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The Travel Accountants

CAA Reveals New ATOL Criteria Commencing 1 June 2016

The Civil Aviation Authority (CAA) has today released the criteria by which all ATOL applications and renewals will be assessed with effect from 1 June 2016.

Those businesses that hold a standard ATOL will be familiar with the free asset test, which has been in place for many years. This formulaic calculation will be replaced with a risk-based assessment of seven financial factors (7 Tests), with each having a different weighting. An online form will be available for ATOL-holders to self-assess their financial position with the CAA providing an indicative decision prior to the formal renewal process.

Elman Wall comment: *Under the free asset test, it was relatively simple to predict whether the CAA would request a cash injection prior to renewal of an ATOL. The new criteria, which are more akin to a credit-score, do not have such a formulaic approach and the CAA will not be divulging the methodology that sits behind the overall assessment. The online self-assessment form will prove to be a useful tool when making plans for dividend distributions or capital investments.*

Small Business ATOL (SBA)

Under the previous criteria, a business could hold an SBA, subject to a limit of 500 passengers per year, with little, if any, financial assessment being undertaken by the CAA.

Under the new regime, the limit of 500 passengers will remain, but an additional limit of £1M of ATOL turnover will be introduced. In addition, SBA-holders will now be subject to a financial assessment based on four tests – *see table below.*

Elman Wall comment: *The retention of the SBA concept for truly small ATOL-holders is to be welcomed. However, the larger current SBA-holders will exceed the limit of £1M ATOL turnover so careful planning will be required when they are required to 'trade up' to a Standard ATOL. Well-run businesses with prudent decision-making policies should have nothing to fear.*

Standard ATOL-holders with ATOL turnover up to £20M

These ATOL-holders will be subject to the financial assessment based on 7 Tests – *see table below.*

Some businesses considered to be higher risk will be subject to a more in-depth analysis of the resources and financial arrangements. Examples would include high seasonality, over-reliance on a limited number of destinations or suppliers, or a risk of over-trading (growing too quickly).

Elman Wall comment: *With the exception of those businesses that are considered to be of higher risk, ATOL-holders with ATOL turnover of £5M - £20M will now fall under the self-assessment regime so they should now see their assessment burden reduced.*

Large ATOL-holders

The largest ATOL-holders, with licensable turnover of £20M or more, are currently subject to a more in-depth risk-based approach. These companies will see little difference in the way they are assessed, with the CAA continuing to review finances, business models & strategy and corporate governance.

Financial assessment – SBAs and Standard ATOLs

The financial assessment for ATOL-holders is based on an analysis of certain ratios. SBA-holders are assessed on four ratios and Standard ATOL-holders on seven, as set out below. The result of this assessment provides an indication of whether or not an ATOL-holder meets the overall financial criteria for holding an ATOL. Where the criteria are not met, the CAA would normally require a cash injection.

7 Tests Table

Financial ratio	Calculation	Demonstrates	Target	SBA	Standard ATOL
Current ratio	Current assets / Current liabilities	Ability to settle liabilities as they fall due	Positive, the higher the better	Yes	Yes
Cash ratio	Cash / Current liabilities	Ability to settle liabilities as they fall due using existing cash reserves	Positive, the higher the better	Yes	Yes
Leverage ratio	Total Liabilities / Total assets	Balance sheet strength; Reliance on debt	Less than 1, the lower the better	Yes	Yes
Return on assets	Net profit/(loss) / Total assets	Efficiency to generate profits from assets	The higher the better	Yes	Yes
EBITDA margin	EBITDA / Revenue	Profitability	The higher the better	N/A	Yes
Revenue growth	Revenue / Prior year revenue	Growth or decline	Positive, controlled increase to demonstrate manageable growth	N/A	Yes
Revenue variance	Revenue / Projected revenue	Ability to forecast accurately	As close to 1 as possible	N/A	Yes

Elman Wall comment: *Profitable and solvent companies should have nothing to fear about these tests. Our biggest concern is the impact of the new accounting standard FRS102 which is expected to increase volatility within the Profit & Loss Account, particularly for companies entering into forward contracts for foreign currency purchases. Careful planning will be required when deciding whether to make significant investments.*

Share capital

ATOL-holders must have a minimum of £30,000 ordinary share capital.

The only exception is where an ATOL-holder held an SBA on 31 May 2016 and there have been no material changes to ownership or control. In these cases, there is not normally a requirement to have a minimum of share capital.

Elman Wall comment: *The exemption for existing SBA-holders is welcome news, so it looks like the CAA has listened to the initial concerns from these businesses. Careful planning will be required when an SBA-holder is close to the limits and likely to need to trade up to a Standard ATOL, particularly in terms of the company's share capital.*

Audit requirement

The CAA generally requires companies to submit audited financial statements. Where an ATOL-holder with an ATOL limit of less than £5M is not required to prepare audited financial statements under the Companies Act, the CAA may accept unaudited accounts.

Elman Wall comment: *This is good news for those businesses that do not need to have an audit, reducing the cost and administration of compliance. There are a number of reasons why a company may choose to have an audit even when there is no statutory or regulatory need so, before deciding to dispense with the audit, businesses should consider all stakeholders such and banks and potential investors.*

ATOL Reporting Accountants

The ATOL Reporting Accountants' (ARA) scheme takes effect **from 1 April 2016**. From this date, the CAA will only accept documents from accountants and their firms who undergo registration, training and accreditation from their professional body such as the Institute of Chartered Accountants in England & Wales.

Elman Wall comment: *We see numerous examples of accountants not really understanding their travel clients' business and the regulation that sits behind it, so this is a positive step towards improving that knowledge across the industry. Elman Wall participated in the pilot scheme and Jonathan Wall, Ian Palmer and Yasin Khandwalla received their accreditation in December 2015.*

Summary

The new financial assessment regime has been designed to allow the CAA to focus their attention and resources on the largest ATOL-holders and those which are deemed to have the highest risk of failure.

Elman Wall comment: *Overall, we consider the new assessment regime to be a positive step forward. Undoubtedly there will be a period while the industry gets a feel for the new assessment criteria, but many ATOL-holders will see their administrative burden reduced.*

If you are an Elman Wall client, we will be liaising with you about the impact of these new financial assessments but please contact Ian Palmer or Yasin Khandwalla if you have any immediate questions.

Elman Wall - The Travel Accountants currently has over 170 travel industry clients, of which more than 100 hold ATOL licences. If you have any questions about the new ATOL rules or about the ATOL Reporting Accountants' Scheme, then also please do not hesitate to be in touch.

For further guidance on the new ATOL criteria, or about the ATOL Reporting Accountants' Scheme, please contact Ian, Yasin or Jonathan on 020 7600 5667 or email travel@elmanwall.co.uk