

1 Small company exemption thresholds – examples (Lecture A687 – 20.50 minutes)

It is surprisingly common to see financial statements where small company exemptions have been used despite the company not being eligible to take them! Where a qualified accountant was involved in the preparation of the accounts this creates a major risk for them because their professional body expects them to check that a company is eligible for the small company exemptions that it applies.

Consequently, it is not unusual to see professional accountants being disciplined by ACCA or ICAEW for failings in this area.

This section is intended to remind accountants of the rules and how easy it is to get an assessment of eligibility wrong.

1.1 Small company exemption thresholds

The qualifying conditions to be small are met by a company (or group) in a year if it satisfies two or more of the following requirements:

- **Turnover** Not more than £10.2 million
- **Balance sheet total** Not more than £5.1 million
- **Average number of employees** Not more than 50

In order to qualify as small in any financial year (other than its first) the entity must:

- a) meet the qualifying conditions in the current year and the previous year; or
- b) meet the conditions in the current year and qualify as small in the previous year; or
- c) meet the conditions in the previous year and qualify as small in the previous year.

Note that, in the case of c), it does not have to satisfy the requirements in the current period.

Example 1

X Ltd incorporates on 1 July 2017. These are its results for its five periods ending on 31 December:

	2017	2018	2019	2020	2021
Turnover	£6.5m	£11.2m		£9.2m	£8.0m £8.5M
Balance sheet total	£6.1m	£7.5m	£5.5m	£4.5M	£5.5M
Number of employees	40	45	51	45	45

Is the entity eligible to apply the small company accounting exemptions?

Is the entity eligible for small company audit exemption?

Example 2

The following data applies to the H Group for the year ended 31 December 2019. The group consists of H Ltd (parent) and three wholly owned subsidiaries – A Ltd, B Ltd and C Ltd.

	H Ltd	A Ltd	B Ltd	C Ltd
Turnover	£1m	£11m	£1m	£1m
Balance sheet total	£2m	£4m	£1m	£1m
Number of employees	10	55	10	10

The figures for the years 31 December 2018 and 31 December 2017 were the same as those shown above. There is no trading within the group and no balances with other members of the group.

Which of the companies qualify as a small company in 2019 and which of them qualify for audit exemption?

Example 3

My firm is the auditor of a UK subsidiary of Spanish holding company. The UK company has turnover and gross assets below the audit exemption thresholds and the directors wish to take advantage of audit exemption in order to reduce costs. The holding company has not requested an audit and has stated that they will be satisfied with a compilation report from my firm. The holding company auditor has also not requested that the subsidiary is audited.

Can the UK company directors take advantage of audit exemption when the company is part of a group?

Example 4

Currently, my firm is considering whether to accept appointment as advisors for a UK company who takes advantage of audit exemption. The company is a subsidiary of a holding company incorporated in an offshore jurisdiction where financial statements are not publicly available. The UK directors say that they do not have access to financial information for the holding company or other group companies.

Is this company eligible for audit exemption?

The solutions to these examples are overleaf.

2 Appendix: Small company exemption thresholds – solutions to examples

Example 1 - Solution

X Ltd incorporates on 1 July 2017. These are its results for its five periods ending on 31 December:

	2017	2018	2019	2020	2021
Turnover		£6.5m	£11.2m		£9.2m £8.0m £8.5M
Balance sheet total		£6.1m	£7.5m	£5.5m	£4.5M £5.5M
Number of employees			40	45	51 45 45

Is the company eligible to apply small company accounting exemptions?

2017: No – remember to pro-rate turnover for the six-month accounting period

2018: No

2019: No

2020: No – it has to be small for two consecutive years

2021: Yes – this is the second year it is small

Is the company eligible for small company audit exemption:

2017: No

2018: No

2019: No

2020: No

2021: Yes

Note: Ignoring groups, if a company is small then it is also able to claim audit exemption. Small company audit exemption is not available to members of medium sized or large groups.

Example 2

The following data applies to the H Group for the year ended 31 December 2019. The group consists of H Ltd (parent) and three wholly owned subsidiaries – A Ltd, B Ltd and C Ltd.

	H Ltd	A Ltd	B Ltd	C Ltd
Turnover		£1m	£11m	£1m £1m
Balance sheet total		£2m	£4m	£1m £1m
Number of employees			10	55 10 10

The figures for the years 31 December 2018 and 31 December 2017 were the same as those shown above. There is no trading within the group and no balances with other members of the group.

Which of the companies qualify as a small company in 2019 and which of them qualify for audit exemption?

H Ltd – Parent of a medium-sized group. Therefore, it cannot be small, it must be medium-sized. No audit exemption can be claimed unless it were a member of a larger group where the s479A group audit exemption might apply (if the conditions are met).

A Ltd – Clearly medium-sized – small company audit exemption is not available but s479A might be.

B Ltd & C Ltd – Small for accounting purposes. Small company audit exemption is not available because it is a member of a medium-sized group. s479A audit exemption might be available.

Example 3

My firm is the auditor of a UK subsidiary of Spanish holding company. The UK company has turnover and gross assets below the audit exemption thresholds and the directors wish to take advantage of audit exemption, in order to reduce costs. The holding company has not requested an audit and has stated that they will be satisfied with a compilation report from my firm. The holding company auditor has also not requested that the subsidiary is audited.

Can the UK company directors take advantage of audit exemption when the company is part of a group?

Small company audit exemption is not available because the group is not small. The fact that the group includes overseas companies makes no difference; the overseas entities are included when considering the size of the group. Note s479A audit exemption could be available

Example 4

Currently, my firm is considering whether to accept appointment as advisors for a UK company who take advantage of audit exemption. The company is a subsidiary of a holding company incorporated in an offshore jurisdiction where financial statements are not publicly available. The UK directors say that they do not have access to financial information for the holding company or other group companies.

Is this company eligible for audit exemption?

Small company audit exemption is only available if the directors are satisfied that the conditions for the exemption are met. Ignorance is not an excuse for getting this wrong. s479A is probably not available because of the nature of the holding company.