Supplier management

Supplier financial appraisal guidance: annexes

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Supplier financial appraisal guidance
Annexes

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Annex A
Audit and filing dates and exemptions

The detailed rules concerning the preparation and filing of accounts are published in the Companies House booklet *Accounts and Accounting Reference Dates*. These rules are summarised below.

Legislation

The regulations regarding the preparation of accounts and their filing at Companies House are legislated for under the Companies Act 1985 as amended.

Accounting records

All limited and unlimited companies, whether or not they are trading, must keep accounting records. Generally, accounts must include:

- a Profit & Loss account (or income and expenditure account if the company is not trading for profit);
- a balance sheet signed by a director;
- an auditors' report signed by the auditor (if appropriate);
- a directors' report signed by a director or the secretary of the company;
- notes to the accounts; and
- group accounts (if appropriate).

Accounting Reference Date

The Accounting Reference Date (ARD) is the financial year-end and the date that determines when accounts are due for delivery to Companies House.

A company's first accounts cover the period starting on the date of incorporation, not the first day of trading. They end on the ARD or up to seven days either side of that date. Subsequent accounts start on the day after the previous accounts ended. They finish on the ARD or up to seven days either side of it.

An accounting period cannot be extended so that it lasts more than 18 months. It also cannot be extended more than once in five years unless:

- the company is subject to an administration order, or
- the company is aligning its accounting reference date with that of a subsidiary or parent undertaking established within the European Economic Area.

A company incorporated overseas which has registered a branch in Great Britain, and which does not have to publish audited accounts in its country of incorporation, or has registered a place of business in Great Britain, is subject to the same ARD rules except that it is not restricted as to how often it may extend accounting periods.

A company incorporated overseas which has registered a branch in Great Britain, and which has to publish accounts in its country of incorporation is subject to different rules.

Filing of accounts

All limited and public limited companies must send their accounts to the Registrar at Companies House. If they are eligible and wish to, medium-sized, small and dormant companies may prepare and file abbreviated accounts.

Unlimited companies need only deliver accounts to the Registrar if, during the period covered by the accounts, the company was:

- a subsidiary or a parent of a limited undertaking; or
- a banking or insurance company (or the parent company of a banking or insurance company); or
- a qualifying company within the meaning of the Partnerships and Unlimited Companies (Accounts) Regulations 1993; or
- operating a trading stamp scheme.

Filing dates

The time normally allowed for delivering accounts is:

- for a private company, 10 months from the ARD;
- for a public company, seven months from the ARD.

The period allowed for sending a company's first accounts is calculated differently.

If a company carries on business or has interests overseas, a 3-month extension to the normal filing period can be claimed by the company delivering Form 244 to Companies House. This form must be delivered before the normal filing deadline.

There are penalties for late filing (e.g. £5,000 if a public company delays by more than 12 months; £1,000 if a private company delays by more than 12 months). Failing to deliver accounts on time is also a criminal offence for which company directors may be prosecuted.

SMEs

Certain small or medium-sized companies (often referred to as Small to Medium sized Enterprises or SMEs) may prepare and deliver abbreviated accounts to Companies House. If the company ceases to be small or medium-sized, the exemption continues for the first year that the company does not fulfil the conditions.

Public companies and certain companies in the regulated sectors cannot qualify as small or medium-sized companies.

To be a small company, at least two of the following conditions must be met:

- annual turnover must be £2.8 million or less;
- the balance sheet total assets must be £1.4 million or less;
- the average number of employees must be 50 or less.

Abbreviated accounts of a small company must include:

- the abbreviated balance sheet and notes; and
- a special auditor's report (unless the company is also claiming audit exemption).

To be a medium-sized company, at least two of the following conditions must be met:

- annual turnover must be £11.2 million or less;
- the balance sheet total assets must be £5.6 million or less;
- the average number of employees must be 250 or less.

Abbreviated accounts of a medium-sized company must include:

- the abbreviated Profit & Loss account;
- the full balance sheet;
- a special auditor's report;
- the directors' report; and
- notes to the accounts.

The special auditor's report should state that in the auditor's opinion the company is entitled to deliver abbreviated accounts and that they have been properly prepared in accordance with the Companies Act.

The balance sheet (and if appropriate, the directors' report) must contain a statement that the accounts are prepared in accordance with the special provisions of the Companies Act relating to small or medium-sized companies, as the case may be.

SME groups

A parent company need not prepare group accounts or send them to Companies House if the group is small or medium-sized and none of its member companies is a public company.

To qualify as small, a group of companies must meet at least two of the following conditions:

- aggregate turnover must be £2.8 million net (£3.36 million gross) or less;

- the aggregate balance sheet total assets must be £1.4 million net (£1.68 million gross) or less;
- the aggregate average number of employees must be 50 or less.

To qualify as medium-sized, a group must satisfy at least two of the following conditions:

- its aggregate turnover must be £11.2 million net (£13.44 million gross) or less;
- the aggregate balance sheet total assets must be £5.6 million net (£6.72 million gross) or less;
- the aggregate average number of employees must be 250 or fewer.

Small companies

Small companies with a turnover of not more than £1 million and total balance sheet assets of not more than £1.4 million can claim exemption from audit. However, audited accounts must be delivered to Companies House if the company falls into any of the following categories:

(a) A parent company or subsidiary undertaking (unless dormant for the period during which it was a subsidiary) except where the group:

- qualifies as a small group;
- turnover for the whole group is not more than £1 million net or £1.2 million gross; and
- the group's combined balance sheet total is not more than £1.4 million net (£1.68 million gross).

(b) A member of a group of companies in which any member is a public company.

(c) A subsidiary company incorporated under the Companies Act which is part of the group whose parent company is an overseas undertaking.

(d) A public limited company unless the company is dormant.

An audit-exempt company needs to send unaudited accounts to Companies House in the form of an abbreviated balance sheet. Unaudited accounts do not of course provide the reassurance of accounts that have been independently audited.

Partnerships

The Partnerships and Unlimited Companies (Accounts) Regulations 1993 require companies which are members of 'qualifying partnerships' to prepare and attach accounts of the partnership to their own accounts.

A qualifying partnership is a partnership that is governed by the laws of any part of Great Britain if each of the members is:

- A limited company; or
- An unlimited company or a Scottish firm, each of whose members is a limited company.

Annex B
Key ratios for analysis

Accounting ratios are an aid for analysing and interpreting relationships existing between different items in a candidate's financial statements. Ratio analysis helps to highlight areas and items that should be subjected to more detailed examination and questioning.

Few figures in financial statements are highly significant in and of themselves. Rather it is their relationship to other quantities or the direction and amount of change over a period that is important.

Ratios can be logically divided into three main groups (a summary table for reference is shown at the end of this annex):

Financial structure

Assessment of whether a candidate is likely to experience cash flow problems and whether the business is adequately financed and from what sources. The main areas are liquidity and gearing (or leverage). The following principal ratios would assist this analysis:

Acid test ratio - also known as the liquidity or quick ratio
(current assets – stock) / current liabilities

This is a more severe test of liquidity than the Current Ratio as it excludes the least liquid portion of current assets, stocks. Its 'defect' is that it does not define the liquidity of the individual components of liquid assets and current liabilities. These individual liquidities could be crucial to the overall liquidity of the business. While a ratio of 1:1 is generally considered appropriate, many companies can survive and trade with ratios considerably less than that and others have liquidity problems with ratios well in excess of it.

Long-term leverage ratio
(long-term debt / net worth) × 100 = %

This is sometimes calculated in relation to total capital employed rather than to net worth. It highlights the relative importance of long-term debt in the capital structure and can therefore provide useful additional information for assessing the acceptability of the overall leverage position of the business.

Bank leverage ratio
(bank debt / net worth) × 100 = %

This is important in terms of the financial viability of the business because of the relatively strong position in which banks usually put themselves relative to other

providers of funds. Bank debt is usually secured and entails comprehensive powers for the bank to take action if the ratio gets out of line or some other financial deterioration in the position of the business occurs. The ratio should be kept at a level acceptable to the lending bankers.

Interest cover
operating profit / interest charges

This shows the number of times available profit covers interest charges and measures the extent to which operating profit can fall without being insufficient to cover the interest charges and thereby create a pre-tax loss.

Operating performance

The principal ratios for assessing operating performance are listed below and combined with the ratios above would assist the detailed financial appraisal process.

Return on capital employed (ROCE) - also known as the primary ratio
(operating profit / capital employed) × 100 = %

ROCE is the most important measure of the overall efficiency of the management of the business because it relates the result of operations to the total funds being used in the business. It avoids the distortions that might arise from different capital and financing structures and therefore gives a measure of the efficiency with which the resources of the business have been utilised irrespective of how they have been financed. It sheds more light on the criticality of gearing and, when compared with the acid test, gives an idea as to the candidate's vulnerability to take-over and bankruptcy. Capital employed is the total of shareholders' funds and long-term debt or expressed in terms of assets as total assets less current liabilities. Operating profit is used because loans are included in the capital employed and therefore the return on them must be calculated before charging the interest on them.

Return on total assets
(operating profit / total assets) × 100 = %

This ratio measures the overall efficiency with which assets are being utilised.

Gross profit ratio – also known as the gross margin
(sales less cost of sales / turnover) × 100 = %

This ratio is an indicator of the efficiency of the production operations of the business as distinct from the selling and general management areas. A gross loss would usually indicate that the company was selling its products below cost.

Operating profit ratio – also known as the Operating Margin
(profit before interest and tax / turnover) × 100 = %

This ratio is one of the best measures of the efficiency of the operating management of the business and indicates management's ability to generate profits from the business before deducting costs that have nothing to do with operating efficiency.

Collection period or debtor days ratio
(average debtors × no. of days in period) / turnover

This gives an estimate of the number of days between the dates of credit sales and when payment has been received for them. It is a good indicator of the credit trends within the business and of the liquidity of debtors.

Payments period or creditor days ratio
(average creditors × no. of days in period) / cost of sales

This ratio gives an estimate of the number of days credit being taken from the candidate's suppliers. An increase in this period could be an indication of cash flow problems causing the candidate to delay the payment of its creditors. As with the Collection Period, it should first be compared with the period of credit given to ascertain whether the creditors are being stretched and thus likely to put pressure on the business's liquidity.

Inventory period and stock turnover
(stock × no. of days in period)/ cost of sales

This gives an estimate of the number of days' stock in terms of cost of sales, being held in the business. It effectively determines the number of days it takes to convert stock, in all its forms, into cash or debtors. It therefore can give a good indication of the liquidity of the inventory element in current assets. Stock turnover is derived by dividing cost of sales by the average stock of finished goods. If the rate of stock turnover declines, it is longer for stock to be converted into debtors or cash.

Investment ratios

Investment ratios can also be used to assist with the detailed financial appraisal analysis. They are an indicator for assessing future prospects. The principal ratios calculated are:

P/E ratio
market price of share / earnings per share

This is the most important ratio used by the market generally to assess the relative rating of a share and the candidate's prospects. The higher the P/E ratio the higher

the market's rating of the share. It identifies the number of years' earnings needed to cover the current market price of the share. It should not be used to compare suppliers in differing industries.

Earnings yield (inverse of P/E ratio)

Dividend yield
dividend per share / market price of share

This is the actual yield currently available on investment in the share at the current market price.

Asset backing per share
net assets per share

These ratios are usually only applicable to public companies whose shares are traded on the stock market(s).

Industry averages

The table below shows some average industry ratios:

Average ratios: UK industry classifications

Industry classification	Median ratio					
	Acid test	Long term leverage	ROCE	Return on total assets	Collection period (debtor days)	Payments period (creditor days)
Manufacture of computers and other information processing equipment	0.9	1%	25%	6%	51 days	24 days
Software consultancy and supply	1.2	-	267%	133%	18 days	-
Data processing (FM services)	1.0	-	90%	43%	28 days	-
Business and management consultancy activities	1.1	-	84%	24%	18 days	-
Telecommunications	1.0	-	63%	14%	25 days	4 days
General construction of buildings and civil engineering works	0.9	4%	28%	9%	20 days	12 days
Labour recruitment and provision of personnel	1.1	-	48%	13%	45 days	3 days

Summary of ratios

The following summary table shows the grouping of the principal ratios and how they should be calculated

Principal ratios: reference table

Area of assessment	Ratio	Calculation
Financial structure		
Liquidity	Acid test or quick ratio	(current assets – stock) / current liabilities
Gearing	Long term leverage ratio	(long-term debt / net worth) × 100 = %
	Bank leverage ratio	(bank debt / net worth) × 100 = %
Interest payments	Interest cover	Operating profit / interest charges
Operating performance		
Efficiency	ROCE or primary ratio	(operating profit / capital employed) × 100 = %
	Return on total assets	(operating profit / total assets) × 100 = %
Profit margins	Gross profit ratio or gross margin	(sales less cost of sales / turnover) × 100 = %
	Operating profit ratio or operating margin	(profit before interest and tax / turnover) × 100 = %
Debtors	Collection period or debtor days ratio	(average debtors × no. of days in period) / turnover
Creditors	Payments period or creditor days ratio	(average creditors × no. of days in period) / cost of sales
Stock	Inventory period and stock turnover	(stock × no. of days in period) / cost of sales
Investment		
Future prospects	P/E ratio	Market price of share/earnings per share
	Earnings yield	Inverse of P/E Ratio
	Dividend yield	Dividend per share / market price of share

Annex C
Financial glossary

abbreviated accounts — See modified accounts.

acquisition — The members of the acquired company relinquish ownership because the company cannot compete, or raise sufficient capital, or because the shareholders are offered an attractive price for their shares. The acquired company may be merged with the acquiring company, or it may continue to trade as a separate legal entity as a subsidiary of the acquiring company.

adjusting events — Events which provide additional evidence relating to conditions existing at the balance sheet date. For example, if a debtor has become insolvent after the balance sheet date, the valuation of debtors in the financial statements will be revised.

amortisation — Another term for depreciation of intangible assets.

ASB — Accounting Standards Board, which issues accounting standards and is recognised for that purpose under the Companies Act 1985. These standards apply to all companies and other entities that prepare accounts that are intended to provide a true and fair view. **http://www.asb.org.uk**

associated company — A company is an associated company to another if it acts as a partner to the other in a joint venture, or has significant equity voting rights in the other (i.e. not less than 20%).

balance sheet — A balance sheet is a statement which shows the financial position of an organisation at a point in time. It is a snapshot picture of assets and liabilities (usually) in terms of historical cost.

bonus share issues — A company's Share Premium account is used to finance the issue of bonus shares to existing shareholders. The issue of bonus shares may be a sign that prospects for the company are good. Conversely, the issue of bonus shares may be considered to be an alternative method of maintaining shareholder confidence than the payment of dividends during periods of adverse cash flow.

book value — See net book value.

capital employed — The aggregate of shareholders funds and long term debt.

capital expenditure — Fixed assets such as land and buildings, motor vehicles and office equipment not bought for resale.

capitalised	This is when costs are treated as an asset in the balance sheet and written off over a number of accounting periods, instead of treated as expenditure in the period in which the cost is incurred. Such costs will be written off by either depreciation (tangible assets) or amortisation (intangible assets).
chairman's report	A statement of company policy and future prospects from the chairman that is presented with the published accounts. It also helps to build a picture of how the directors feel about the period under review. The statement tends to be a personal and subjective view of the company.
consolidated accounts	Where a parent or holding company owns over 50% of the shares of others, or is in a position to exert control, the annual report and accounts of the parent company will include two levels of balance sheets. These will be the balance sheet of the parent company itself, and a consolidated balance sheet showing the combined totals of all the subsidiaries. The only figure which is certain to be the same on both the parent and consolidated balance sheets, will be the issued capital.
convertible loan stock	An unsecured debt instrument convertible into equity at the option of the holder under specific terms and conditions. It is used for strengthening the capital structure of the business.
creditors	Suppliers and others to whom money is owed.
current assets	Assets which the company intends to consume, turn into cash, or sell in the normal cause of business, usually within twelve months of the date of the balance sheet. They usually include stocks and work in progress, cash in hand and at bank, and debtors.
current liabilities	Liabilities which fall due for payment within a year from the date of the balance sheet and include bank overdraft, trade creditors, taxation, and dividends which have not yet been paid.
debenture	A debenture is a document which acknowledges a debt. It is usually secured on the assets of the company and repayable at some date in the future. The date of redemption is shown against the debenture on the balance sheet and, where a company can redeem at any time between two dates, both dates will be shown.
deferred liability	Some grants are set up as deferred liabilities in the balance sheet, rather than passing through the Profit & Loss in the year of receipt. A proportion can then be passed through the Profit & Loss account each year over the expected useful life of the asset to which the grant relates.

dividends, plcs	Public limited companies, plcs, can only pay a dividend if, after payment, net assets are equal to or greater than the total of issued share capital plus undistributable reserves.
draft accounts	These are provisional accounts or just the balance sheet that may appear at any stage before they are made final. It may be some months before the draft becomes final because of delays in agreeing items such as tax adjustments and directors remunerations. However, final accounts usually vary only marginally from the draft figures.
EBIT	Earnings Before Interest and Taxes, i.e. net profit before all interest payments and tax.
equity capital	Equity (or share) capital provides the basis of the company's capital structure. It should be sufficient to absorb any normal trading loss. The cost of financing equity capital in the dividend yield necessary to induce investment in the company. See share capital.
equity finance, types	There are four types of equity, finance: ordinary shares, preference shares, redeemable shares and reserves. Ordinary shares carry full rights to participate in controlling the business through voting at general meetings and sharing in profits. Preference shares carry no voting rights but holders receive dividends at a specified rate before the ordinary shareholder. Redeemable fully paid ordinary and preference shares can be issued and redeemed at a premium out of distributed profits or new issue proceeds. Reserves consist of retained earnings or profit not distributed to shareholders.
exceptional items	Items derived from transactions or events that fall within the ordinary activities of the company and need to be disclosed separately by virtue of their size or incidence, if the financial statements are to give a true and fair view. For example, rationalisation costs relating to continuing activities. These items pass through the Profit & Loss account above the line, i.e. they are deducted in arriving at net profit before tax and taken to reserves.
extraordinary items	Items derived from transactions or events that fall outside the normal or ordinary activities of the company and which are both material and expected not to recur regularly. For example, reorganisation costs associated with discontinuance of a significant part of the business. These items are shown in the Profit & Loss account net of taxation; they are not deducted in arriving at net profit before tax. Ultimately, these are taken to reserves under total recognised gains and losses.
final (or certified) accounts	These are the final figures, presented as the report and accounts, signed by the principal directors. Their purpose is for issue to the shareholders 14 days before the annual general meeting. They consolidate the most reliable of all the variations

of balance sheet, though the reader should always look at the auditors report to see if there are any reservations or qualifications about the way the directors have presented the figures.

financial risk	The risk associated with debt. It arises from the prior call which debt has on the cash flow of a business irrespective of the level of profit. Debt usually carries rights to confiscate assets and / or force liquidation.
fixed assets	Fixed assets are used in the conduct of business and not with the intention of reselling in the normal course of business. Fixed assets are valued, in the majority of balance sheets, at cost less aggregate depreciation to date.
gearing	The same as leverage. Refers to the extent to which costs have been financed by borrowing. A company is said to be highly geared when it has a high ratio of borrowing to shareholders funds.
goodwill	The difference between the value of the business as a whole and the fair value of its separable net assets. Purchased goodwill must be capitalised and amortised over time. Only purchased goodwill can be shown on the balance sheet.
holding company	A holding company usually has a number of operating subsidiaries. It owns either all or the majority of shares of the subsidiaries. In some cases the parent or holding company is a non-trading entity and simply holds the investments in the subsidiaries, many of which can be trading in different countries with their own subsidiaries. The parent / holding company of a vast group could comprise merely an office with a few legal and financial staff. The shareholders of the holding company must receive 'group accounts' which includes a single set of consolidated accounts for the group.
leverage	See gearing.
liabilities, current	Liabilities which fall due for payment within a year from the date of the balance sheet and include bank overdraft, trade creditors, taxation, and dividends which have not yet been paid.
liabilities, long-term	Financial obligations which must be paid by the company beyond the next accounting period. Long term liabilities represent long term loans and debentures.
liquidation	Where a company, unable to pay off debts as and when they become due, is forced to stop operations and be wound up. Creditors may apply for an order from the Courts which may grant a liquidation order or one for administration / receivership. Also, the directors may seek a voluntary liquidation of a company, and the DTI also has powers to seek a winding up of a company.

liquidity	The ability of a company to pay amounts owing as they fall due for payment; a measure of the degree to which current assets can be used to pay off current debt. Refer also to the definition of solvency.
long term debt	See liabilities, long-term.
long term loan capital	Long term loans which must be paid 12 months or more after the date of the balance sheet.
merger	Where the total operations and assets of two companies are merged by placing them under the control of a new company under one management but jointly owned by the shareholders of the original companies.
modified accounts	Produced by 'small' or 'medium' size companies. All companies must file their accounts with the Registrar of Companies. However, companies defined as small or medium size need only send abbreviated information to the Registrar.
net assets	Total assets less total liabilities. Some accountants refer to a firm as being solvent if total assets exceed total liabilities.
net book value	The value of fixed assets in the books found by deducting all the depreciation charged to date from the original cost of the asset.
net current assets	See working capital.
net income	See net profit.
net margin	Net profit as a percentage of sales. The net margin indicates the profitability of sales after taking account of normal operating expenses.
net profit (or loss)	The residual after expenses have been deducted from gross profit over a period of time.
net worth	The realistic true net asset value of a company after all adjustments have been allowed for. It is equivalent to the sum of original capital subscribed, and accumulated retained earnings i.e. reserves less intangible fixed assets. (This is not usually the value the company would realise if sold as a going concern).
non-adjusting events	An event, relevant to the accounts, that had not taken place before or at the balance sheet date. It does not result in changes to the amounts in the financial statements. However, the event may need to be noted. Examples of this type of event are a government announcement or an act of God. See adjusting events.

notes to the accounts	A supplementary set of statements providing further details of items in the Profit & Loss account and balance sheet. This is a requirement of the Companies Act. The notes will also disclose the major accounting policies adopted by the company (e.g. whether rentals under operating leases are charged to the Profit & Loss account on a straight line basis) and any significant changes in accounting policies.
operating profit	Profit net of selling and administration expenses, but before interest and tax.
overtrading	Overtrading arises when a company expands to such an extent that its capital base is insufficient to support the additional activity either directly or through increased borrowing. Hence it is important that a company has an appropriate capital structure; the correct mix of debt, equity and liquid funds.
preference shares	A preference share, under the terms of issue normally laid down in the company's Articles of Association, is a claim to an annual dividend at a specified rate out of the profits before anything is paid to the ordinary shareholders. The shares also carry preference for the return of capital if the company is wound up, but only to the extent of the par value of the shares.
private limited company	A registered company with limited liability which cannot offer its shares to the public. Ownership is usually confined to a small circle of investors. The transfer of shares only occurs with the consent of existing shareholders.
Profit & Loss account	Shows the results of operations in terms of profitability over a period of time, usually the company's accounting year. It is also referred to as the income statement and basically includes details of sales revenue less the cost of sales and the components of that cost, gross profit, expenses, profit before tax, and net profit.
provisions	Provisions are charges for known liabilities of an unknown amount made before arriving at profit.
public limited company	A public limited company may offer shares to the public. It must be a company limited by shares or guarantee, with a minimum issued share capital and have a Memorandum which states that it is a registered plc.
qualified audit report	If an auditor has reservations in relation to matters concerning the accounts then he should qualify the report. All the reasons for the qualification should be given, together with a quantification of its effect, if possible. Audit reports are qualified where there is uncertainty which prevents the auditor from forming an opinion on a matter, or where the auditor's view conflicts with the view given in the financial statements. Auditors are in a fairly strong position to get their point of view accepted by the directors.

ratio analysis	Ratios are useful for analysing the adequacy or otherwise of a company's efficiency over a period and its financial stability at the end of that period. However, they cannot be used in isolation; they should be regarded as comparative tools. The comparisons which should be made are: • with other years for the same company to show any trend; • with other businesses of a similar type. All relevant factors must be considered before any conclusions are arrived at. These factors will include the effects of inflation and the social/economic conditions prevailing.
report of the auditors	The Companies Act requires that auditors report to shareholders, as distinct from directors, on whether the financial statements show a true and fair view and whether they comply with the provisions of the Act. They must also form an opinion on whether proper books have been kept and that the accounts are in agreement with the books. The auditors are appointed by the shareholders of the AGM on the recommendation of the directors. See also qualified audit report.
report of the directors	Included in the company's annual report and provides a review of the development and prospects of the business and also information concerning important events occurring after the financial year end. It also includes information on acquisition of the company's own shares and sometimes information concerning R & D activity.
reserves	An element of shareholders funds. Reserves can be either capital reserves or revenue reserves and are profits or surpluses which have not been distributed as dividend. Capital reserves are not available for distribution as dividend and may include the increase resulting from a revaluation of fixed assets and a share premium account (which shows the amount by which the issue price of shares exceeded their face value).
retained profit	Profits retained in the business (not distributed), forming part of the company's reserves. Accumulated retained profits are shown as a capital component in the balance sheet. Retained profit can be transferred back to the Profit & Loss account and made available for distribution as dividend. Some companies do this to maintain a dividend during a bad trading year.
revenue	Usually refers to the sales income of the business.
Rights Issue	The most common way for companies with existing public issues to raise new equity capital. Rights Issues are new shares offered to existing shareholders. It is

normally required that any new issue of shares should first be offered to the existing shareholders unless there is specific permission granted by the shareholders to allow up to 10% of share capital to be offered to outsiders. The Rights Issue enables existing shareholders to subscribe for shares in proportion to their existing holdings.

share capital The main types are nominal, issued and called-up capital. Nominal (or authorised) capital is set out in the company's Memorandum which states the division of the authorised capital into fixed amounts. Issued capital is that part of authorised capital issued by the company. Called- up capital applies where shares are partly paid and represents that part of issued capital which has been called-up for payment.

share capital, classes A company's Memorandum of Association may divide the share capital into classes and the rights attaching to each class is recorded in the Articles of Association.

See equity finance, types.

share premium account When a company issues shares at incorporation it will normally do so at their par or nominal value which represents the legal liability attaching to the share. If the company's prospects are good, then the directors may wish to issue additional shares at a premium particularly where the share market price exceeds the par value. A company usually raises further capital with a Rights Issue to existing shareholders. The issue price will be set at a price below the current market value. The premium received is taken to a share premium account and classified under capital reserves in subsequent balance sheets. The share premium represents the difference between the face value of the shares and the sums actually raised when they were sold to the shareholders.

shareholders funds Shareholders funds consist of the company's share capital and reserves.

solvency Solvency is the ability of the firm (a) to pay off its current debt i.e. current liabilities as and when they become due; and (b) to maintain total assets in excess of total liabilities. A company is technically insolvent when its liabilities exceed its assets. The only justification for a company to continue to trade in this situation is when the management knows that the position is temporary and is certain to be retrieved.

subsidiary company Where all or the majority of a company's shares are owned by a holding or parent company.

take-over Where one company takes control over another by acquiring a majority interest in its voting share capital. This is usually deemed to be anything over 50%.

working capital

Working capital, or net current assets, is the excess of current assets over current liabilities (creditors due in less than one year). If a company has insufficient working capital and cannot meet its liabilities, it becomes insolvent.

Further information

Contacting the SIS

Telephone: 01603 704680
e-mail: sis@ogc.gsi.gov.uk

About OGC

OGC – the UK Office of Government Commerce – is an office of HM Treasury.

OGC Service Desk

OGC customers can contact the central OGC Service Desk about all aspects of OGC business. The Service Desk will also channel queries to the appropriate second-line support. We look forward to hearing from you.

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