

Guernsey Companies Law - Audit Exemption

This memorandum has been prepared for the assistance of our clients in connection with the provisions of the Companies (Guernsey) Law, 2008, as amended (the "**Companies Law**") relevant to the exemption available to audit requirements. It is intended to provide only a summary of the main legal and general principles and it is not intended to be comprehensive in scope. It does not cover transitional provisions in place in respect of the Companies Law. It is strongly recommended that you seek specific legal advice on such matters and we would be pleased to assist in this respect. A series of briefings on other specific aspects of Guernsey companies has been produced by Ogier and is available on our website www.ogier.com.

The memorandum has been prepared on the basis of the law and practice in Guernsey as at 10 August 2009.

Audit Requirement

A Guernsey company's accounts for a financial year must be audited in accordance with the provisions of the Companies Law unless the company is exempt from audit under the provisions of the Companies Law.

Audit Exemption

The members of a company may pass a waiver resolution exempting the company from the requirement to have its accounts for a financial year audited.

Such a waiver resolution electing for exemption must be passed in the financial year before the financial year to which it relates, or, if the financial year is the company's first financial year, in that financial year.

A waiver resolution is a resolution of the members of a company passed by a majority of not less than 90%. Waiver resolutions are required to be delivered to the Registrar of Companies within 30 days of being passed.

Limitations

The Companies Law grants the Department of Commerce and Employment the power to make regulations preventing certain types, classes or descriptions of company from being exempt from audit and in this regard it has issued regulations in the form of the Companies (Audit Exemption) Regulations, 2008 (the "**Regulations**").

The Regulations provide that the members of a company which is a "large company" are prohibited from passing a waiver resolution exempting the company from having its accounts for a financial year audited. However, where during the course of a financial year the members of a large company are satisfied that the company will not meet the qualifying conditions in that financial year, then they may pass a waiver resolution revoking the appointment of the auditor.

A company is a "large company" if (i) any two of the qualifying conditions stipulated in the Regulations (see below) are met in any financial year and in the preceding financial year and (ii) it is not deemed to be a small company.

The qualifying conditions referred to above are that:

- (a) the company has an annual net turnover of £6.5 million or greater;
- (b) the company has a net balance sheet of £3.26 million or greater;
- (c) the company has an average number of employees of 50 or more.

"Net" is defined in the Regulations as "in relation to turnover of balance sheet totals means the turnover or balance sheet total after any set-offs or other adjustments made to eliminate group transactions in accordance with generally accepted accounting principles or other international reporting standards" (emphasis added). We suggest that the underlined word "of" is a typographical error and should be "or", as per the same phrase later in the sentence.

Accordingly "net turnover" (as referred to in condition (a) above) is turnover after any set-offs or other adjustments made to eliminate group transactions in accordance with generally accepted accounting principles or other international reporting standards.

The phrase "net balance sheet" referred to in condition (b) above is not defined in the Regulations while the term "balance sheet total" is defined as meaning "the aggregate amounts shown as assets in the company's balance sheet".

The term 'balance sheet total' is unfortunately not used in the body of the Regulations but is rather only used in the definition of "net" referred to above. We suggest that the reference in the conditions to a company having a net balance sheet of £3.26 million or greater should have

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actually been a reference to a company having a net balance sheet total of £3.26 million.

Certain companies are not “large companies”, regardless of whether they otherwise meet the qualifying conditions. These are (a) “dormant companies”, (b) “asset holding companies” and (c) companies with 10 or fewer members.

A company is “dormant” during any period in which (disregarding any transaction arising from a founder’s subscription for shares in accordance with the company’s memorandum, and disregarding any fees payable under the Companies Law) no transaction occurs which is required by the Companies Law to be entered in its accounting records (and a company ceases to be dormant on the occurrence of such a transaction).

A company is an “asset-holding company” during any period in which:

- (a) its principal purpose is to own specified assets or assets of specified descriptions;
- (b) it does not engage in trade;
- (c) its activities (if any) are all directly connected with its ownership of those assets;
- (d) it receives no significant income other than income derived directly from its ownership of those assets; and
- (e) it incurs no significant expenditure other than expenditure incidental to its ownership of those assets;

and a company ceases to be an asset-holding company when it no longer has all of the above attributes.

Rescission and Non Companies Law Requirements to Audit

The Companies Law provides for the rescission of a waiver resolution exempting a company from the audit requirement if the company receives requests to do so from:

- (a) members holding more than 10% in value of the company’s share capital or any class of it (excluding any shares held as treasury shares), or
- (b) if the company does not have a share capital, more than 10% in number of the members of the company.

Finally, it should be noted that the Companies Law also provides that its provisions as regards passing a waiver resolution in respect of exemption from audit only have effect in respect of obligations under the Companies Law and do not prejudice any other obligation of a company to have its accounts audited. Supervised companies (i.e. companies supervised under various regulatory laws such as the Protection of Investors (Bailiwick of Guernsey) Law, 1987, as amended) would not be able to waive the audit requirement.

Application

The use of a Guernsey company with unaudited status in a transaction structure may have favourable implications in respect of time and cost savings and clients may wish to take this into account when considering jurisdictions in which to structure products. If there is compliance with the provisions of the Companies Law and the Regulations then entities used in specific types of structures (e.g. in securitisation structures) should not be barred from using the exemption.

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