INTER *face*

towards promoting accountability

Vol. VI Issue I January - March 2006

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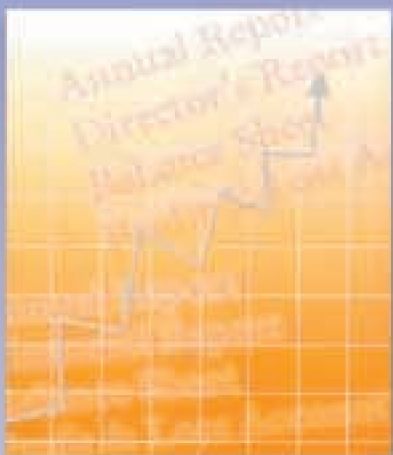

ICAI Awards for Excellence in Financial Reporting

Year 2004-2005

Yet another time!!!

Financial Management Service Foundation has been awarded the "**Gold Shield"** by the Institute of Chartered Accountants of India (ICAI) for "Excellence in Financial Reporting" for the year ended 31st March 2005 for best presented accounts under the "Not-for-profit organizations" Category. The "Gold Shield" was handed over to Mr. Sanjay Patra, the Executive Director of FMSF by the honorable Minister for Company Affairs, Mr. Prem Chand Gupta in a function organized by ICAI on the 2nd February 2006.

The 'ICAI Awards for Excellence in Financial Reporting' propagate that financial reporting should be committed to the canons of accountability, transparency, integrity, reliability and social responsibility. Last year under the not-for-profit organizations category, FMSF had received the 'Copper Plaque'. The 'Gold Shield' received by FMSF this year reaffirms its commitment to the guiding principles of accountability, transparency and social responsibility.

Between Us ....

Actions and Scars

In our interpersonal relationships with people around us, many times, we tend to hurt others and also get hurt by others. Relationships are fragile and therefore, they need to be handled with utmost care. Now–a-days, we have super glue which can join broken pieces and they look like new. But if you look carefully, even after it is joined, there remains a mark reminding us that it has been joined after being broken.

I am reminded of a story of a boy who had a very bad temper. He used to get irritated over small issues. He went to his father for advice as to how to deal with this problem. His father said," Next time when you are angry, take a nail and hammer it on the wall in your bed room." So the boy started doing it. First day, he hammered about 20 nails on the wall. Next day he was more conscious. So he hammered only 14 nails. This exercise continued till he reached a day when he did not need to hammer a single nail on to the wall. He was overjoyed. Finally, he has been able to control his anger fully and his father`s advice had worked. He went to his father and told him about it. His father was also happy for him. Then he gave him another bit of advice. He said "every day you don`t loose your temper anymore; you go to the wall and pull out one nail." The boy started doing it. One after another, the nails came out of the wall. Then a day came when there was not a single nail left on the wall. His father said, "I am very happy for you my son that you have been able to overcome your anger completely. But look at what has happened to the wall in the process. There are so many holes that are left on it. The wall will not be the same again."

A verbal wound is as bad as a physical wound. When we deal with people in anger, we hurt them and in the process leave a scar on their minds; a scar that would remain.........

Letter to the Editor

08/02/06

Sanjay Patra
Publisher, ***INTER face***
Financial Management Service Foundation
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Dear Mr. Patra,

You are kind enough to send me a copy of Interface though I do not believe we subscribe to it.

We appreciate your gesture. We run one of the very few MBA programs in India, which specialize in Rural Management. Your magazine is helpful for our students.

Incidentally, I congratulate you for printing the "Between us -Purpose Driven Leadership" in your Oct - Dec, 2005. It is a masterstroke.

Once again many thanks.

Michael.V.d.Bogaert,sj
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CONTENTS

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Salient Features of the Budget 2006

"Growth is the best antidote to poverty"
- Mr. P. Chidambaram Finance Minister, 28th February 2006.

On 28th February 2006 the Union Finance Minister Mr. P. Chidambaram presented the 2006-07 Union Budget in the Parliament.

The Plan Expenditure for the year is estimated at Rs.1,72,728 crores (17,27,280 million) which has increased by 20.37% from the previous budget. The Finance Minister presented an optimistic budget and claimed that the GDP for the current year would be 8.1% as compared to 7.1% in 2005-06 budget. The contribution of the Manufacturing Sector is estimated to be 9.4%, an increase of 1.3% from the earlier budget. The Agricultural Sector has also shown a steady growth and has bounced to 2.3%.

Salient Features of the Budget with regard to the Social Sector:

- **Bharat Nirman:** The current outlay under this program is Rs.18,696 crores (1,86,960 million) which is an increase by 54% from the previous year's budget allocation.

- **Sarva Siksha Abhiyan:** The Government proclaims that 93% of the children in the age group of 6-14 years are in school. The number of out-of-school children has considerably reduced and the outlay under this program is estimated to increase from Rs.7,156 crores (71,560 million) to Rs.10,041crores (1,00,410 million); an increase of 40.3%.

  The Government also plans to construct 500,000 additional class rooms and will be appointing another 1,50,000 teachers. The education fund - '**Prarambik Siksha Kosh'**-created for funding the program during 2005-06, has been further endowed with Rs.8,746 crore (87,460 million) from the revenues generated through the education cess.

- **Mid- Day Meal**: The allocation to this flagship program has been increased from Rs.3,010 crore (30,100 million) to Rs 4,813 crore (48,130 million).

- **Rajiv Gandhi National Drinking Water Mission:** The allocation has been increased to Rs.4,680 crore (46,800 million) showing an increase of 28.3% in comparison to the previous year.

- **Rural Sanitation Campaign:** The budget allocation for the campaign has been increased by 14.28% amounting to Rs.720 crore (7,200 million).

- **National Rural Health Mission:** The program was launched in April 2005 and has shown good progress. The current budget allocation for the same has been increased to Rs.8,207 crore (82,070 million), showing an increase of 25.24%.

- **Integrated Child Development Scheme:** The world's largest child development program has been showing progress and the budget allocation of the program for the current year is Rs. 4,087 crore (40,870 million).

- **National Rural Employment Guarantee Scheme (NREGS):** NREGS, also referred to as the primary instrument to combat rural unemployment, hunger and poverty has been allocated a total of Rs. 14,300 crore (1,43,000 million). Since there is a legal guarantee of employment under the NREG Act, more funds would be provided according to the need.

- **Jawaharlal Nehru National Urban Renewal Mission:** The program was launched on 3rd December 2005 in selected cities which includes an urban infrastructure development scheme for small and medium towns.Out of the estimated outlay of Rs 6,250 crore (62,500 million),Rs 4,595 crores (45,950 million) has been granted.

- **National Social Assistance Program**: The Government has planned to increase the old age pension to destitutes above the age of 65 years from Rs. 75 per month to Rs. 200 per month showing a remarkable increase by 166.67%.

- **Women and Children:** The statement on gender budgeting has been enlarged to include schemes where 100 per cent of the allocation is for the benefit of women as well as schemes where at least 30 per cent of the allocation is targeted towards women. The outlay of this program is Rs. 28,737 crores (2,87,370 million).

- **Scheduled Castes (SCs) and Scheduled Tribes (STs):** The scheme benefiting only SCs and STs has been enhanced by 14.5% amounting to Rs. 2,902 crore (29,020 million) and the allocations for schemes with at least 20 % allocation for SCs and STs have been enhanced by 13.9% to Rs.9,690 crore (96,900 million).

- **Minorities:** The govt. proposes to increase the financial support to the organizations involved in the welfare of minorities. The corpus fund of the Maulana Azad Educational Foundation has been doubled to Rs.200 crore (2,000 million). The allocation to the National Council for Promotion of Urdu Language has been increased from Rs.10 crore (100 million) to Rs.13 crore (130 million).

- **Kasturba Gandhi Balika Vidyalaya Scheme:** The Government proposes to open another 1,000 new residential schools for girls from SC, ST, OBC and minority communities in 2006-07. The total budget allocation is Rs.172 crore (1,720 million). Further, there is an incentive provided to the girl child who passes the eighth standard and enrolls in a secondary school.

- **Agriculture:** Government's focus is on agriculture. Assured irrigation, credit, diversification and creating a market for agricultural products are the thrust areas.

  - **Irrigation:** The outlay for 2006-07 has been increased to Rs.7,121 crore (71,210 million) and the Central Government will support the programme through a grant of Rs.2,350 crore (23,500 million). The Ministry of Water Resources will revamp the Command Area Development Programme to allow participatory irrigation management through water users' associations**.**

  - **Farm Credit:** Farm credit was increased to Rs.1,25,309 crore (12, 53,090 million) in 2004-05 (well above the target) and is again expected to cross the target of Rs.141,500 crore (14, 15,000 million) set for the current year.

    Banks are encouraged to increase the level of credit to Rs.1,75,000 crore (Rs. 17,50,000 million) in 2006-07 and also add another 50 lakh farmers to their portfolio. Farmers can obtain short-term credit from the co-operative credit structure and Regional Rural Banks (RRBs) with refinance from NABARD. Increasingly, scheduled commercial banks are also lending more to farmers.

- **Micro Finance:** Banking sector to credit-link another 3,85,000 self-help groups (SHGs) in 2006-07. The Government is planning to propose NABARD to open a separate line of credit for financing farm production and investment activities through SHGs.

  Further, with a view to bring more cultivator households within the banking fold, Government will appoint a Committee on Financial Inclusion. The Committee will be asked to identify the reasons for exclusion, and suggest a plan for designing and delivering credit to every household that seeks credit from lending institutions.

  *The Government also plans to introduce a bill which would provide a formal statutory framework for the promotion, development and regulation of the Micro Finance sector***.**

Conclusion: The analysis of the budget shows that the allocation of resources to the Social sector has increased considerably as compared to the last year's budget. However, as always the successful implementation of it is dependent on 'good governance'

NEW

CHANGE IN DIRECT TAXES

Union Budget 2006

Tax on anonymous donations received by NGOs

The Finance Minister while presenting the Budget 2006, on the floor of the house has made the following statement:

"The Standing Committee on Finance has expressed concern that many charitable institutions misuse the provisions of the Income Tax Act. I propose to focus on one misuse, namely, receiving anonymous or pseudonymous donations. Accordingly, I propose that anonymous or pseudonymous donations to wholly charitable institutions will be taxed at the highest marginal rate. Such donations to partly religious and partly charitable institutions/trusts will be taxed only if the donation is specifically for an educational or medical purpose. However, I make it clear that such donations to wholly religious institutions and religious trusts will not be covered by the new provision."

Section 115BBC to Income Tax Act,1961 has been proposed to be inserted. Accordingly, any charitable organization receiving any anonymous donation will be charged tax at maximum marginal rate. On one hand, it seems that the intention of the government is to ensure that all income of NGOs are well established but on the other hand, this measure will adversely affect the sector in terms of resource mobilization. As per the traditions prevailing in India, many times the donors would like to donate without revealing their identity. Similarly, there are donation boxes kept at public places like air ports, shopping centres etc. on behalf of various reputed NGOs. These incomes now it seems will be taxable. Introducing this new section may affect the spirit of voluntarism and raising of resources from within the country.

DEBATE

Space of their Own

A Note on Auditors and their Independence

- Dr. Shailendra Awale

Introduction: For many development workers like me, financial management is a grey area. Therefore, we generally delegate this responsibility to the person who in turn becomes "the most hated person" in the organization for undertaking the unpleasant task of monitoring and managing finances.

Further, auditing is an activity. To speak frankly, many of us would not have liked to have auditing if it had not been a statutory requirement. It is said that auditors are those who fly like a butterfly and sting like a bee. They are most unwanted yet well treated guests. In an earlier organization, where our finance manger used to check, how many cups of tea (yes, tea!) a staff had on tour, used to spread a lavish treat for the auditors. Let me present below few examples which are from my own experience to substantiate further:

1. During the course of the Annual General Meeting (AGM) of a membership based organization, at the time of presentation of audited financial statement, the chairperson requested one member to withdraw from the meeting for the time being. After the above presentation was over, the member was called back to join the meeting. Later, I came to know that the member was the auditor of the organization as well as a board member.

2. While I was undertaking an organizational development process (including setting up financial systems) for a small mission hospital in Jharkhand, it was noted that only the Receipt and Payment Account of the Hospital was audited. On further scrutiny, it was noticed that there were huge liabilities for medical supplies purchased on credit which were never reported. Further, we noted that the auditor of the hospital is also the auditor of all church related organizations as well as tea gardens. He did not have enough capacity to undertake all these audits. Afterwards, we realized that the internal Auditor of the hospital was one of his own staff and the two major medical suppliers to the hospital were his close relatives.

3. I have once come across a situation where an Audit Firm was also acting as a recruitment agency for the position of consultant on health systems management and AIDS program.

Last but not the least, the Enron issue has shaken the very foundation of our reporting processes. For common people like us, audit is a ritual of examination of accounts by an authorized person. They enjoy plenty of well deserved respect. Even though, they may not be fully independent, they are an indispensable part of our society.

In the Voluntary Sector

The voluntary sector has grown considerably in its size and function. Its sheer size and growth requires more professional and systemic interventions. Whatever may be the size of voluntary sector, its very nature calls for greater social accountability. To enhance its social accountability, the fundamental responsibility of any development oriented institution is to ensure normative tools and practices to ensure transparency and accountability. Statutory audit is one such measure while social audit can take the function to higher levels of transparency. Accounting procedures in development sector varies from that of the for-profit enterprises. Cash basis is the preferred method of accounting than accrual basis. Having received funding from foreign sources, reporting to the Ministry of Home Affairs (MHA) & Foreign Contribution Regulation Act (FCRA) authority is mandatory within a time frame. Besides this, there is always a concern as to how to account for certain expenditures. For instance, salary of the program staff should be establishment cost or expenditure towards program. Many Non -Government Organization (NGO) leaders do rightfully expect the auditors to be aware and sensitive towards functioning of voluntary organizations (Indira Dasgupta in INTER*face*). This is not a special concession but a necessary skill required for anyone to join the sector. There is also a need to differentiate between Professional, Not- for- Profit, and Voluntary Development Agency. The last two are people centered and community oriented but unfortunately have to operate on the principles borrowed from market and business management.

Challenges

In post liberalized economy, NGOs are engaged in building collective struggle to protect and enhance rights and interest of the poor. Auditors are also having many newer opportunities for specialized consulting services. This means that fees may be much higher than those normally associated with audit work. Besides, there is stiff competition with emergence of new international firms coming in. NGO leaders do expect auditors to develop appropriate systems ensuring transparency to retain their integrity in a corrupt society. International agencies like Transparency International have ranked India as 83rd among the worst in the world for graft and dishonesty. Mr. C Vittal, former Chief Vigilance Commissioner (CVC) had mentioned Jhola (NGO), Dada (criminals) and Babu; (government officials) as few common parishioners propagating the corruption. NGO sector with due recognition to its work need to accept that all is not well with its accounting systems. Such environment underlines the paramount importance of independent auditors. Among all civil services, Indian Accounts & Audit Service (IAAS) under Comptroller & Auditor General (CAG) enjoys highest reputation for integrity and honesty. Election Commission has also laid a foundation to be an 'independent agency' functioning without fear and prejudice.

The Auditor's relationship with his clients has three primary aspects. They are economic interest (any direct or indirect financial relationship), management of client company (where auditor and the audited are directly or indirectly having same management, control or capital) and third is 'relative' (any connection as a relative or any lineal ascendant or descendent). (Joselyn Martins **INTER** ***face*** Oct-Dec. 2005)

Relationship

Many steps and measures are suggested to ensure independence of auditors. In my opinion most of them are feasible. Rotation of auditor is one such practice. I do subscribe to the view of Mr. Joselyn Martins that it would be the first step to fraud or misuse of the funds. Besides this, we may have to restrict our choice to those who are not adequately competent or largely ignorant about need of the values, work ethics and practices of the voluntary sector.

In fact, there is a need for more interface between auditors and rest of the trustees. Action Taken Report prepared by the Chief Executive need to be taken seriously. Letter of Management prepared by the auditor deserves better attention and treatment. However, there is a necessity to maintain a practice for a disclosure of remuneration of auditors for audit and other services.

Responsibility

To maintain validity and reliability to the process of audit, independence of auditors is important. They need not have any direct and indirect business relationship with the client. At the same time, only economic interest with voluntary sector is not tenable as it will lead to friction. Besides developing special technical skills for specific need of this sector, the auditor needs to have empathetical understanding and appreciation towards their work. There needs to be shared values with an understanding of the vision and organizational process of the development sector. In the process, NGOs should take adequate care to avoid over dependency on auditor and need to take ample steps for self monitoring and regulation. When corporate sector is taking enough steps to ensure constructive governance and appointing independent experts as members, NGO sector is still lagging behind in this aspect.

Conclusion

The subject of independence of auditor is not new. It has been around there for a long time. Debacles like Enron revive these discussions. Independence is ultimately in the minds of the auditor and the audited. Both need to realize that they are accountable to larger community and enhancing integrity is their fundamental responsibility. There is a need to move from the trap of helplessness. Efforts are required to promote values as a culture of the organisation. Auditors should be independent but not indifferent to values and culture of an organization. Collectively we can build a society promoting integrity, honesty and truth. Can we accept the challenge?

(The author is the Chief Co-ordinator of Church of North India - Synodical Board of Social Services, New Delhi. He is a qualified Medical Doctor with rich experience in the development sector.)

DEBATE

Independence of Auditors

- S. Narayanan

Independence, both historically and philosophically, is the foundation of the public accounting profession and upon its maintenance depends the profession's strength and stature. This has gained momentum due to the number of recent, high-profile corporate failures especially in the US which has raised concerns about the accuracy and reliability of a company's financial statements. Ultimately, no law can force us to be good citizens; it has to come from within.

The success of this concept can be achieved by tri-fold action i.e., by effective introduction of various statutes, accounting and reporting guidelines by the respective governing bodies and last but not the least, to sensitize the management and also the professionals who are ultimately responsible for reporting.

I – Statutory Regulations:

In the direction of upholding Independence of Auditors, Sarbanes-Oxley Act 2000 in US was introduced. In Australia, the Australian Institute of Company Directors' (AICD) submission on the Ramsay Report also emphasized the need of independence of auditors through various regulatory measures like extending other services to the corporate by the statutory auditors.

With regard to Indian scenario, the existing rules and regulations are very stringent when compared to other western countries. Most of the provisions of the Sarbanes-Oxley Act have already been covered under the Indian Companies Act and the Indian Accounting Standards issued by the Institute of Chartered Accountants of India (ICAI). The Indian professionals' standards are second to none.

Though not essential, we have been constrained to follow certain rules and regulations to be inline with the international practices due to globalization and liberalization of our economy. Accordingly, Securities & Exchange Board of India (SEBI) has introduced various regulations to protect the interest of the investors like the Accounting Committee, Corporate Governance etc. These are based on the various committees such as Naresh Chandra Committee to evaluate the corporate governance. Much more regulations and restrictions are being implemented for the commercial sector in order to keep the independence of auditors.

The impact of globalization in influencing the rules and regulations in the corporate sector has raised a question whether such a concept of Independence of Auditors should be extended to the NGO sector. The effectiveness of these regulations in the NGO sector need to be considered from the perspective of multi-legislature promulgated by both Central and State Governments. The various statutes governing this sector are Indian Trust Act, Societies Registration Act of the different States, Companies Act, 1956 for those entities registered under Section 25 of this Act. Hence, effective amendments to the respective legislatures are the need of the hour to be in line with the commercial sector with regard to the independence of auditors.

The main areas needing consideration are the accounting committee, NGO Sector governance rules, creation of apex body in order to monitor the NGO's activity, uniformity and transparency in reporting etc.

II – Standardization of Accounting Standards for NGO Sector : Recently, the ICAI has come out with recommendatory guidelines which needs to be fine tuned to suit the nature of activity in NGO Sector.

III – Self-regulation, high ethical and professional standards and sensitization of the management:

The Australian Institute of Company Directors' (AICD) submission on the Ramsay Report, placed before the Treasury states that "Self-regulation through the professional associations of auditors would be a far more effective means of monitoring ethical behaviour and compulsory membership of auditors to these associations should be introduced". They also state that prescriptive legislation will not be the solution unless it is felt and understood by the person concerned. It is more of subjective in nature.

In the context of India, this need not be overemphasized since due to cultural background, the extent of dependence of the clients is more on the auditors than vice-versa. In addition, due to their faith on the professionals, the Indian clients are more closely knitted with the professionals. In fact, in semi-urban areas the clients refer the auditors for every financial transaction. The confidence reposed on the auditors is due to the high standards of professional ethics maintained by the auditors in India.

The independence of auditors in this sector is as good as with other sectors. However, the social responsibility of the auditors in this sector needs to be considered while gauging the independence of the auditors. In any socio-economic project which involves economically poor human beings, understanding the effectiveness of the benefits needs to be taken, into consideration while expressing ones own view on the matter.

With regard to sensitization of the management, the funding agency also plays a very vital role. They have to scrutinize the credibility of the NGO before deciding upon funding. Moreover, the management should also be spread and a committee of social activists should be given the responsibility of management and if the NGO does not fall in line with these parameters the funding agency should abstain from funding those NGOs. It requires auditors to honestly assess operations and not to subordinate their judgment on audit matters to that of others. Auditors should base findings and recommendations on facts rather than impressions and continuously strive to be balanced and fair in carrying out their responsibilities.

In addition to the tri-fold strategy to sustain the independence of auditors, the following area needs to be considered to reach a higher level of independence for the auditors of NGO sector based on the existing practice:

1. A properly qualified and experienced accountant needs to be employed. Most of the time this is missing due to lack of financial resources, especially in the remote areas where trained persons are neither available nor interested to work.

   Suggestions: In order to obviate this lacuna in the NGO, the funding agency can train persons from the beneficiary group itself with the help of the professionals who are willing to impart training to those persons among the beneficiary group. This is neither theoretical nor impractical, since a review of accounts maintained by Self -Help Groups at village level will reveal that village women who are literate with a pass in class 8th or 10th can maintain the accounts meticulously.

2. The auditors of NGO should refrain themselves from doing accounting services. Though prevalent in rural areas, the auditors should restrict themselves to audit services only.

   Suggestions: This can be achieved through regulatory measures by the respective statutes and by advocacy. There are restrictions with regard to the fees, type of work to be performed by the statutory auditors in the commercial sector, whereas those restrictions are absent in this sector. Hence, such restrictions need to be implemented either by respective legislature or by the auditing standards.

3. The Indian Trust Act, Societies Registration Act etc., under which most of the NGOs are formed need to be properly amended so as to ensure the independence of the auditors.

   Suggestion: Under Companies Act, Section 226 (3) (d), if the auditor is indebted to the company for more than Rs.1000/- he or his firm should not continue as auditor of such company since it would affect the independence of the auditor. Section 314 prohibits the appointment of relatives of Directors as auditors of the company. Similar provisions needs to be incorporated under the provisions of the Acts mentioned supra.

4. There is no clear stipulation under these Acts with regard to the purpose of the audit. Under the Companies Act, the auditor has to review the financial statement and state his opinion whether it reflects the true and fair financial position of the organisation. However, the ICAI has suggested the format of audit report for NGO sector but the same has to be supported by the respective statutes.

   Suggestion: Similar regulation needs to be introduced under the above Acts mentioned in sl. no. 3 above.

5. Legislative provision with regard to appointment and removal of auditors and the responsibilities are not considered under the above statutes.

   Suggestions: Necessary provisions need to be introduced to cover the above areas in the respective statutes under which most of the NGOs are functioning.

6. The role of ICAI in this sector is essential in order to govern the high professional standards. Framing and modifying the accounting standards to make them practical and suitable for NGO sector can achieve this.

   Suggestions: The standards issued by the ICAI need to be modified suitably by considering the various types and nature of activities carried out by the NGOs. The scope of the statutory audit be defined as compliance and adherence to the standards of ICAI and not an evaluation of the projects which should be considered as an Investigation or Special Purpose Audit.

7. The management of the NGOs should also be sensitized about the role of auditors. The present attitude of certification of accounts for the purpose of complying with the provisions of Income Tax Act and furnishing the certified copy of the accounts to the Registrar of Societies needs to be changed. NGOs should consider the audit as an evaluation process of their accountability, disclosure and transparency of their activities.

8. The role of funding agencies is also vital since they are the major donors to the NGO sector. They should also understand that the scope of the statutory audit is to ensure the maintenance of proper books of accounts with supporting evidence and that the Balance Sheet shows true and fair position of the financial status of the NGO. The concept of substance over form has its own limitation in statutory audits. The scope of the statutory audit cannot be extended to ensure the reality of the expenditure beyond the supporting evidences produced to the auditors. It is needless to recapitulate that the auditor is only a “watchdog and not the blood hound”. It is the duty of the funding agency to investigate whether the funds donated by them reached the real beneficiary. This has to be carried out by way of special audit and not through the statutory audit. Moreover, the degree of independence will be very high if the special purpose auditor is appointed by the funding agency. It is needless to state that a comparison of the reports, which are based on a different scope, will be a fruitless exercise.

9. Above all, independence is a mind-set and it cannot be achieved by various regulatory measures unless there is an

attitudinal change in the minds of the funding agency, management of NGOs and auditors. This has to come from within and not by enforcement. This can be achieved through the sensitization process and through advocacy by organizations like FMSF.

To conclude, in the present scenario, the results cannot be felt immediately. Nevertheless, a beginning can be made towards attaining the ultimate goal of independence of auditors while executing their attest function and reporting about the financial status of the NGO.

(The author is a practicing Chartered Accountant at Chennai with 15 years of experience in NGO audits)

Risk Management

- A Concept Note

- Sanjay Patra, FMSF

Risks are present in every corner and under every stone. The emergence of risk management as an organized effort is relatively a new trend. The main objective of risk management is to protect the property, earnings and personnel of the organization against losses and legal liabilities that may be incurred due to various risks. It minimizes cost and maximizes the profitability.

Normally, 'risks and risk management' are associated more with businesses and profit making institutions. To many, it may sound strange that even 'not-for-profit' organizations have to manage 'risks'. In the present development scenario, where a lot of emphasis is placed on enhancing the accountability, financial management and reporting of NGOs, information on possible 'risks' that a not-for-profit organization might have to manage will be useful. This concept note on 'Risk Management' is an effort of FMSF in line with the above.

What is Risk?

A risk is a possibility that something different will occur from what is expected. When one decides to take a risk, it is wise to minimize any negative impact and maximize the positive impact. Risk is associated with events whose chances of happening are greater than zero but less than 100 percent.

Voluntary Sector is all about change and it is also true that change brings risk. Therefore, it is important to recognize that the working towards the organizational mission already assumes change and the accompanying risk.

Why manage risk?

Five good reasons to manage risk in voluntary organizations:

- To counter losses
- To seize opportunities
- To reduce uncertainty
- To be responsible to society
- To work towards the mission

Financial Resources in an NGO

Basically, there are three kinds of financial resources in NGOs:

- Money – cash, bank, securities & other investments
- Goods – stock, supplies, equipments etc.
- Services – programmes & activities

Any action which contributes to the reduction in value or loss of any of the organization's financial assets can be termed as a risk.

Few of the common risks faced by Voluntary Organisations

An illustrative list is given below:

- Injury to employees, volunteers, public etc.
- Damage to property
- Employment practices
- Fraud
- Violation of legal requirements

Key Areas of Risk in the Voluntary Sector

- **Governance Risk** – Inappropriate organizational structure, Board members with inadequate skills, conflict of interest.

- **Operational Risk** – Work quality & efficiency, employment issues, health and safety issues, fraud and misappropriation.

- **Financial Risk** – Accuracy & timeliness of financial information, -cash flow, diversifying income sources, investment management.

- **External Risk** – Adverse publicity & public perception, changes in government policy, demographic changes.

- **Compliance Risk** – Violation of legal provisions relating to employment, government etc.

How to manage the Risks?

These risks can be managed in primarily three ways :

- Transferring the financial implications to third parties (e.g insurance, outsourcing etc.)

- Avoiding the activity which gives risc to such risk.

- Precaution and vigilance where such activities cannot be avoided.

Risk Assessment and Management Process

There can be several models that can be used to identify and manage risk. Some of the key stages can include:

i. **Establishing Risk Policy**

Each organization has different capacity to absorb risk. Risk policy means to put in place and maximum limit upto which risks would be taken.

ii. **Identifying Risks and Control**

This process has to be undertaken as an internal management exercise. Key indicators have to be set to identify the risk.

iii. Assessing Risk

After the risk has been

Chance of Happening

High Chance of Happening Low Impact III	High Chance of Happening High Impact IV
Low Chance of Happening Low Impact I	Low Chance of Happening High Impact II

Impact

identified, it has to be assessed. The table below indicates an analysis in this regard.

An organization always has to be prepared for quadrant II and IV since they are high impact zones.

iv. Evaluate action plan on Risk

When the risks are identified, there has to be an action plan of how to manage them. Therefore a clear action plan needs to be decided.

v. Periodical Monitoring and Assessment

Periodic Monitoring and assessment are necessary to understand if the risks identified are still relevant or they have become redundant due to a change in the environment. At the same time there may be new issues which have evolved as risks. These needs to be analyzed and managed. So this needs to be an ongoing process.

Therefore, Risk Management should be actively and continuously promoted throughout the organization to anticipate and mitigate all categories of risks.

Registrar of Societies

- Powers and Duties

- Pooja Bagga, FMSF

The Registrar of Societies is the authority who regulates the Societies registered under the Societies Registration Act, 1860. The Registrar is responsible for enforcing the various provisions of the Act to the registered Societies. There is no specific definition of the Registrar in the Act. However, Section 1 of the Principal Act States that the Memorandum of Association has to be filed with the ***Registrar of Joint Stock Companies*** for getting their Society registered under the Societies Registration Act, 1860. Inference can be drawn from Section 2(40) of the Companies Act 1956 which defines Registrar as a Registrar, an Additional, a Joint, Deputy or an Assistant Registrar having the duty of registering the Companies under the Act.

The Principal Act does not give any definition of the Registrar.However various State Acts have given definition or meaning of Registrar (or as per amendment made by them) in their respective State Acts like:

Goa, Daman and Diu Societies Act states that "Inspector-General" means the Inspector-General of Registration appointed under Sec. 3 of the Indian Registration Act, 1908 (Central Act 16 of 1908) and includes any of the District Authorities subordinate to the Inspector-General of Registration not below the rank of a District Registrar to whom powers may be delegated in respect of this Act.

Respective State Acts of Kerala, **Andhra Pradesh and Punjab** defines 'Inspector-General of Registration' as the Inspector-General of Registration appointed by the State Government under Sec. 3 of the Indian Registration Act, 1908 (Central Act XVI of 1908) or any of the district authorities subordinate to the Inspector-General of Registration not below the rank of the District Registrar to whom powers may be delegated in respect of this Act.

Maharashtra and Gujarat Acts gives the definition under Section 1-B as : Registrar of Societies and Assistant Registrar- The State Government may, by notification in the official Gazette, appoint a person to be called the Registrar of Societies who shall exercise such powers and shall perform such duties and functions as are conferred by or under the provisions of this Act and shall subject to such general or special orders as the State Government may make, superintend the administration and carry out the provisions of this Act throughout the State of Maharashtra.

The State Government may also, by notification, appoint persons to be called "Assistant Registrar of Societies" for such areas as may be specified in the notification and empower them to exercise powers and perform duties and functions under all or such provisions in this Act as may be specified in the notification.

In different States under Section 1, certain amendments have been made and the words 'Registrar of Joint Stock Companies have been substituted by words 'Inspector General of Registration'. For example:

- In respective State Acts of **A.P. (Andhra Area**), **Bihar, Goa, Kerala, Tamil Nadu** the word 'the Registrar of Joint Stock Companies' has been substituted by the words 'the Inspector-General of Registration'.

Similarly in respective State Acts of:

- **Assam, Nagaland, Tripura (U.T.)-** The words "Registrar of Joint Stock Companies' have been substituted by the words "Registrar of Societies appointed by Government".
- **Delhi (U.T.). -** The words 'of Joint Stock Companies' have been substituted by the words 'to be appointed by the Chief Commissioner of Delhi by notification in the official gazette, for carrying out the purposes of the Act'
- **Himachal Pradesh-** The words 'of Joint Stock Companies" have been substituted by the words "to be appointed by the Lieutenant Governor of Himachal Pradesh, by notification in the Himachal Pradesh Gazette, for carrying out the purposes of the Act'
- **Pondicherry**- The words" Registrar of Joint Stock Companies" have been substituted by the words "Registrar of Companies"
- **Punjab**- The words "of Joint Stock Companies "have been substituted by the words "Registrar of Companies to be appointed by the State Government. by notification in the official Gazette, for carrying out the purposes of this Act"
- **Uttar Pradesh-**The words "Registrar of Joint Stock Companies" have been substituted by the words "Registrar".

Appointment of Registrars

Orissa Act gives the provisions for the Appointment of Registrar of Societies, wherein the State Government may, by notification, appoint a person to be called the Registrar of Societies. The appointed person shall exercise such powers and perform such duties and functions which are conferred by or are under the provisions of this Act. Subject to such general or special order, which the State Government may make from time to time, superintend the administration and carry out the provisions of this Act throughout the State.

Also the State Government may, by a notification, appoint one or more Additional Registrars with such local jurisdiction as may be assigned to them by the State Government. The Additional Registrars so appointed shall, subject to the control of the Registrar of Societies, exercise such of the powers and perform such of the functions of the Registrar of Societies as the State Government may authorize in that behalf.

Powers of the Registrar

The Powers of the Registrar are not stated directly in the Principal Act; however various State Acts have made amendments into the Principal Act which brings out certain powers of the Registrar. These powers are:

- **Registration of a Society-** Sec. 3 of the Societies Registration Act, 1860 indirectly states that the Registrar upon the receipt of the Memorandum can certify that the Society is registered upon payment of fees.

- **Certification and Inspection of Documents-** The Registrar may allow inspection of documents at payment of prescribed fees and the inspection can be carried out by any person.

- **Power to call for Information-** Various State provisions say that the Registrar has the powers to call for certain information and explanations regarding various documents, accounts, assets etc., required for the registration of a Society and also after registration of the Society. The Registrar may, under a written order, require any Society to furnish in writing such information or document within such time as specified.

- **Investigation into affairs of the Society**-Certain sections of the State Societies Acts give the powers of the Registrar regarding investigation and inspection of the Society by the Registrar .The Registrar may conduct an investigation or inspection on his own or on the instruction of the State Government for circumstances which may suggest that the business of the Society is being conducted against the objects of the Society. Section 21 of the Pondicherry Act states that every Society shall be inspected atleast once in two years by the Registrar or an officer authorized on behalf of him who shall be entitled to inspect the premises of the Society and shall also be entitled to call for such information or explanation .

- **Cancellation of the registration-** The Registrar may cancel the registration of a Society in cases when :
  - the office of Society has ceased to be in the State of Registration or there is change of office from the State in which the Society is registered.
  - the activities being undertaken by the Society are against the objects of the Society.
  - unlawful activities are being carried out by the Society.
  - the activities undertaken are against the provisions of the Societies Registration Act and other laws of the country.

- **Refuse Registration-** The Registrar may refuse registration of a Society in certain cases when:
  - a Society registered under

Section 17 and if the proposed name is undesirable and may resemble each other and is likely to deceive the public (Sec 18A of Pondicherry Act)

- any of the objects mentioned in the Memorandum to be registered is not covered under the objects specified in the Societies Registration Act.
- the objects are against the laws of the country.

- **Settlement of Disputes**-The Registrar may hold an enquiry on his own or on the request of the members of the Governing Body on the working of the Society.

- **Power to order Audits-** In certain cases the Registrar may order audit of accounts if it is considered necessary in his opinion. The officers of the Society are required to furnish the necessary records as required by the auditor.

- **Removal of the name of the Society from the Registrar in case the Society is dissolved -**The Registrar has the powers to remove the name of the Society if the procedure of the dissolution of the Society has been completed.

- **Disputes regarding the election of office bearers-** The Registrar may refer to the prescribed authority (officer or court authorized in this behalf by the Government by notification published in official gazette) for hearing and deciding the dispute in respect to the election of the office bearers .The Registrar may also call a meeting of the General Body (Section 25 of the UP Act) to be conducted by the Registrar.

- **Compounding of Offences-** The Registrar may accept from any person, against whom reasonable suspicion exists that he has committed any offence punishable under the Act or against whom a prosecution has been instituted, a sum of money by way of composition fee for the offence which the person has been accused to have committed

Serving of Notice by the Registrar:

Section 32 of the UP (Amendment)Act states that any notice, order or requisition meant for the Society which is to be issued by the Registrar may be served on the Secretary of the Society which would imply that the notice has been served on every member of the Society unless the Registrar otherwise directs. The notice may be sent by post at the registered office of the Society.

(With this, we conclude of the series of articles on Societies Registration Act, 1860)

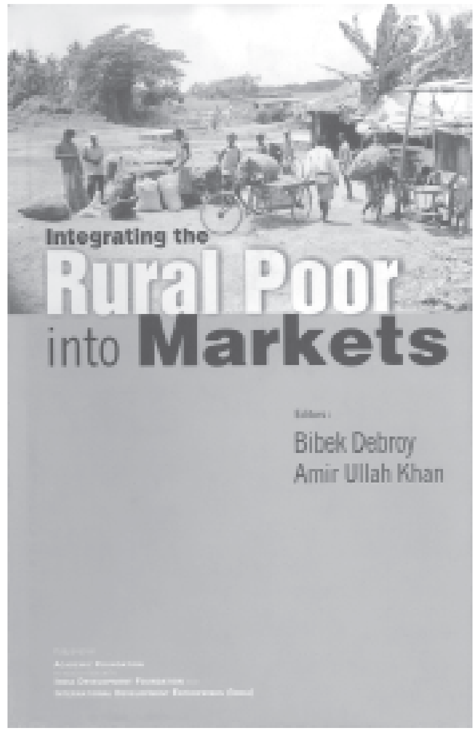
Book Review

Integrating the Rural Poor into Markets

Editors; Bibek Debroy & Amir Ullah Khan. Published by Academic Foundation in association with India Development Foundation & International Development Enterprises (India),

Rs. 695.

The book is a collection of 17 papers authored by experts from diverse backgrounds; 11 of which relate to the various aspects of a revamped agricultural strategy that would result in a marketable surplus in the hands of the rural farmer. Two papers relate to the use of information technology in aid of agricultural productivity, one to the role of genetically modified crops and the remaining three deal with international issues like subsidy to American agriculture, and environmental and phyto-sanitary standards.



The International Development Enterprises India (IDEI) has been experimenting with projects based on an approach called Integrating the Poor into Market Systems (IPMAS) in India aimed mainly at helping the rural poor to produce a marketable surplus of some saleable commodity so that they may first enter the market as sellers, acquire purchasing power, increase consumption and thus rise above the poverty line. Amitabh Sadangi in the very first paper discusses IDEI's approach and interventions of integrating the poor into the market systems. N.C. Saxena's paper 'Agricultural Policy and Rural Poverty Reduction in India' is a sketch of what has happened to agricultural policy and rural poverty in the reform decade of 1990s highlighting the policy failures. Amir Ulla Khan's paper reiterates some of those arguments. The paper 'what ails Indian agriculture?' looks at Indian agriculture from two different perspectives; the institutional and second the technological. S.J.Phansalkar's paper argues that an empowered and informed integration of small holders into markets can lead to significant poverty impacts. Hence, it is desirable to explore and evolve ways of moving towards such an empowered and informed integration into the markets. Rajesh Chakrabarti provides a bird's eye view of the Indian micro finance sector in India. The problem in most of the cases is not lack of entrepreneurship skills but an inability to handle risks. The issue of insurance for the rural poor is often neglected and this is covered by Saleema

Razvi in her paper. With due technological advancements, regulatory issues assume significance. Globally, the issue of genetically modified crops has been a controversial issue and in India, the issue of Bt cotton has been extremely contentious. Shabana Zahoor discusses this contentious issue and the regulatory failure in this regard.

Shaswat Mody's paper discusses United States' agricultural subsidies and their impact on developing countries. Samrat Bose's paper is on the Sanitary & Phyto Sanitary (SPS) agreement while Sujata Ghosh's paper is on organic farming.

The remaining three papers cover different grounds. Information technology can be a promising tool, not only for removing or reducing asymmetry of information but also for improving public governance. Having covered the conceptual issues, Nirvikar Singh discussed some recent IT initiatives. Bibek Debroy's paper is on Information and Communication Technology and its links with poverty. Finally, the Gangopadyaya and Wadhwa Paper set out a formal model for the incidence of child labor and also test it on the basis of empirical data.

The perception in India that liberalization has been anti-poor and pro-rich is largely because the agriculture cum rural sector has been neglected even though it employs almost 70 percent of the population (directly or indirectly). The book attempts at addressing this lacuna. As the name suggests, the book offers a very good idea about what needs to be done to integrate the rural poor into the markets. The one underlying strand that knits the 17 papers together is a belief in "markets (not unregulated) and in a pro-poor focus".

- Madhuchhanda Mishra, FMSF

Foreign Contribution (Management & Control) Bill, 2005
- An Appeal

Dear Readers,

As you all may be aware that the Government of India has released the Draft of the Foreign Contribution (Management & Contribution) Bill [FC(M&C)], 2005, which when passed in the Parliament will replace the existing Foreign Contribution (Regulation) Act, 1976. As the proposed provisions in the FC(M&C) Bill, 2005 raises few practical concerns, we have made an appeal on behalf of the Development Organisations to the Ministry of Home Affairs sharing the same. The content of the letter written by us is provided here.

In case you agree with the points expressed therein, kindly send this appeal letter to :

Shri. Shiv Raj Patil
Ministry of Home Affairs
North Block, Central Secretariat, New Delhi - 110 001.
Ph: 011-23092011; 23092161, Fax: 011- 23093750; 23092763
E-Mail : svpatil@sansad.nic.in

Reg: Foreign Contribution (Management & Control) Bill,2005.

Dear Sir,

We do appreciate that the Foreign Contribution (Management and Control) Bill,2005 has been put in the public domain for reactions and suggestion. Before the Bill is formally introduced in the Parliament, we would like to bring to your notice the following concerns:

- **From Controls to Compliance:** After the liberalization of the economy, Foreign Exchange Regulation Act (FERA) has been replaced by Foreign Exchange Management Act (FEMA).This change brought in simpler procedure for the commercial sector to bring in foreign exchange into the country.

However, in the proposed FC(M&C) Bill,2005, we find that the controls have become even more stringent and it infringes upon the democratic space enjoyed by the Civil Society Organisations in our country. The Voluntary Sector would welcome any accountability mechanism brought in by the Government, but increasing controls would prove to be detrimental to their work and vision which is primarily to serve the poor and marginalized sections of our society. Therefore, we would like to submit that the ethos of the proposed Act be that of a "compliance" mode rather than "controls" mode.

In the light of the above, we would like to bring before you the following concerns for your kind consideration in the FC(M&C) Bill,2005:

- **Fresh Registration: Section 11(1)-Para 2:** The proposed Bill requires existing FCRA registered organisations to seek fresh registration within two years of the commencement of the proposed Act. This will create additional administration load both at the end of the Voluntary Organisations as well as of the Government.

We recommend that existing FCRA registered bodies continue working without seeking fresh registration under the proposed Act. This would imply that the new Act recognizes the existing FCRA registered organisations as registered in the proposed Act as well.

- **Renewing of Registration every five years: Sec 12(7), read with Sec16:** Again the proposed Bill states that the Certificate of Registration will be valid for a period of five years. This will mean that about 30,000 organisations (which are presently registered under FCRA) would have to go through the procedure of renewal every five years. This will again create huge administrative burden. We would like to submit that NGOs work with small budgets and few staff. So they will find it extremely difficult to cope with this new situation.

Therefore, we request you to kindly withdraw this provision so that NGOs can only have one time registration and then comply with the necessary reporting requirements as in practice now.

- **Fixing of Administrative Cost: Section 8 read with Section 47(e) and (f) :** The proposed Bill specifies that not more than 30% of Foreign Contribution shall be used to meet administrative expenses. This clause if implemented would create a lot of confusion and would be open for interpretation which could be quite subjective. The following examples are a case in point:

  (i) In a hospital or dispensary, will the salary cost of the doctors, nurses, ward boys, ambulance driver be termed as programme cost or administrative cost?

  (ii) In an educational institution, will the salary of teachers be programme cost or administrative cost?

  (iii) In cleaning a pond or watershed structure in a village or district, will the labour cost paid be administrative cost or programme cost?

  (iv) In printing of posters for a campaign against HIV/AIDS awareness, is printing and stationery an administration cost or programme cost?

  (v) Telephone/STD calls from Tsunami or disaster affected areas, is it programme cost or administration cost?

Therefore we request you to drop this issue, as NGO funds come generally from donor organizations and are spent on directions from donors as well. Therefore, they allow specifically certain percentages as administrative costs which needs to be adhered to by NGOs in any case.

- **Disposal of Assets: Section 22 read with Sec 47(1) (Y)** The Bill authorizes the Central Government to specify the disposal of assets and the manner in which it can be disposed off. Again, the assets created out of Foreign Contribution can be of two types. The first type are those assets which are created at the community level as part of the project. These assets are not in control of the organization. These are managed and maintained by the beneficiaries. The second types of assets are those which are created for the organization. These assets are used for the purposes of the organization. In both the cases it will be quite complicated if the government determines the manner in which it can be disposed off as the disposal will have to be determined on the basis of its utility. The organization is in the best position to determine the same. Generally, the disposal of these assets are made with the approval of the respective donors.

Therefore, we recommend that this provision may be withdrawn. NGOs may be required to report on the sale proceeds to the Government as they are doing now, in the event of any sale of assets.

The above are a few examples of the various areas of the law which needs to be reconsidered.

We would earnestly request your goodself to kindly make the new law “compliance” oriented rather than “control” based as it is now.

Yours sincerely,
Sd/-

This can also be viewed and down loaded at : http://www.fmsfindia.org/main/fcmc-bill.pdf

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