

<b>Institution: Kingston University</b>
<b>Unit of Assessment: 19, Business and Management Studies</b>
<b>Title of case study: Change in UK government policy on auditing and accounting requirements for SMEs, and influence on related policies within Europe.</b>
<p><b>1. Summary of the impact</b></p> <p>Kingston University research into auditing and accounting regulation for small and medium-sized companies influenced the decision by the UK government to increase the size thresholds for these companies to the EU maxima in 2008. Subsequently the mandatory audit thresholds were also increased in 2012, aligning them with the accounting thresholds. This change exempted approximately 36,000 companies from compulsory audit.</p> <p>The research was also used by regulators in Denmark, Sweden, Norway and Finland to inform their decisions on audit exemption thresholds, and by the UK government in lobbying the European Commission on the regulation of micro-companies.</p>
<p><b>2. Underpinning research</b></p> <p>In 2003, Kingston University carried out a survey of 790 small and medium-sized private companies commissioned and published by the Department of Trade and Industry (DTI) as part of the Regulatory Impact Assessment (RIA) on the government's proposal to raise the turnover threshold for audit exemption [R1]. This laid the foundation for a further series of studies by the university.</p> <p>"Directors' Views on Accounting and Auditing Requirements for SMEs" [R2] was a survey of 1,294 small and medium-sized companies commissioned and published by the Department for Business, Enterprise and Regulatory Reform (BERR). It was part of the government's RIA on the effect of raising the turnover threshold for audit exemption from £1m to £5.6m; the likely effects of raising the size thresholds for audit exemption, filing abbreviated accounts and adopting the FRSSE to the EU maxima; and the EC's initial proposals on removing or lightening regulatory burdens on small and medium-sized companies. The survey found that 33% of directors supported the notion of exempting firms with less than 10 employees, 42% were in favour of extending auditing exemptions to medium-sized entities, but 73% of directors of such medium sized companies predicted they would continue to have their accounts audited. A majority of directors (63%) were against increasing the threshold transition period for crossing the size thresholds from 2 to 5 years. Further work applied the same research instrument to a comparative analysis of the UK and Denmark, showing that turnover alone is not a sufficient surrogate for the costs and benefits of audit [R3].</p> <p>"Small company abbreviated accounts: A regulatory burden or a vital disclosure?" [R5] was commissioned by the Institute of Chartered Accountants of Scotland (ICAS). It examined the trade-off between reducing the regulatory burden on small companies in order to try to stimulate growth, and increasing the transparency of financial information in order to reduce business uncertainty, improve credit allocation and facilitate economic development. The study showed that company preparers prefer financial confidentiality but users prefer greater transparency. It also uncovered how reducing financial reporting obligations can in certain situations produce unintended adverse outcomes. Prior to this study, there was little data available from preparers and users on the utility of abbreviated accounts.</p> <p>"Determinants of Voluntary Audit and Voluntary Full Accounts in Micro and Non-micro Small Companies in the UK" [R6] showed the benefits of placing full audited accounts on public record to outweigh the costs for significant proportion of companies. In non-micro small companies, voluntary audit is determined by cost and agency factors, whereas in micro-companies, management factors also play a role. (Note that this research was carried out by Collis in 2007 while she was employed by Kingston University)</p> <p>This research was undertaken by Jill Collis (Reader Kingston 1998-2010; Brunel 2010-present), Prof Rob Blackburn (Director of Research, Director of Small Business Research Unit, Kingston),</p>

Eva Kašperová (Research Assistant, Kingston) and John Kitching (Reader, Kingston)

### 3. References to the research

[R1] Collis, J (2003) Director's Views on Exemption from the Statutory Audit", London: Department of Trade and Industry. Available from <http://www.berr.gov.uk/files/file25971.pdf>)

[R2] Collis, J. (2008) Directors' Views on Accounting and Auditing Requirements for SMEs, London: BERR. Available from <http://www.bis.gov.uk/files/file50491.pdf>

[R3] Collis, J. (2010) 'Audit exemption and the demand for voluntary audit – a comparative analysis of the UK and Denmark', International Journal of Auditing, 14(2), pp. 211-231. This journal is ranked as 2\* by ABS 2010.

[R4] Kitching, J., Kašperová, E., Blackburn, R. and Collis, J. (2011) Small company abbreviated accounts: A regulatory burden or a vital disclosure? Edinburgh: Institute of Chartered Accountants in Scotland. ISBN 978-1-904574-80-4 EAN 9781904574804. Available from <http://www.icas.org.uk/site/cms/contentviewarticle.asp?article=7529>

[R5] Collis, J. (2012) 'Determinants of voluntary audit and voluntary full accounts in micro- and non-micro small companies in the UK', Accounting and Business Research, 42(4), pp. 1-28. This journal is ranked as 3\* by ABS 2010.

#### Research grants

Survey on the Small Company Audit  
Department for Trade and Industry (DTI).  
March 2003 – October 2003  
£9,583 awarded to Jill Collis, Kingston University  
Related outputs: [R1], [R3]

SME Accounting and Auditing Requirements  
Department for Business, Enterprise and Regulatory Reform (BERR)  
August 2007 - February 2008 (7 months)  
£25,000 awarded to Jill Collis, Kingston University [see S2]  
Related outputs: [R2], [R5]

The Value of Small Company Abbreviated Accounts  
Institute of Chartered Accountants of Scotland (ICAS)  
August 2010 - January 2011 (6 months)  
£24,828 awarded to John Kitching, Kingston University with Jill Collis, Brunel University  
Related output: [R4]

### 4. Details of the impact

In 2008, the UK government raised the UK size thresholds for accounting regulation to the EU maximum for smaller companies [S3]. The results of the Kingston research influenced the UK government's decision to raise the UK thresholds through engagement with the relevant government departments, as detailed below. These increases in the size thresholds formed an amendment to the Companies Act 2006. It is estimated that 3,100 medium-sized companies and 1,600 large companies were eligible to prepare and file less detailed accounts at Companies House due to this change. The reduced reporting requirements would lead to a saving of only 6 hours of accountancy time per year, using an hourly rate of £26.0017 the savings per company would be in the region of £156 per annum [Dept. for Business Innovation & Skills (BIS) Impact Assessment No 0301] This could result in a reduced burden for all 4,700 qualifying companies amounting to a total saving of up to £730k per annum. Around 2100 companies also became eligible for first year capital allowances provided by the tax system. [S4]

The underpinning research cited in Sections 2 and 3 above, in particular [R1] and [R2], formed a critical part of the process that led to this change. The research findings were used as part of the evidence on which the Department of Business, Enterprise and Regulatory Reform (BERR) based recommendations to the Secretary of State in deciding the approach the UK should take on audit exemptions [S1, S2]. The Director of Accounting Policy Corporate Law & Governance at BERR,

said “The statistics produced on the numbers of small companies using an external accountant to prepare their statutory accounts gave us useful data... and meant we were able to present to Ministers options which were grounded in experience” [S2].

One of the key research findings showed that the directors of small companies see benefits in retaining the audit and having an independent check on their results. Nevertheless, they supported the proposals to increase the audit exemption threshold. This helped BERR gauge the potential reactions of small companies and meant the options BERR presented to the Secretary of State for Business were firmly grounded. [S4] (Note: Audit size exemptions were not changed at this point).

In 2011, BERR - now renamed the Department for Business Innovation & Skills (BIS) - drew on the results of [R1 and R2] in drafting an initial impact assessment of aligning audit exemptions with accounting exemptions for small companies and in the final impact assessment published in 2012. The research [R2] was referenced six times by BIS when it was assessing whether to align audit exemptions with accounting exemptions for small companies. [S6, S8]. The research concerned take-up rates for small company audit exemption, related time and cost savings. Of particular interest to BIS were the findings on the director’s perceptions of users of their published accounts [S7]. The regulations introducing the changes have now been published [S9] and the changes apply for accounting years ending on or after 1st October 2012. This change exempts approximately 36,000 from compulsory audit. The Government also exempted most subsidiary companies from mandatory audit, as long as their parent company guarantees their liabilities, affecting a further 83,000 subsidiary companies [S10]

In addition, another 67,000 dormant subsidiaries will no longer need to prepare and file annual accounts, provided they receive a similar guarantee.

The research instrument [R3] was subsequently used as the basis for regulatory impact assessments in Denmark, Finland, Norway and Sweden, where the regulators were investigating the most appropriate thresholds for introducing audit exemption. The Chairman of the Governmental Commission on Audit and Auditing, Ministry of Justice, Sweden said, “The information you provided was excellent and gave us a more comprehensive view on policy on audit and accounting...” [S5]. Thus, Kingston University’s research on this topic had an impact on policy making in the UK and four Nordic countries, and consequently on auditors, preparers and users of the financial statements.

The main beneficiaries of the research are regulators in the UK and other jurisdictions who have conducted consultations and regulatory impact assessments on the EU changes to the accounting and auditing requirements for smaller entities. The findings of the research are also useful in helping the directors of such companies and their accountants weigh up the costs and benefits of their options under the Companies Act 2006, and will also be of interest to lenders, creditors and other users of the financial statements.

**5. Sources to corroborate the impact**

[S1] BERR Scope of Work for Research Grant, 2007

[S2] Letter from Director of Accounting Policy Corporate Law & Governance, BERR, July 2007 (Corroborating Identifier: 1)

[S3] Statutory Implementation of Directive 2006/46/EC

[S4] Dept for Business Enterprise & Regulatory Reform (BERR) Explanatory Memorandum 2008, no 393

[S5] Letter from Chairman of the Commission on Audit and Auditing, Ministry of Justice, Goteborg, Sweden. Nov, 2007. (Corroborating Identifier: 2)

[S6] Dept. for Business Innovation & Skills, Impact Assessment No BIS 0301, 05/09/2011 Consultation. Contact: Member of Audit and Accounting team, Department for Business, Innovation and Skills. (Corroborating Identifier: 3)

**Impact case study (REF3b)**

[S7] Email from Audit Policy staff member, Department for Business, Innovation and Skills 2012  
(Corroborating Identifier: 4)

[S8] Dept for Business Innovation & Skills, Impact Assessment No BIS 0301, 12 June 2012 Final,  
Contact: Member of Audit and Accounting team, Department for Business, Innovation and Skills.  
(Corroborating Identifier: 3)

[S9] Statutory Implementation 2012 No 2301

[S10] ACCA Guidance on Changes to Audit Exemption Threshold from 1 Oct 2012. Available at  
[http://uk.accaglobal.com/uk/members/technical/advice\\_support/audit\\_assurance/auditing\\_guidance/2012aud/caet](http://uk.accaglobal.com/uk/members/technical/advice_support/audit_assurance/auditing_guidance/2012aud/caet)