



Accounting and Auditing of Trusts (and Underlying Companies)

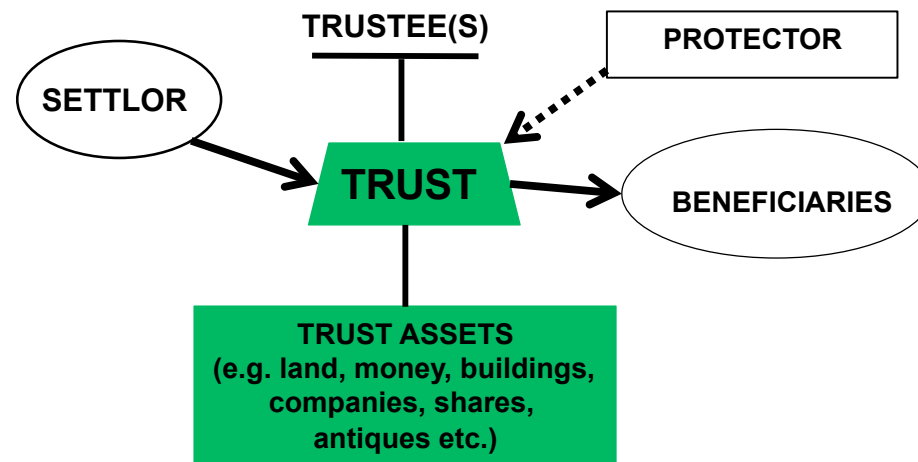
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What is a Trust?

- **Definition**

A relationship created at the direction of an individual (the “Settlor”), in which one (or more) person(s) (the “Trustee(s)”) hold the individual's property (the “Trust Assets”) subject to certain duties to use and protect for the ultimate benefit of others (the “Beneficiaries”).



What is the purpose of a Trust?

- **Trusts may be set up for a number of reasons:**
 - Asset protection / maintenance
 - Succession planning
 - Tax planning
 - Estate planning
 - For the benefit of charities and/or institutions

Is Trust Accounting Necessary?

- Trends show that more Trustees are now preparing accounts
- Trust accounting: A necessity or a luxury?
 - Legal / statutory obligations?
 - Avoidable cost? Cost today v. cost tomorrow
 - Duty to account is a fundamental duty of stewardship
 - Beneficiaries (including minors/unborns?), co-trustee, court...
 - Bank Statements are not financial accounts
 - How can you manage a trust as trustees if you do not have up-to-date financial information?

Consequences of Not Doing Accounting

- **Distributions**
 - Do you know exactly what you CAN distribute?
 - Income v capital distributions
- **Loss of historical knowledge**
 - Changes in trustees/personnel
 - **Potentially erroneous tax (and other compliance) filings**
 - **Acting for an insolvent trust / company**
 - **Cost today v cost tomorrow**

Still with me?



Are you sure?



Sets of Accounts: Contents

- **Synopsis**
- **Accountant's / Auditor's Report**
- **Balance Sheet** - Trustees to sign and date
- **Capital and Income Account (s)**
- **Accumulation Account (s)** - Where separate from capital account
- **Investment Schedule** – Income, Capital gains/losses
- **Notes**
 - Contingent liabilities / assets - book at nominal value of 1 (or 0)
- **See STEP Accounting Guidelines: Appendices**

Accounting Policies: No GAAP

- **No GAAP for trusts because of the private nature of trusts**
 - Currently no authoritative pronouncement from IASB, FASB etc
 - Settlor has wide discretion in establishing the terms
 - Can “choose” a recognised GAAP (e.g. IFRS) but costs
 - No public filing....
 - Tailor to financial literacy of the users – i.e. not too much detail

Accounting Policies: Basic Concepts

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- **The basic rules of trust accounts preparation**
 - **Going Concern, Consistency, Prudence**
 - **Accruals Concept**
 - Exception: Record income when received (cash accounting)
 - Some tax authorities work on cash basis
 - **Compliance with the Trust Deed!**
 - Accumulation of income; apportionment of expenses between capital and income; payment of income to life beneficiary, etc

Accounting Policies : Accounts v Tax Figures

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- **Most likely different → 2 sets of numbers**
 - Tax principles do not equal accounting principles
 - For example: UK: QRBS; 31 March 1982 CGT base cost v historical cost; depreciation v capital allowances
 - Accumulated income being used to purchase new investments
 - Multiple tax regimes for multinational families
- **Accounts can produce base figures for tax returns**
 - Detailed investment schedules
- **Choice of date of year-end of accounts**

Methods

- **Historical Cost Method**

- May wish to book a market value reduction provision (either on balance sheet, or through capital account) or add market value as a note
- STEP Guidelines: historical cost for assets other than available-for-sale (AFS) assets

- **Market Value Method**

- Commercial reality - clear view of trust value
- Subjective? Costly?
- Better assessment for trustees before making a decision
- STEP Guidelines: AFS assets at MV

Anyone still with me?



We're (almost) finished!



Audits of Trusts: An Obligation or a Right?

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- No statutory requirement to audit a trust
- Right / obligation in trust deed?
- Trustees Act 1925 s22(4) provided for trustees to get an audit every 3 years
- Costs charged to the trust
- Difficulty of 3 years re opening balances
- Generally, no statutory audit requirements in IFCs for SPVs.
- Does your auditor understand trusts?

Questions



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APPENDIX - Examples of Legal Requirements

- **Trusts**
 - Example, Jersey: “A trustee shall keep accurate accounts and records of the trustee’s trusteeship”
- **Underlying Companies**
 - Example, BVI: “...must keep records sufficient to show and explain the companies transactions and which will, at any time, enable the financial position of the company to be determined”

APPENDIX - Income v Capital Account (1)

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- **Capital**
 - Assets received and gains/losses thereon
 - Assets bought upon disposal of a previous asset
- **Income**
 - The regular return produced by an asset
- **Why split income and capital accounts?**
 - Taxation
 - Different interests in income and capital, e.g. life beneficiary

APPENDIX - Income v Capital Account (2)

- **Apportionment of expenses**
 - Review trust deed!
 - Must document any decision made with regard to allocation of expenses
 - Fair and reasonable split
 - Trustee fees: 50% : 50% ?
 - 10-20% income charge?
 - Tax optimisation: discuss with beneficiaries
- **Schedules of income and capital gain in SPV**
 - When distribute up, you know what you're distributing up

APPENDIX - Income v Capital Account (3)

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- **Capital**
 - Investment management fees: capital, per case law
 - Expenses re dealing with disposals: capital
- **Income**
 - Interest on bonds purchase / sale: book to income account
 - Treatment of dividends: book as received: price contains value of next dividend
 - Redecoration expenses

Contact Details

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