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ASSESSING TRADING TRUSTS

SCCB Contract 0702055 - Provision of Financial Assessment Services

It is not legally possible to enter into a contract with a trust. However, it is common practice to enter into a contract with a trustee company acting as the trustee of a trust.

A trustee can be a company or an individual. Sometimes a company is incorporated for the sole purpose of acting as trustee for a trust. A trustee company can also undertake other activities if it so chooses.

When a trustee's activities are confined to acting solely as a trustee, the trustee company does not generally prepare its own financial statements because it does not trade. Rather, the company is most likely to supply the financial statements of the trust for which it is a trustee.

For example, the financial statements provided by a tenderer may be headed *Company A Pty Ltd as trustee for the ABC Family Trust*. The financial statements themselves will be trust accounts and relates to the activities of the trading trust.

It is recommend that Contract Managers determine their Agency's policies regarding dealing with trusts and trustee companies when encountering this issue.

"Equity transformed to debt" and "substance over form"

At financial year-end Trusts generally distribute their entire net income to their beneficiaries. In some cases the beneficiaries subsequently loan all or some of the funds back to the trust, thereby transforming equity (i.e. retained profits) into debt (i.e. loans from beneficiaries). As a result of this transaction trading trusts often fail to met the required financial criteria applied in an assessment. To address this issue, it is not unreasonable to treat beneficiaries loans as retained profits instead of liabilities. So, while in form, the beneficiaries' loans take the legal form of debt, in substance the loans may be taken to represent profits or quasi-equity. Kingsway's reports address this in the Executive Summary. For more information about this subject, feel free to contact our office.

