decision.

Q26. Do the proposed changes in any way increase the risk of financial irregularities? If so, what would you estimate the potential impact to be on investors?

Q27. What is the risk that investors will be misled or confused by a company switching between accounting frameworks?

Q28. Do you agree with the Government's assessment of the risks of the proposal?

Questions 26-28: Government Response

59. We believe the proposed changes will not significantly increase the risk of financial irregularities, and consider the risk level of confusion for investors to be low. As discussed in our response to question 23, we believe the risk of misrepresentation will be mitigated by the similarities between the frameworks under the proposals of the FRC, and by existing requirements in company law. The scope for tax arbitrage will be addressed by application of the powers of the tax authorities, with HMRC already having powers to manage the risks associated with companies changing accounting frameworks.

Q29. Do you agree that the proposals should apply to entities for financial years ending on or after 1 October 2012?

Question 29: Government Response

60. 1 October 2012 is the first common commencement date after publication of this Government response. In order to allow companies to take advantage of the increased flexibilities allowed by these changes, it is intended that the changes will apply for accounting periods ending on or after that date.

4. Next Steps

61. The Impact Assessments are published on the BIS website. It is intended that the statutory instrument will be laid before Parliament in order to come into force on 1 October 2012 and that the regulations will apply to accounts for financial years ending on or after that date.

5. Annex A: Responses by Category

Category	Number	% of total responses
Preparer: Large Business (over 250 staff)	3	5%
Preparer Representative Bodies	5	8%
Accountants: over 500 UK Partners	1	2%
Accountants: 200 – 500 UK Partners	2	3%
Accountants: 100 - 199 UK Partners	2	3%
Accountants: 50 - 100 UK Partners	3	5%
Accountants: under 50 UK Partners	20	34%
Accounting Bodies	7	12%
User representative Bodies	4	7%
Regulators and Government Bodies	2	3%
Individuals	5	8%
Credit Rating Agencies and Business Information Providers	6	10%
Total	**60**	**100%**

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