INTER *face*

towards promoting accountability

Special Focus:

Applicability of Accounting Standards for Not-for-Profit Organisations

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between us . . .

Another world possible !

The woman was in tears. She had come all the way from a far off village. Infact, she was forced to come to a bigger city in search of livelihood. Having come from a poor economic background, with a family of four young children to support and an indifferent husband was making life even more difficult. After moving to the city, she started staying with a family who were her relatives.

Initial days went off well. Her relatives were ironing clothes in front of a multistoried building. She started helping them and everyone was happy. She could rent a small place for herself as well. After a while however, things started becoming difficult. The family started making use of her in their work more and more without adequate financial benefits. One day she reacted and revolted. It was enough to start a big fight. In the process she was beaten up and was threatened with dire consequences. She was back to the same place from where she started.

We always discuss about the rich exploiting the poor. This is a case of less poor exploiting the more poor. Another world would be possible only when exploitation stops at all levels and in all forms. Another world would be possible only when justice, fairness and truth would be the guiding principles in our system. Another world would be possible only when we respect and be sensitive to the environment……….

…….. Let us make that another world possible !

Sanjay Patra

Contents

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"Accountability"
- a development perspective - challenges for NPOs

Rosemary Viswanath
Organisational Development Consultant

I would in this brief paper wish to share some trends and some reflections on the development sector, and the challenges that face it – more as a backdrop to the other more pointed and specific issues this group will address. I believe this backdrop is important in terms of the task of evolving regulatory frameworks and standard practices. Non-profits have basically built on the spirit of service, participation, dialogue and privileged civil society's role in building just and sustainable societies. Regulations are most effective when they aim to strengthen and not merely to control. In that sense, understanding the ethos, realities and spirit of the non-profits is essential to any debate on their accounting and their accountability.

The canvas of non-profits

When addressing the issue of accountability and accounting standards it is important that we understand the nature of the non-profit sector in India, the challenges it faces and the wide variety of spaces it inhabits and roles it attempts to perform.

Some key facts about the spread and nature of the non-profit sector in India comes up with somewhat startling revelations:

- India has 1.18 million NGOs : 53% in rural areas, 47% in urban
- Of the 20 million persons involved, 85% are volunteers, rest are paid staff
- 73.4 % of these have less than one paid staff, 8.5% have above 10 paid staff
- 26.3 % are religious groups

There are two factors that I would like to highlight here – if a large number of organisations are in rural areas, and given the spread of our vast country, one has a huge challenge in terms of communication, access to trained resources and capacity building. Also added to that is the reality of number of full time staff. Valuing the cost of voluntary contribution in economic terms has for long been an unresolved debate. Any attempt at guidelines and standards that are mandatory must take these realities into account. This by no means implies that accountability both as a value or as criteria is inapplicable to non-profits.

Historical Context of NPOs in India

Apart from the spread and variety in the kinds of non-profits, it would be useful to focus also a little more on the history of the kind of non-profits that many of us are involved with (social change, human rights and advocacy) and how these non-profits responded to the needs and issues of their time.

1960-70 : Rehabilitation, Rural Development, Disasters, Displacement

This period (in fact civil society involvement was perhaps at its peak pre-independence and post with the nationalist movement and freedom struggle) focused on very basic issues of development with the vast rural areas of India needing to be included in the development agenda. The **language of rights and obligations**, and in particular the obligations of the state were articulated through the choice of a Nehruvian –socialist- centralist form of government. Gandhian thought and practice also inspired the NPO space.

The 1970's saw the emergency, the event responsible for the political conscientisation of many second-generation NPO activists and leaders today. The realisation that **democracy and civil and political rights** were not given but needed to be guarded and fought for, gave birth to many non-profits working in that broad area.

The 1980's saw the consolidation of and convergence of several vibrant movements - the **environmental** movements - (Chipko), **people's** movements - dalit, tribal, Narmada, fisher folk, and the **women's** movement. The voice of the marginalised claiming their space to define development and not just get their due share was the defining theme. The space occupied by the rights debate expanded to include these concerns as rights. A series of NPOs also addressed these issues.

1990 onwards - saw the spotlight on the **crimes of development** - with the majority of the world people (poor) questioning the current forms of development and its benefits to them. Current economic models, the rules of world trade, neocolonialism, corporate globalisation and its proponents have come under sharp scrutiny and attack, while issues of religious, ethnic, minority rights and identity, localisation & local governance, diversity, sustainability and peace are being keenly debated.

Unfortunately none of the basic issues - poverty, health, basic rights, social justice has been "solved" to any level of satisfaction and have only been exacerbated. And with the passage of time each of these periods has contributed a new layer of complexity and more inter-linkages to existing debates.

The context in which non-profits operate

The wider political and civil society context

There has been an aggressive market led growth of northern capital softened by a stronger civil society concerns in the north itself.

Southern societies face the compulsions of electoral /other politics - the last decade has seen the fragile move to more democratic polities and the ousting of many oppressive dictatorial regimes in Asia and Africa and in eastern Europe and the America. There has been rising aspiration and articulation of the under-classes and much more evident civil society and judicial activism.

NPOs are much more in the public domain - in the media, in decision-making spaces of various hues and in the alternative spaces that they create as a symbolic political statement (e.g. in large WTO meetings or meetings of the governments or multilateral agencies and international financial institutions of the world economic forum etc). Thus being in the public glare is a reality for most and as a result managing public perception has also become an inevitable task of the NPO.

The criticism and scrutiny has also increased correspondingly. NPOs are coming increasingly under pressure to enhance their transparency and accountability – e.g., FCRA and related regulation, and often the pressure (targeting) comes from right wing, partisan organisations intending to quell civil society dissent

Paradigm shifts in development co-operation

Increase in direct aid from northern governments, bilateral, multilateral and international aid agencies (often bypassing northern NPOs) leading to increased state control over funds and a fear of being "co-opted".

There has also been an increase in collaboration between NPOs and the state. NPOs are being relied upon more than governments or commercial interests to "deliver" development (leading to a new breed of "government-ngo!).

While there is a trend particularly in Indian non-profits of shrinking funds – as new priorities and urgencies "divert" funds into areas such as the least developed countries, Africa, and eastern post communist Europe, the reality also is that in real terms the number of NPOs and the funds they work with has almost doubled in the last decade. What is undeniable is that development funds are getting marketised. NPOs need to be efficient and professional in accessing and managing scarce resources as there are competing demands.

What are the demands on and challenges before NGOs?

This makes new demands on NPOs to meet stringent market criteria to access aid, cost-effectiveness, proven organisational and institutional capacity to achieve and monitor results, and have transparent systems of accountability.

However, in order to respond more effectively to these complex issues that they deal with, NPOs have created new forms of organisations – networks, campaigns, clusters and alignments – oftentimes trans-regional, transcontinental, and sometimes virtual. This is a clear shift from the traditional geographically bounded project or implementation mode of non-profits. Managing these new forms of organisation itself is a significant challenge in terms of leadership, managerial and organisational skills. The management of finances becomes a new challenge as well, because many of the earlier assumptions about inflows and outflows and sharing of resources simply do not hold.

Added to this is managing the increasing legal statutory and political and policy space (hurdles) as well as increasingly tight donor requirements.

In order to survive and remain effective, non-profits need to be able to focus on the inside-outside simultaneously. This implies serious and concerted work on:

- The organisation's vision (and its percolation to the rest of the organisation) & practiced values
- Ability to operate in a truly public space
- Financial accountability & transparency
- Work culture aligned with values
- Deliverables in a complex macro-environment
- Leadership
- Professional and management skills in a resource deficit space

Hopefully the debate on accountability will keep in mind these realities and trends while encouraging non-profits to be effective organs of civil society aspirations.

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Accrual Basis of Accounting in NPOs and its implications

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Introduction

Accounting is the discipline which provides financial and other information essential to the efficient conduct and evaluation of the activities of any organisation.

Accounting is the tool for proper financial management. Sound financial management is essential in all organisations - profit or non-profit - where funds are involved. It attempts to use the funds in the most productive manner.

Basis of Accounting

The term 'basis of accounting' refers to the timing of recognition of revenues, expenses, assets and liabilities in accounts. The commonly prevailing bases of accounting are:

a) Cash Basis of Accounting ;

b) Accrual Basis of Accounting; and

c) Mixed Basis of Accounting

Cash Basis of Accounting

Under cash basis of accounting, transactions whether of capital or revenue nature, are recorded when the related cash receipts or cash payments take place.

Thus, revenue (e.g., from donations, grants, etc.) is recognised when cash is collected. Similarly, expenditure on acquisition and maintenance of assets used in rendering of services as well as on employee remuneration and other items is recorded when the related payments take place.

The end-product of cash basis of accounting is a statement of Receipts and Payments that classifies cash receipts and cash payments under different heads.

A statement of assets and liabilities may or may not be prepared.

Accrual Basis of Accounting

Accrual basis of accounting is the method of recording transactions by which revenues, costs, assets and liabilities are reflected in the accounts in the period in which they accrue.

The accrual basis of accounting includes considerations relating to deferral, allocations, depreciation and amortisation.

This basis is also referred to as 'Mercantile Basis of Accounting'.

Accrual basis of accounting attempts to record the financial effects of the transactions and other events of an organisation in the period in which they occur rather than recording them in the period(s) in which cash is received or paid by the organisation.

Accrual basis recognises that the economic events that affect an organisation's performance often do not coincide with the cash receipts and payments.

The goal of accrual basis of accounting is to relate the accomplishments (measured in the form of revenues) and the efforts (measured in terms of costs) so that the reported net income measures an organisation's performance during a period rather than merely listing its cash receipts and payments.

Apart from income measurement, accrual basis of accounting recognises assets, liabilities or components of revenues and expenses for amount received or paid in cash in past and amounts expected to be received or paid in cash in future.

Mixed Basis of Accounting

Mixed basis is also called "modified accrual basis". It combines a mix of both : cash as well as accrual basis.

For example, expenditure may be recognised on accrual basis but income on cash basis or partly on cash and partly on accrual basis. For example, Grant and Donations may be recognised on cash basis whereas rent and interest income on Fixed Deposits may be accounted on accrual basis.

The extent and nature of mixing (cash and accrual) may vary from organisation to organisation which are normally clarified by way of "Notes to Accounts".

Legal Position

The Companies Act, 1956

NPOs registered under Section 25A of the Companies Act, 1956, are required to maintain their books of account on accrual basis and according to the double entry system of accounting (Refer Section 209(3) (b) of the said Act).

If the books are not kept on accrual basis, it shall be deemed as per the provisions of the aforesaid section that proper books of account are not kept.

The Indian Trust Act and The Societies Registration Act, 1860

There is no specific provision with regard to the methods of accounting to be followed by NPOs covered under the aforesaid acts.

Bombay Public Trust Act, 1950

This act is applicable to NPOs registered in Gujarat and Maharashtra.

This Act does not lay down any basis of accounting which should be followed. However, a format of Balance Sheet and Income & Expenditure Account is given in the rules (schedule VIII and IX).

The format shows that both accrual and cash basis is acceptable under the law. Further, accrual basis is mainly considered for rent and interest income.

If accounts are kept on cash basis, then outstanding accrued/due income is shown by way of "Notes to Accounts".

Provisions of Income Tax Act, 1961 relating to Methods of Accounting

Section 145 of the Income Tax Act, 1961 specifies that the income chargeable under the head "Profits and Gains of Business or Profession" or "Income from other Sources" is to be computed in accordance with either cash or accrual system of accounting regularly employed by the assessee (which also includes voluntary organisations). Accordingly, from assessment year 1997-98, all voluntary organisations are required to maintain their books of account either in Cash or Accrual system of accounting on regular basis.

Foreign Contribution (Regulation) Act, 1976

As per the provisions of FCRA and rules framed therein, NPOs are required to submit a statement of Receipt and Payments Account in respect of receipt and utilisation of foreign contributions alongwith a Balance Sheet.

This implies that FCRA recognises Cash Basis of Accounting.

Recommendations of The Institute of Chartered Accountants of India

Accrual is the scientific basis of accounting and has conceptual superiority over the cash basis of accounting. It is, therefore, recommended that all NPOs, including non-company NPOs, should maintain their books of account on accrual basis.

Funding Agencies

Most of the funding agencies primarily require their assisted NPOs to submit a financial statement in a prescribed form or otherwise at periodical intervals to show :

a) the actual receipts ;
b) disbursements ;
c) utilisation of grant amounts ; and
d) unutilised balance.

thereby approving the Cash Basis of Accounting.

Accrual Basis and Accounting Standards

Accounting is often said to be a social science. It operates in an open and ever-changing economic environment.

The nature of transactions entered into by various organisations and the circumstances surrounding such transactions differ widely.

This characteristic of accounting measurements historically led to the adoption of different accounting practices by different organisations for dealing with similar transactions or situations.

Comparability is one of the important qualitative characteristics of accounting information.

This implies that the information should be measured and presented in such a manner that the users are able to compare the information of an organisation through time and with similar information of other organisations.

Adoption of different accounting practices by different organisations for similar transactions or situations tends to reduce the comparability of accounting information.

Recognising the need for bringing about a greater degree of uniformity in accounting measurements, the trend all over the world now is towards :

a) following the accrual basis of accounting;
b) formulation of accounting standards to be adopted in preparation of accounting information and its presentation in financial statements.

Accounting standards lay down the rules for measurement and presentation of accounting information by different organisation.

In India, the task of formulating Accounting Standards has been taken up by The Institute of Chartered Accountants of India.

Accounting Standards issued by the Institute are based on the fundamental accounting assumption of accrual basis of accounting.

These Standards thus reflect what can be construed as proper application of accrual accounting to different types of transactions and events.

Recommendation of ICAI on Applicability of Accounting Standards

As per ICAI, Accounting Standards issued by the Institute do not apply to an NPO if no part of the activity of such entity is commercial, industrial or business in nature. The standards would apply even if a very small proportion of activities is considered to be of commercial, industrial or business in nature.

Treatment of various items of revenue receipts/expenditure under Cash and Accrual Basis of Accounting

Revenue Receipts normally consist of:

* Grants
* Interest on Investments
* Annual Subscriptions
* Donations
* Miscellaneous Receipts

Revenue Expenditure normally consist of:

* Programme Co-ordination
* Administrative Expenditure
* Others
* Depreciation

The treatment of the above major items of revenue receipts and expenditure under cash basis and accrual basis of accounting is as under:

REVENUE RECEIPTS

Particulars	Cash Basis of Accounting	Accrual Basis of Accounting
Grants	on actual receipt basis	on actual receipt basis/ sanction letter
Interest on Investments	on actual receipt basis	on due basis (whether actually received or not).
Annual Subscription	on actual receipt basis	on due basis (whether actually received or not).
Donations	on actual receipt basis	on actual receipt basis
Misc. Receipts	on actual receipt basis	on actual receipt basis

REVENUE PAYMENTS/EXPENDITURE

Particulars	Cash Basis of Accounting	Accrual Basis of Accounting
Programme Expenditure	on actual payment basis	on actual payments plus year end adjustments on accrual / due basis.
Programme Co-ordination Administrative Expenditure (Rent, Salaries, Telephones, Vehicle Running Expenses etc.)	on actual payment basis	on actual payments plus year end adjustments on accrual / due basis.
Others	on actual payment basis	on actual payments plus year end adjustments on accrual / due basis.
Depreciation	normally not charged	charged as per Straight Line/ Written Down Value Method as per Income Tax Rates /on independent assessment basis.

Technical Guide issued by ICAI and Accrual Basis of Accounting

Manoj Fogla
LL.B., M.A. (Phil), F.C.A.

The Institute of Chartered Accountants of India (ICAI) has recently released a "Technical Guide on Accounting and Auditing in Not-for-Profit Organisations". It is for the first time that ICAI has made some substantive efforts towards rationalising the auditing and accounting of the hitherto neglected NPO sector.

The stated objectives of this technical guide are as under:

- To suggest a standardised framework for the preparation and presentation of financial statements of NPOs, so that they are able to meet the common information needs of the various stakeholders. This includes examination of the applicability of existing Accounting Standards, issued by The Institute of Chartered Accountants of India, to such organisations. In this regard, an attempt has also been made to examine the feasibility of :

  a) applying the accrual system of accounting to NPOs;

  b) applying all the Accounting Standards issued by the Institute of Chartered Accountants of India to NPOs;

  c) developing formats of financial statements for NPOs; and

  d) recommending the disclosure of relevant non - financial information in the financial statements of NPOs.

- To provide guidelines on the conduct of audit of NPOs.

The State of Existing Accounting Practices

The current accounting practices are based on the compliances required under various statutes such as Income Tax Act & FC(R)A and therefore there is very little co-herence in accounting practices followed by various NPOs. The following are the characteristics of existing practices.

There is no standard basis of accounting being followed by NPOs. Cash, hybrid, accrual, modified cash/accrual basis of accounting are being followed.

- The Accounting Standards, issued by The Institute of Chartered Accountants of India, are generally not being applied.
- There is lack of uniformity in presentation of financial statements.
- There are different disclosure practices being followed by individual NPOs.

- There is diversity in terminology and accounting policies being adopted.
- The idea of this technical guide is to rationalise the exisiting accounting and financial reporting framework.

Accrual Basis of Accounting

ICAI recommends accrual basis of accounting for NPOs. Accrual basis of accounting is the method of recording transactions by which revenues, costs, assets and liabilities are reflected in the accounts in the period in which they accrue. The accrual basis of accounting includes considerations relating to deferral, allocations, depreciation and amortisation. This basis is also referred to as 'Mercantile Basis of Accounting'.

Accrual basis of accounting attempts to record the financial effects of the transactions and other events of an enterprise in the period in which they occur rather than recording them in the period(s) in which cash is received or paid by the organisation. Accrual basis recognises that the economic events that affect an organisation's performance often do not coincide with the cash receipts and payments. The goal of accrual basis of accounting is to relate the accomplishments (measured in the form of revenues) and the efforts (measured in terms of costs) so that the reported net income measures an organisation's performance during a period rather than merely listing its cash receipts and payments. Apart from income measurement, accrual basis of accounting recognises assets, liabilities or components of revenues and expenses for amounts received or paid in cash in past, and amounts expected to be received or paid in cash in future.

Accrual Basis and Accounting standards

ICAI proposes accrual basis of accounting largely because of the accounting standards which are based on the fundamental accounting assumptions:

- Going concern
- Consistency
- Accrual

To make accounting standards applicable to the NPOs it becomes important that all the above three accounting assumptions are also followed. The application of accrual systems in NPO has its own difficulties and apprehension as mostly NPOs prefer to follow cash basis of accounting.

Applicability of Accounting Standards

The ICAI in 1995 had clarified that their Accounting Standards will not apply to NPOs unless any part of its activity is commercial, industrial or business in nature. The clarification provided by ICAI in 1995 are as under :

"The reference to commercial, industrial or business organisations in the aforesaid paragraph is in the context of the nature of activities carried on by the organisation rather than with reference to its objects. It is quite possible that an organisation has charitable objects but it carries on, either wholly or in part, activities of a commercial, industrial or business nature in furtherance of its objects. The Board believes that Accounting Standards apply in respect of commercial, industrial or business activities of any organisation, irrespective of whether it is profit oriented or is established for charitable or religious purposes. Accounting Standards will not, however, apply to those activities which are not of commercial, industrial or business nature (e.g., an activity of collecting donations and giving them to flood affected people).

It is also clarified that exclusion of an entity from the applicability of the Accounting Standards would be permissible only if no part of the activity of such entity was commercial, industrial or business in nature. For the removal of doubts, it is clarified that even if a very small proportion of the activities of an entity was considered to be commercial, industrial or business in nature, then it could not claim exemption from the application of Accounting Standards. The Accounting Standards would apply to all its activities including those which were not commercial, industrial or business in nature."

Now by virtue of the recent technical guide, ICAI has withdrawn its earlier position and has recommended that NPOs should follow accounting standards even if no part of its activities is commercial, industrial or business in nature. Thus, ICAI has recommended the application of most of the Accounting Standards for NPOs also and therefore, accrual automatically becomes a part of the recommendations made by the ICAI.

Income Tax Accounting Standards

Under Section 145 of the Income Tax Act, an organisation can follow any one of the two methods of accounting i.e. Accrual and Cash Basis of Accounting. Further, the Income Tax Rules has also notified two accounting standards including the Accounting Standard on the "Disclosure of Accounting Policies".

The AS issued by the Income Tax department is similar to the AS of ICAI but, there are some important deviations. The following are the differences between AS1 of ICAI and AS1 of the Income Tax department :

i) The Income Tax AS1, does not apply to the organisation following cash basis of accounting but ICAI AS1, applies to organisations following cash system of accounting also, barring the assumption of accrual basis of accounting.

ii) The consideration of prudence in AS1 provides "In view of the uncertainty attached to future events, profits are not anticipated but recognised only when realised though not necessarily in cash". These words are absent in the discussion regarding prudence in the Income Tax AS1. It means that under the Income-Tax Act profits can be anticipated and recognised even when they are not realised.

Legal Provisions Effecting NPOs:

Under the prevailing laws, even if accrual basis of accounting is made mandatory it may not create any legal compulsion on the part of the NPOs. Accounting Standards are mandatory for the Chartered Accountants and NPOs not complying will invite qualifications in the Audit Report from their Auditor. In this regard the following may be considered :

i) ICAI has recommended that NPOs should adopt accrual basis of accounting as it is a more scientific & rational method, therefore, NPOs should look forward to shifting to accrual basis of accounting, over a period of time. But, as yet, it is only recommendatory in nature.

ii) Irrespective of the Accounting Standards issued by the ICAI, the Income Tax law recognises both methods of accounting. The AS1 issued by the authorities is not applicable to organisations following cash basis of accounting.

iii) There are other confusions as far as Income Tax laws are concerned. Section 145, which specifies the method of accounting, is applicable only to those assessees who has income from business and profession or other sources. In this context, it is worthwhile to note that various heads of Income are specified under Chapter-14 of the Income Tax Act, only to determine the taxable income. But since, the entire income of NPOs is exempted (subject to conditions), it has been held that Chapter-14 is not relevant to the NPOs. Therefore, the income of the NPOs are not required to be determined under various sources of income as the provision of Chapter – 14. They can be determined under various heads but, only as per the principles of commercial accounting.

In such circumstances, even if an NPO has income from the head business & profession, it is not clear, whether Section 145 will be applicable or not. So again, one will have to resort to the normally accepted principles of accounting provided by ICAI.

Issues of Concern :

There is a possibility of misuse of accrual method of accounting and at times it may not be acceptable to the funding agencies. For instance, an organisation can show the utilisation of funds on the basis of outstanding expenses and the funds can remain in the possession of the organisation on the date of certification. In such circumstances, it will depend on the materiality of the amount involved. If the amount remaining outstanding is substantial then the funders may not accept it. Therefore, ICAI should provide NPO specific guidelines and standards.

Similarly, the accrual of project grants is another contentious issue where there is a need for lending a greater clarity. This issue becomes more important when one considers that the Income Tax Accounting

Standards has deleted the words "In view of the uncertainty attached to future events, profits are not anticipated but recognised only when realised though not necessarily in cash."

The difference between the accounting standard issued by ICAI and Income Tax Authority signifies a major shift in principles of accounting and it may be a possible source of complication for NPOs following Accrual Basis of Accounting.

Accounting Standards and its applicability to Non-Profit Organisations

M. Kandasami
F.C.A., D.I.S.A.

International Scenario

World over, professional bodies of accountant have the authority and the obligation to prescribe "Accounting Standards". International Accounting Standards (IASs) are pronounced by the **International Accounting Standards Committee (IASC)**. The IASC was set up in 1973, with headquarters in London (UK) with the following objectives:

a) To **formulate and** publish in the public interest, **accounting standards** to be observed in the presentation of financial statements and to promote their world-wide acceptance and observance; and

b) To work generally for the **improvement and harmonisation** of **regulations,** accounting standards and procedures relating to the presentation of financial statements.

National Scenario

In India, the Institute of Chartered Accountants of India (ICAI) had established in 1977 the **Accounting Standards Board (ASB). ASB** is entrusted with the responsibility of formulating Standards on significant accounting matters, keeping in view (a) international developments as also (b) legal requirements in India.

AS 1 – Disclosure of Accounting Policies

1. Objectives of this standard

To promote better understanding of the financial statements through disclosure of significant accounting policies including the manner.

This standard also helps for meaningful comparison between financial statements of different organisation and different periods of the same organisation.

2. Principles governing Selection of Accounting Policies

- **"Prudence"** - In view of the uncertainty attached to future events, profits are not anticipated but recognised only when realised though not necessarily in cash. Provision is made for all known liabilities and losses even though the amount cannot be determined with certainty and represents only a best estimate in the light of available information.

- **"Substance over Form"** - The accounting treatment and presentation in Financial Statements of transactions and events should be governed by their substance and not merely by the legal form.

- **"Materiality"** - Financial Statements should disclose all "material" items, i.e. items the knowledge of which might influence the decisions of the user of the financial statements.

3. Fundamental Accounting Assumptions

- **"Going Concern"** - The organisation is normally viewed as continuing in operation in the foreseeable future.

- **"Consistency"** - It is assumed that accounting policies are consistent from one period to another.

- **"Accrual"** - Revenues and costs are accrued, that is, recognised as they are earned or incurred (and not as money is received or paid) and recorded in the financial statements of the periods to which they relate.

4. Disclosure requirements of AS-1

- Disclosure of significant policies adopted in the preparation and presentation of financial statements.
- Disclosure of change in accounting policy having a material effect along with the effect of change.
- Disclosure should form part of the financial statement and normally at one place.
- If the fundamental accounting assumption is not followed, the fact should be disclosed.

5. Issues of NPO Sector for AS - 1

Disclosure requirements relating to fundamental assumption :

- **Going concern assumption:**

  - Stoppage of project funds of an NPO funded by a single donor.
  - Society has not renewed its registration under the relevant Societies Act.
  - FCRA Division has banned the NPO from receiving Foreign Contribution and NPO has no local source.
  - Registration under section 12A denied and tax, interest and penalty levied.

- **Consistency assumption:**

  - NPO changing its method of accounting and reporting from non- fund based to fund based.

- **Accrual assumption:**

  - Approved project grant (foreign/ local) (Refer AS-9)
  - Interest on fixed deposits.
  - Salaries.
  - Provident Fund and Gratuity (Refer AS-15)
  - Other disclosure requirements of AS-1
  - Treatment of contingent liabilities.

- **Prudence:**

  - Is it prudent to disclose project funds as surplus in Income & Expenditure Account
  - Substance over form
  - Assets generated for community beneficiaries – treatment in the Balance Sheet

- Revolving Fund - written off as grant by NPO but treated as loan by the SHG/Federation.

- **Materiality:**

  - FCRA Division has initiated an investigation into the affairs of an NPO to transfer the assets to another NPO.
  - Requirement in the project contract to transfer the assets to another NPO

    ✓ Period
    ✓ Valuation of in-kind receipts (e.g. medicines, equipments etc.)
    ✓ Valuation of fixed assets in case of partly funded by foreign contribution and partly by local funds.
    ✓ Assets transferred to another NPO after using it for a project – valuation
    ✓ Disclosure by recipient.
    ✓ Valuation of investments (Refer AS – 14)

- **Contingent Liabilities:**

  Evaluation/project audit funding has resulted in donor claiming return of the project funds.

AS 3 (Revised) – Cash Flow Statements

1. Objective of this standard

- Provides the desired information about historical changes in cash and cash equivalents of an organisation classified into operating, investing, financing activities.
- Provides useful information to the users of financial statements to assess the ability of the organisation to generate cash and cash equivalents and to utilise the cash to needs of the organisation.

2. Classification of activities for the purpose of cash flow statement

Operating activities - Principal revenue producing activities of the organisation.

Investing activities - Acquisition of long term assets and investments

Financing activities - Resulting in changes in size and composition of owner's capital and borrowings of the organisation.

3. Methods of presentation of cash flow statement

Direct method - Major classes of gross cash receipts and cash payments are disclosed

Indirect method - By showing the operating revenues and expenses excluding non-cash items disclosed in the statement of profit and loss and the changes during the period in inventories and operating receivables and payables.

4. Disclosure requirements

- Components of cash and cash equivalents to be disclosed
- Reconciliation of the amounts in cash flow statements with the equivalent items reported in the Balance Sheet

- Significant cash and cash equivalents held by the organisation but not available for use by it along with the commentary by management
- Voluntary disclosures relating to :

  1) undrawn borrowings facilities amount.
  2) aggregate amount of cash flows that represent increases in operating capacity separately from those cash flows that are required to maintain operating capacity.

5. Issues of NPO sector for AS-3

The major heads listed (e.g. proceeds from issue of shares for cash or other considerations etc.) are applicable to for-profit entities only. Hence a separate set of heads relevant to NPOs should be listed in the standard. The classifications namely operating, investing and financing prescribed is relevant to for-profit sector bodies. The classification has to be different for NPOs namely project /programmes and administration, foreign and local funding, Income Generation activities, sustainability income (e.g. income from corpus fund, reserve fund etc.)

AS 4 – Contingencies and events occurring after the Balance Sheet date

1. Objective of this standard

Contingencies:

Following the principle of prudence this standard ensures that all probable losses are provided for and no contingent gains are accounted.

Events occurring after the Balance Sheet date:

Due to timelag between the Balance Sheet date and date of approval, certain events may require either adjustment to the Balance Sheet (e.g. falling prices of the stock, wage dispute settled after the Balance Sheet date, bad debt declared irrecoverable by the court) or disclosure (e.g. fraud or defalcation, major fire in the factory, labour trouble resulting in lock-out)

2. Disclosure requirements

S. No.	Nature of contingency	Treatment
1.	**Contingent loss**	
1.1.	If probable	To be provided
1.2.	If unspecified	To be disclosed
2.	**Contingent Gain**	
2.1.	If recovery certain	To be recognised
2.2.	If not	Not to be recognised

S. No.	Adjusting Events	Non-adjusting events
1.	Falling Prices of Stock	Major fire & Loss
2.	Bad Debts declared irrecoverable by court	Fraud or defalcation
3.	Labour dispute settled after Balance Sheet Date	Labour dispute & Lock out

3. Issues of NPO sector for AS-4

S. No.	Nature of Contingency	Treatment
1.	**Contingent Loss**	
1.1.	If probable : - Income tax demand - Corporation/municipality tax demand - Guarantee given for SHG loans invoked on the NPO by the bank	To be provided
1.2.	If unspecified : - Notice for revision of corporation tax - Donor's recovery action for misuse of funds	To be disclosed
2.	**Contingent Gain**	
2.1.	If recovery certain : - Revision of rent with retrospective effect	To be recognised
2.2.	If not : - Legacy income - Approved Govt. Grant	Not to be recognised

S. No.	Adjusting Events	Non-adjusting events
1.	SHG's taken over by Govt. programmes resulting in loss of revolving fund loans	Defalcation by cashier
2.	Programme staff left the NPO with a huge advance	Dispute among the trustees
3.	Money suit by the contractor against the NPO	

AS 5 (Revised) – Net profit or loss for the period, prior period items and changes in accounting policies

1. Objective of this standard

- To prescribe the classification and disclosure of certain items in Profit and Loss Account to ensure uniformity.
- To enhance the comparability of the financial statements among organisations.

2. Classification of the items for disclosure

1. Ordinary activities
2. Extraordinary items
3. Prior period items
4. Changes in accounting policies
5. Changes in accounting estimates

Classifications of Disclosure Requirements

S. No	Classification	Examples	Disclosure Requirement
1.	Ordinary activities	Writing down of inventories Disposal of fixed assets	Separate disclosure of nature of the item and the amount.
2.	Extraordinary items	Loss due to earthquake Attachment of the property	Separate disclosure of the nature and amount to ensure that impact on current profit or loss can be clearly perceived.
3.	Prior period items	Omission of recording expenses due to over sight Understatement of income due to mathematical mistakes	Separate disclosure of nature and amount to ensure that impact on current profit or loss can be clearly perceived.
4.	Changes in accounting policies	Inventory valuation from weighted average to FIFO. Method of depreciation from Written Down Value to Straight Line Method	Disclose the * Change * Period of Impact and the resulting adjustments in the period of change * If impact not ascertainable, such fact * No material impact in the current period but as a material impact in later periods, fact of change in the year of change
5.	Changes in accounting estimates	Change in the amount of bad debts Change in the useful life of depreciable assets	Disclose in the year of change 1.Nature and amount of change 2.If not practicable to quantify the amount, disclose such fact

Some of the examples stated above will apply to NPOs. In addition, there can be some special issues, which are specific to NPOs such as non-fund to fund based accounting, sale of asset from a funded project and credit to the project fund, etc.

AS 9 – Revenue Recognition

1. Objective of the standard

To lay down certain criteria subject to fulfillment of which the revenue should be recognised.

2. Criterion for revenue recognition

- Sale of goods
- Rendering of services
- Use by others of organisations's resources yielding interest, royalties and dividend

3. Disclosure requirements

- Revenue recognition policy
- Changes in accounting policy and the impact thereof
- Circumstances when revenue recognition has been postponed
- Gross turnover, excise duty and net turnover

4. Issues of NPO Sector for AS - 9

- The overall objective of AS 9 is quite in order for the NPO sector also.
- Does the criteria used by this standard (sale of goods etc.) cover all the revenue categories of NPO sector namely grants from donor agencies for programme, administration, capital assets, income from IGPs?
- Interest from fixed deposits invested for long-term (corpus funds, reserve funds etc.)

AS 12 – Accounting for Govt. Grants

1. Objective of this standard

To prescribe the accounting treatment for Government Grants and the manner in which the disclosure should be made.

2. Disclosure requirements of AS 12

- Accounting policy including the methods of presentation

- Nature and extent of Govt. grants recognised for the financial statements including grants of non-monetary assets given at a concessional rate or free of cost.

3. Issues of NPO sector for AS-12

- AS 12 is an important standard for the NPO sector as many organisations in this sector does receive Govt. grants.

- Although examples mentioned in this standard are for the for-profit sector, the issues covered in this standard significantly affects the NPO sector as well.

- Govt. grants should be recognised only when there is reasonable assurance that the organisation will comply with the conditions attached to them and the grant will be received.

- In the NPO sector, many times there is reasonable assurance of receipt of grants only when it is actually received. In such a situation, what should the NPO do? Should it recognise only when it is received? Will it amount to NPO adopting cash system?

- In the case of grants received for fixed assets, the standard prescribes that the grant should be deducted from the gross value of the asset and depreciate the asset on the net value. Is this an appropriate approach when transparency and accountability is a cry in the NPO sector by the stakeholders.

- When the grant is equal or nearly equal to the cost of the asset, then the asset should be recorded at a nominal value. But it is not clear as to how to determine the nominal value.

AS 15 - Accounting for retirement benefits in the financial statements of employers

1. Objective of this standard

To lay down the accounting treatment and disclosure requirements for retirement benefits.

2. Schemes for which AS 15 is applicable

Provident Fund, Gratuity, Superannuation or Pension and Leave Encashment, Health and Welfare schemes, provided they are defined contribution or benefit scheme.

3. Benefits for which AS 15 does not apply

Those schemes for which the employers obligation cannot be reasonably estimated. (example ad hoc ex-gratia payments on retirement.)

4. Disclosure requirements

Method adopted for determining retirement benefits:

- In the case of defined benefit scheme, when the actuarial valuation was made (at the end of the reporting period or an earlier date)

- If it was done on an earlier date, the date of last actuarial valuation and the method used for determining the accrual for the period if it is not based on the report of an actuarian.

- If there is a change in the actuarial method, the same should be disclosed.

5. Issues of NPO sector for AS - 15

- By and large NPO sector bodies follow cash system by accounting for retirement benefits as and when they pay. This is certainly not the appropriate system.

- If the scheme is operated through a trust, then disclosure should be made about the status of the contribution and the treatment of the same in the accounts.

- Disclosure should be made in the financial statements about the actual situation of the retirement benefits, whether they are provided, funded and invested or whatever is the practice followed.

- The main problem in the NPO sector is that many are not paying any benefits especially those, which are already mandatory.

AS 25 - Interim financial reporting

1. Objective of this standard

- To lay down what information should be provided in interim financial reports

- To prescribe the recognition and measurement principles

2. Form and Contents of interim financial statements

Minimum components :

- Condensed Balance Sheet,Profit and Loss Account,Cash Flow statement and selected explanatory notes.
- Basic and diluted EPS to be presented if it is also presented in annual financial statements.
- Should include CFS if the annual financial statement also contain CFS

3. Issues of NPO sector for AS-25

NPOs are often required to submit interim reports to the donors.

Hence this standard is quite important for NPOs.

Conclusion

NPOs should start following Accounting Standards in order to present a true and fair picture of their finances and their state of affairs. Voluntary adoption of the Accounting Standards by the NPOs will demonstrate their commitment of transparency and accountability. The standards should also be made mandatory in order to promote transparency and accountability.

Accounting Standards and its applicability to Non-Profit Organisations

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The Non-Governmental Organisations (NGOs) sector occupies a unique position in the receipt of funds and its utilisation. It is a sector which plays the role of a trustee of funds that are made available to it in its endeavour to serve various stakeholders. NGOs have adopted varied accounting policies as could be easily followed or was understood by them. The central problem has been measuring their performance. In NGOs, 'service' is the objective, which is not as easy to measure or quantify as compared to 'profit'. In this context there has been a long felt need to develop common accounting standards, which can be followed by NGOs. The Institute of Chartered of Accountants of India (Institute) have recently issued a Technical Guide on Accounting and Auditing in Not-for-Profit Organisations (NPOs).

The Institute of Chartered Accountants of India have stated that the accounting standards issued by the Institute from time to time apply to an NPO if any of its activities, no matter how small, is either commercial, industrial or business in nature and would then apply to all the activities of the NPO. These standards are mandatory on the members of the Institute in the performance of their attest functions (para 3.31).

In issuing the technical guide the Institute has stated that accounting standards contain wholesome principles of accounting. These principles provide the most appropriate guidance even in case of those organisations to which Accounting Standards do not apply. The Institute has (para 3.29) therefore recommended that all NPOs, irrespective of the fact that no part of the activities is commercial, industrial or business in nature, should follow accounting standards issued by the Institute.

NPOs, which are registered under section 25 of the Companies Act 1956 are required to comply with the Accounting Standards by virtue of section 211(3A) of the said Act. Section 227(3)(d) of the Companies Act requires the Auditor to state whether the Income and Expenditure Account and Balance Sheet comply with the Accounting Standards referred to u/s 211(3C). Deviations to the Accounting Standards have to be disclosed together with reasons for it and the financial effect, if any, arising from such deviation {Sec 211(3B)}.

In respect of recommendatory Accounting Standards, the duty of members of the Institute is to examine whether the recommendations made in the Standard have been followed in the presentation of financial statements covered by their audit. If the same have not been followed, the members have to consider whether, keeping in view the circumstances of the case, a disclosure in the audit report is necessary. In other words, they have to exercise their professional judgment to determine whether the departures from the recommendatory Accounting Standards are justified under the circumstances or not (para 3.32).

The Institute has issued various Accounting Standards and the standards that are normally applicable to an NPO are discussed below:

1. Accounting Standards Applicable To Charitable Institutions

1.1 The following accounting standards would normally be applicable to NPOs:

S. No.	Number of the Accounting Standard (AS)	Title of the Accounting Standard	Date from which mandatory (accounting periods commencing on or after)	Applicability
1	AS 1	Disclosure of Accounting Policies	01.04.1991 for companies governed by the Companies Act, 1956. From 1.4.93 for all other organisations.	For all organisations
2	AS 2 (Revised 1999)	Valuation of Inventories.	01.04.1999	For all organisations
3	AS 4 (Revised 1995)	Contingencies and Events Occurring after the Balance Sheet Date	01.04.1995	For all organisations
4	AS 5 (Revised 1997)	Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies	01.04.1996	For all organisations
5	AS 6 (Revised 1994)	Depreciation	01.04.1995	For all organisations
6	AS 7(Revised)	Accounting for Construction Contracts	As in case of AS 1 above and contracts entered into during accounting periods commencing on or after 01.04.2003	For all organisations

S. No.	Number of the Accounting Standard (AS)	Title of the Accounting Standard	Date from which mandatory (accounting periods commencing on or after)	Applicability
7	AS 8	Accounting for Research & Development	As in case of AS 1 above and will be withdrawn from 01.04.2004 as AS - 26 will come in effect from that date	For all organisations.
8	AS 9	Revenue Recognition	As in case of AS 1 above	For all organisations.
9	AS 10	Accounting for Fixed Assets	As in case of AS 1 above	For all organisations.
10	AS 11 (Revised 1994)	Accounting of the Effects of Changes in Foreign Exchange Rates	01.04.1995 & (Revised 2003). AS 11 will be mandatory from accounting periods commencing on or after 01.04.2004	For all organisations. (except in respect of forward exchange transactions entered into by authorised exchange dealers)
11	AS 12	Accounting for Government Grants	01.04.1994	For all organisations.
12	AS 13	Accounting for Investments	01.04.1995	For all organisations.
13	AS 14	Accounting for Amalgamations	01.04.1995	For all organisations.
14	AS 15	Accounting for Retirement Benefits in the Financial Statements of Employers	01.04.1995	For all organisations.
15	AS 16	Borrowing Costs	01.04.2000	For all organisations.
16	AS 19	Leases	In respect of all assets leased during accounting periods commencing on or after 01.04.2001	For all organisations.

S. No.	Number of the Accounting Standard (AS)	Title of the Accounting Standard	Date from which mandatory (accounting periods commencing on or after)	Applicability
17	AS 21	Consolidated Financial statements	01.04.2001	For all organisations.
18	AS 22	Accounting for Taxes on Income	01.04.2002 for Unlisted Companies and from 01.04.2003 for all other organisations	For all organisations.
19	AS 24	Discontinuing Operations	01.04.2004 for organisations having turnover over Rs. 50 crores & from 01.04.2005 for others	For all organisations w.e.f. 01.04.2005.
20	AS 25	Interim Financial Reporting	01.04.2002	For all organisations.
21	AS 26	Intangible Assets	01.04.2003 for organisations having turnover over Rs. 50 crores & from 01.04.2004 for others	For all organisations w.e.f. 01.04.2004.
22	AS 27	Financial Reporting of Interests in Joint Ventures	01.04.2002	For organisations preparing consolidated financial statements
23	AS 28	Impairment of Assets	01.04.2004 for organisations having turnover over Rs. 50 crores & from 01.04.2005 for others	For all organisations w.e.f. 01.04.2005

1.2 The other accounting standards issued by the Institute are the following and would apply to NPOs depending on the circumstances:

S. No.	Number of the Accounting Standard (AS)	Title of the Accounting Standard	Date from which mandatory (accounting periods commenc-ing on or after)	Applicability
1	AS 3	Cash Flow Statements	01.04.2001	For organisations whose equity or debt securities are listed on a stock exchange and other organisations, whose turnover exceeds Rs. 50 Crore

S. No.	Number of the Accounting Standard (AS)	Title of the Accounting Standard	Date from which mandatory (accounting periods commencing on or after)	Applicability
2	AS 17	Segment Reporting	01.04.2001	For organisations whose equity or debt securities are listed on a stock exchange and other organisations, whose turnover exceeds Rs. 50 Crore
3	AS 18	Related Party Disclosures	01.04.2001	For organisations whose equity or debt securities are listed on a stock exchange and other organisations, whose turnover exceeds Rs. 50 Crore
4	AS 20	Earnings per Share	01.04.2001	For organisations whose equity or debt securities are listed on a stock exchange to companies required to give information under part IV of Schedule VI
5	AS 23	Accounting for Investments in Associates in Consolidated Financial Statements	01.04.2003	If an organisation presents consolidated financial statements

Accounting Standards that would be normally mandatory to NPOs

2. AS 1 - Disclosure of Accounting Policies

2.1 AS 1 principally requires the disclosure of significant accounting policies and specifies the manner of their disclosure. A clear statement of significant accounting policies followed in preparation and presentation of financial statements is necessary irrespective of the type of entity presenting the financial statements. Accordingly, NPOs should disclose their significant accounting policies. Further, all significant accounting policies should be disclosed at one place.

2.2 The major principles in selecting accounting policies are prudence, substance over form and materiality.

2.3 Going concern, consistency and accrual are the fundamental accounting assumptions for preparing financial statements.

2.4 Where an NPO has followed a basis of accounting other than accrual, a disclosure in this regard should be made.

2.5 An illustrative list of accounting policies that an NPO could disclose is as follows:

- ✓ Method(s) of depreciation.
- ✓ The bases of recognition of major type of expenses and revenue including grants, donations, subscriptions, etc.
- ✓ Accounting for income from and expenditure on specified activities such as research.
- ✓ Conversion or translation of foreign currency (in case of organisations receiving foreign funds).
- ✓ Valuations of Inventories.
- ✓ Valuations of Investments.
- ✓ Treatment of Retirement Benefits.
- ✓ Valuations of Fixed Assets.
- ✓ Treatment of Contingent Liabilities.

3. AS 2 - Valuation of Inventories

3.1 Where an NPO is carrying on any trading / manufacturing activity and has inventories at the year – end that are:

a) held for sale in the ordinary course of business;

b) in the process of production for such sale; or

c) in the form of materials or supplies to be consumed in the production process or in rendering of services;

the inventories should be valued at lower of cost or net realisable value.

3.2 A question may arise as to the applicability of AS 2 in case of those NPOs, where certain items are manufactured or purchased for the purpose of distributing them to beneficiaries either free of cost or at a nominal amount. It is felt that since items are not held for the purpose of sale or in the process of production for such sale or they are not in the form of materials or supplies to be consumed in production process or in rendering of services of commercial, industrial or business nature, such items cannot be considered as inventories within the meaning of AS 2. In view of this, it is replacement cost, if available.

3.3 In certain cases, NPOs may receive items from donor agencies either free of cost or at nominal charge for distribution to beneficiaries or for sale. Some part of these items may remain undistributed / unsold, at year - end. NPOs should disclose market price or estimated net realisable values of such items, lying at the year - end, in the notes to accounts, along with quantitative details.

4. AS 4 - Contingencies & Events Occurring After Balance Sheet Date

4.1 Contingency is a condition or situation, the ultimate outcome, gain or loss will depend on the occurrence or non-occurrence of one or more uncertain future events. The contingent loss should be provided for if a reasonable estimate of the amount can be made. Contingent gains should not be recognised in the financial statements.

4.2 Events occurring after the Balance Sheet date are those significant events both favourable and unfavourable, that occur between the balance sheet date and the date the accounts are approved by the Board of Directors or Governing Body.

4.3 The principles laid down in AS 4 are applicable irrespective of the type of the entity. Accordingly, they should be complied with in their entirety by NPOs. The reference to the report of board of directors made in AS 4 may be constructed, in the context of NPOs, to a comprehensive periodic report of the governing body by the NPO, eg.: the trustees, on the functioning of the NPO, during the period.

5. AS 5 - Net Profit / Loss for the Period, Prior Period Items & Changes in Accounting Policies

5.1 This Standard lays down requirements for accounting for prior period items, extraordinary items, changes in accounting policies and changes in accounting estimates in the Income and Expenditure Account so that the user may be able to make meaningful comparisons of performance of the NPO over time and also with other organisations.

6. AS 6 - Depreciation

6.1 Depreciation is an important item of expenses. Under-provisions or over-provisions of depreciation would vitiate the true and fair view presented by the financial statements. Therefore, NPOs should provide depreciation in accordance with the requirements of AS 6.

6.2 In case of donated fixed assets, no depreciation is required to be provided since the assets are required to be recorded at nominal value. It is also argued that no depreciation need to be provided in case of fixed assets which are purchased and are expected to be replaced by donors when the useful life of the assets is over. This argument is not valid because, in accounting, the purpose is to allocate the cost of the fixed asset over its useful life so that the periodic net result of operations of the organisation reflects the use of the fixed asset.

7. AS 7 - Accounting for Construction Contracts

7.1 This Standard applies to contractors. As such, its applicability to NPOs is limited. While the Standard gives an option to contractors for following either the percentage of completion method or the completed contract method, from the viewpoint of a contractee, the recognition of expenditure on various projects should be based on stage of completion of the project. Thus, where in case of an NPO, a building or other such asset is under construction by or on behalf of the NPO, it should recognise it as capital work-in-progress based on the stage of completion rather than recognising the same only when the construction is completed.

8. AS 8 - Accounting for Research and Development

8.1 AS 26, 'Intangible Assets', which, inter alia, deals with treatment of research and development costs, supersedes AS 8, with the effect from the former becoming mandatory. Therefore, NPOs, which carry out research and development activities, should follow AS 26 with regard to accounting for research and development costs, from the date AS 26 becomes mandatory i.e. 1.4.2004.

9. AS 9 - Revenue Recognition

9.1 NPOs should follow the requirements of the Standard in their entirety for recognition of revenue arising from sale of goods, rendering of services, and use by others of organisation resources yielding interest, royalties and dividends.

9.2 In this context, it may be noted that AS 12, 'Accounting for Government Grants' is applicable with regard to accounting for government grants. Principle enunciated in AS 12 would be relevant for accounting for donations / grants and / or other subsidies received from private donors and other agencies. The following table illustrates the applicability of AS 9 and AS 12.

Type of Revenue	**Applicability of AS**
Sale of non-mission related products for income generation.	AS 9
Grants receivable from Government / Foundations / Donor Agencies on basis of duly approved grant letters, specifying the timeframe / guidance for grant accrual.	AS 12
Interest	AS 9
Royalties	AS 9
Dividend from Investments.	AS 9
Donations	AS 12
Revenue from fundraising appeals, events, collections, etc.	AS 9
Research and Development Grants	AS 12

10. AS 10 - Accounting for Fixed Assets

10.1 The principles enunciated in AS 10 regarding accounting for fixed assets would apply equally to NPOs as to other bodies. However, due to the very nature of their structure and operations, NPOs have certain peculiar features which have accounting implications, and these include the following:

Type of Asset	Accounting treatment
Land acquired through purchase	Record at aggregate of purchase price and other incidental costs e.g. registration etc.
Land acquired under compulsory acquisition	In addition to above make allowance for additional compensation if it is probable and can be reasonably estimated.
Land acquired free of cost	Record at nominal value of Re. 1.00 but record in fixed assets register. (Ref. AS 12)
Vested governmant land	As neither ownership vests with NPO nor any economic benefits arising vest with NPO, it should not be considered as an asset.
Land improvements	Cost of fencing, filling etc. should be capitalised as part of cost of land.If superstructure is built, it should be capitalised separately under buildings.
Buildings	Actual cost and other incidental expenses.
Plant and machinery	Include actual costs, transport, installation costs, professional fees.

Type of Asset	Accounting treatment
Other fixed assets – vehicles, furniture & fittings, office equipment	Purchase price and installation costs, transport, freight etc.
Composite fixed assets	If individual prices are known then recorded at such individual prices. If a composite price is paid then allocate to different components on a reasonable basis.
Opening balance at the time of shift to accrual basis	Record assets, which have not been recorded on the basis of a physical verification and reasonable prices. Allowance be made for any defect in the title.

11 AS 11 - Accounting for Effects of Changes in Foreign Exchange Rates

11.1 NPOs may receive donations, etc., in foreign currency. As required under AS 11, such transactions should be initially accounted for at the exchange rate prevalent on the date of transaction. Exchange difference related to amounts receivable arising on account of change in exchange rates should be recognised in the Income and Expenditure Account.

11.2 Foreign exchange transaction other than those relating to receipt of donations in foreign currencies should also be accounted for in the manner as required under AS 11 with an appropriate disclosure in the financial statement, e.g., closing balances are reflected at the closing rate upto which the account has been prepared, with the exchange difference reflected in the Income & Expenditure Account.

12 AS 12 - Accounting for Government Grants

12.1 This standard is one of the most important of the standards, which are applicable to NPOs.

12.2 Accounting treatment for government grants, as prescribed in AS 12, is based on the nature of grants and the purpose for which these are received. Accordingly, NPOs should follow the requirements of AS 12 in their entirety for accounting for government grants and similarly for grants received from other donors.

12.3 Grants, which are subject to the fulfillment of certain conditions, then they should be recognised only when there is there is reasonable assurance that:

(i) NPO will comply with the conditions attached to the grant and

(ii) the donations and grants will be received.

12.4 A mere promise from the government and other donor agencies as to the donation / grant does not provide reasonable assurance that the grant will be received and, therefore does not require its recognition. The NPO should recognise a grant / donation in its financial statements only at the stage it attains reasonable assurance, on the basis of all available evidence, that the grant / donation will be received. If there is no reasonable assurance that donation / grant, or any part of thereof, will be received, recognition of such donation / grant, or part of thereof, should be postponed. However, the fact that collection of donation / grants has been delayed does not necessary mean that reasonable assurance does not exist. The donation / grant, the recognition of which has been postponed as suggested hereto before, should be recognised only in the period in which reasonable assurance is attained that the donation / grant will be received. In some cases, the reasonable assurance will be attained only when cash is actually received. In such case, recognition of donations/ grants on receipt basis does not mean that the NPO has not followed accrual basis of accounting.

12.5 Non – monetary grants, eg., land, building or any other assets (whether fixed or current) received free of cost or at a concessional rate should be recognized at nominal value or actual cost to the NPO.

12.6 Since NPOs receive large volume of grants to meet certain revenue expenses, it is recommended that both the grant (to the extent utilised during the period) and the relevant expense should be disclosed separately in the Income and Expenditure Account.

12.7 Donations /grants received to acquire / construct specified fixed assets should be accounted for in either of the following ways:

(i) grant should be shown in the balance sheet as a deduction from the gross value of the relevant fixed asset. Or

(ii) gross value of the asset should be left undisturbed and where the grant relates to:

(a) non - depreciable assets e.g. land, it should be credited to capital reserve.

(b) non - depreciable assets, subject to fulfillment of certain conditions, then recognise income over the period the conditions are fulfilled and the balance be reflected in the balance sheet as a deferred income balance.

(c) depreciable assets, it should be treated as deferred income which should be recognised in the Income and Expenditure Account by allocating it over the periods and in proportions in which depreciation on the asset concerned is charged.

13. AS 13 - Accounting for Investments

13.1 Current investments (being held for less than one year), should be reflected in the financial statements at lower of cost or fair value.

13.2 Long term investments should be reflected at cost.

13.3 On liquidation of investments, the gain or loss should be reflected in the Income & Expenditure Account.

14. AS 14 - Accounting for Amalgamations

14.1 Amalgamations and mergers are not common among NPOs, however if it does happen , then the standard should be followed.

15. AS 15 - Accounting for Retirement Benefits

15.1 The cost of providing retirement benefits to employees should be allocated to periods during which the services are rendered by the employees. These will arise through a defined contribution scheme e.g., contributory Provident Fund or a defined benefit scheme e.g., pension or gratuity. Accounting for retirement benefit costs on cash basis is not appropriate.

15.2 An appropriate charge to the Income & Expenditure should be made through a provision for accruing liability under a defined benefit scheme. Actual valuations should be obtained for the purpose.

16. AS 16 - Borrowing Costs

16.1 NPOs normally do not borrow funds for carrying out their operations or for acquisitions, construction or production of other assets and, therefore, do not incur any borrowing cost. In case, however, an NPO has incurred any borrowing cost, it should follow the requirements of this Standard in their entirety for accounting for borrowing costs.

16.2 Borrowing costs directly attributable to the acquisition, construction or production of a asset should be capitalised as part of the cost of the asset. Other borrowing costs should be treated as an expense for the period in which they are incurred.

17. AS 19 - Leases

17.1 Lease is an agreement whereby the lessor conveys to the lessee in return for a payment or series of payments the right to use an asset for an agreed time. The standard classifies leases into finance leases and operating leases.

17.2 A finance lease is a lease that transfers substantially all the risks and rewards incident to ownership of an asset to the lessee. At the inception of the lease the lessee should recognise the lease as an asset and a liability. Lease payments should be apportioned between the finance charge and reduction of the liability. The lessor should recognise the assets in the balance sheet as a receivable at an amount equal to the net investment. The income should reflect a constant periodic rate of return.

17.3 If a sale and leaseback transaction results in a finance lease, the excess or deficiency of sale proceeds over the carrying amount should not be recognised as income or loss immediately but be deferred and amortised over the lease term in proportion to the depreciation of the leased asset.

17.4 In operating leases the lessor should present an asset under the fixed assets. The lessee should recognise the expense on a straight line basis over the lease term.

18 AS 21 - Consolidated Financial Statements

18.1 An NPO may control another organisation either through ownership of more than one half voting power or through control over the governing body. If this exists the NPO would be the parent and the other body would be subsidiary. In such cases consolidated financial statements need to be prepared in addition to the financial statements.

18.2 Consolidated financial statements should be prepared on a line by line basis for like items in assets, liabilities, income and expenses. Adjustments are required for cross transactions. Minority interests in the income of the group should be shown separately.

19 AS 22 - Accounting for Taxes on Income

19.1 The requirement of this standard should be followed by NPOs in their entirety. Normally some kinds of exemptions are allowed to NPOs from payment of income tax due to nature of their charitable objects and non-profit motives. Such exemptions allowed to NPOs under Income Tax Act, 1961 could be considered as permanent difference for the purpose of AS 22. Permanent differences are differences between taxable income and accounting income for a period that originate in one period and do not reverse subsequently.

20 AS 24 - Discontinuing Operations

20.1 This standard will be mandatory from 1.4.2005 for organisations having a turnover of less than Rs. 50 crores. Since the information about discontinuing operations would enhance the utility of the information presented in the financial statements, NPOs should present information about discontinuing operation in accordance with requirements of this standard. For the purpose of this standard, each major programme/ project carried on by the NPO may be considered as a separate major line of business.

21 AS 25 - Interim Financial Reporting

21.1 Where an NPO presents interim financial reports, in terms of the requirements of the donors or others or on voluntary basis it should present interim financial report as per the requirements of this standard.

21.2 An interim financial statement report should include, at a minimum the following components, with comparisons with the identical period in the financial year :

(i) Condensed Balance Sheet
(ii) Condensed Income and Expenditure Account
(iii) Condensed Cash Flow Statement
(iv) Selected Explanatory Notes

22. AS 26 - Intangible Assets

22.1 This standard will be mandatory from 1.4.2004 for organisations having a turnover of less than Rs. 50 crores. The standard lays down recognition, measurement and disclosure criteria for various intangible assets, such as computer software, website development costs, research and development expenditure, etc., in a comprehensive manner. The requirement of the standard should be followed by all NPOs in their entirety.

22.2 Intangible assets should be measured initially at cost. No intangible asset arising from research should be recognised. The expenses will be recognised as and when incurred.

22.3 Goodwill generated internally should not be recognised as the cost cannot be reliably measured.

22.4 Intangible asset acquired free of cost or at concessional cost should be accounted for as per AS 12, Accounting for Government Grants.

23 AS 27 - Financial Reporting of Interests in Joint Ventures

23.1 There may be instances where two or more NPOs jointly undertake or fund a certain project or activity which is considered as a jointly controlled operation. Similarly, two or more NPOs may jointly control an asset. In addition, an NPO may also have joint control in a jointly controlled entity with other organisations that may be in any form of organisation. NPOs should report their interests in such joint ventures in separate as well as in the consolidated financial statements (as per AS 21) in accordance with the requirements of this standard.

24 AS 28 - Impairment of Assets

24.1 The objective of AS 28 is to prescribe the procedures that an organisation applies to ensure that its assets are carried at no more than their recoverable amount. An asset is carried at more than its recoverable amount if its carrying amount exceeds the amount to be recovered through use of the asset. If this is the case, the asset is described as impaired and the organisation should recognise the impairment loss. AS 28 also specifies when an organisation should reverse an impairment loss and it prescribes certain disclosures for impaired assets.

24.2 The requirement of this standard should be followed in their entirety by NPOs.

Other Accounting Standards that may not be normally mandatory to NPOs

25. AS 3 - Cash Flow Statements

25.1 This Accounting Standard applies to organisations whose equity or debt securities are listed on a stock exchange and other organisations, whose turnover exceeds Rs. 50 Crore.

25.2 Cash flow statement should report the cash flows during the period classified by operating, investing and financing activites.

25.3 Cash flow from operations should be presented under the direct method or the indirect method.

25.4 Under the direct method, major classes of gross receipts and gross cash payments are disclosed. Under the indirect method the net cash flow from operating activites is determined by adjusting the excess of income or expenditure for the effects of:

(i) changes during the period in inventories and receivables and payables.

(ii) non-cash items such as depreciation, provisions, deferred taxes, unrealised foreign exchange gain / losses.

(iii) All other items which the cash effects investing or financial cash flows.

25.5 Cash flows from investing activites and financing activites should be classified separately.

25.6 Cash flow statements should be prepared by NPOs as it facilitates economic decision making and it should be a part of the financial statements.

26. AS 17 - Segment Reporting

26.1 Organisations whose equity or debt securities are listed on a stock exchange and other organisations, whose turnover exceeds Rs. 50 crore.

26.2 NPOs operating in different geographical locations or involved in different kinds of service delivery programmes / projects, which meet the definitions of 'geographical segment' and 'business segment', should disclose segmental information according to the requirements of this standard. Different programmes / projects carried on by an NPO would normally constitute different business segments for the purpose of this standard, if they meet the definition of 'business segment'.

27. AS 18 - Related Party Disclosures

27.1 Organisations whose equity or debt securities are listed on a stock exchange and other organisations, whose turnover exceeds Rs. 50 crore.

27.2 Without related party disclosures, there is a general presumption that transactions are undertaken at 'arm's length basis', however in reality that may not be true. A related party relationship could have an effect on the financial position and operating results of the reporting organisation. NPOs should disclose the related party relationships and transactions in accordance with the requirements of AS 18. In an NPO, the trustees would be treated as the key management personnel and their relatives would treated as related parties. Relative in relation to an individual, means the spouse, son, daughter, brother, sister, father and mother who may be expected to influence or be influenced by, that individual in his/ her dealings with the reporting organisation.

28 AS 20 - Earnings Per Share

28.1 Since NPOs are not- for-profit oriented organisations, this standard is not likely to be relevant to NPOs.

29. AS 23 - Accounting for Investments in Associates in Consolidated Financial Statements

29.1 NPOs normally do not have investments in Associates, however if such investments are there and consolidated financial statements are prepared as per AS 21, the statements need to be prepared as per the equity method.

29.2 An associate is defined as an organisation in which the investor has significant influence and which is neither a subsidiary nor a joint venture of the investor.

The Accounting Standards are indeed very exhaustive and within each standard there is scope for tremendous discussion. As one begins to implement them, various real life situations will emerge and would have to be addressed on a case to case basis. There are no ready answers or simple solutions in the developing world of finance and accounts and more so in the development sector. Yet indeed these standards do address the concerns of NPOs for coming towards a common yardstick for presentation of their financial statements.

International Accounting Standards for NPOs

Samir Manocha
F.C.A.

Preface to Statements of International Accounting Standards

A. Objectives

a) To formulate and publish in the public interest, accounting standards to be observed in the presentation of financial statements and to promote their worldwide acceptance and observance; and

b) To work generally for the improvement and harmonisation of regulations, accounting standards and procedures relating to the presentation of financial statements.

B. Accounting Standards

1. Within each country, local regulations govern, to a greater or lesser degree, the issue of financial statements.

2. Prior to the formation of International Accounting Standards committee (IASC) there were frequently differences of form and content between the published accounting standards of most countries. One of the objects of IASC is to harmonise as far as possible the diverse accounting standards and accounting policies of different countries.

3. IASC endeavours not to make the International Accounting Standards so complex that they cannot be applied effectively on a worldwide basis.

4. International Accounting Standards do not override the local regulations governing the issue of financial statements in a particular country.

C. The Scope of the Standards

1. International Accounting Standards are not intended to apply to immaterial items.

2. International Accounting Standards apply to Financial Statements of any commercial, industrial or business organisation.

Indian Accounting Standards vis-à-vis International Accounting Standards

ICAI is one of the members of the International Accounting Standards Committee and has agreed to support the objectives of IASC. While formulating the Indian Accounting Standards, the Board gives due consideration to International Accounting Standards and try to integrate them, to the extent possible, in the light of the conditions and practices prevailing in India.

Underlying Assumptions

Accrual Basis

In order to meet their objectives, financial statements are prepared on the accrual basis of accounting. Under this basis, the effects of transactions and other events are recognised when they occur and they are recorded in the accounting records and reported in the financial statements of the periods to which they relate.

Going Concern

The financial statements are normally prepared on the assumption that an organisation is a going concern and will continue in operation for the foreseeable future.

Qualitative Characteristics of Financial Statements

1. Understandability.
2. Relevance
3. Materiality
4. Reliability
5. Faithful Representation
6. Substance over Form
7. Neutrality
8. Prudence
9. Completeness
10. Comparability

Existing International Accounting Standards

IAS 1	-	Presentation of Financial Statements
IAS 2	-	Inventories
IAS 7	-	Cash Flow Statements
IAS 8	-	Net Profit or Loss for the Period, Fundamental Errors and Changes in Accounting Policies
IAS 10	-	Events after the Balance Sheet Date
IAS 11	-	Construction Contracts
IAS 12	-	Income Taxes
IAS 14	-	Segment Reporting
IAS 15	-	Information Reflecting the Effects of Changing Prices
IAS 16	-	Property, Plant & Equipment
IAS 17	-	Leases
IAS 18	**-**	**Revenue**
IAS 19	-	Employee Benefits
IAS 20	**-**	**Accounting for Government Grants and Disclosure of Government Assistance**
IAS 21	-	The Effects of Changes in Foreign Exchange Rates
IAS 22	-	Business Combinations
IAS 23	-	Borrowing Costs
IAS 24	**-**	**Related Party Disclosures**
IAS 26	-	Accounting and Reporting by Retirement Benefit Plans
IAS 27	**-**	**Consolidated Financial Statements and Accounting for Investments in Subsidiaries**
IAS 28	-	Accounting for Investments in Associates

IAS 29	-	Financial Reporting in Hyperinflationary Economies
IAS 30	-	Disclosures in the Financial Statements of Banks and Similar Financial Institutions.
IAS 31	-	Financial Reporting of Interests in Joint Venture
IAS 32	-	Financial Instruments: Disclosure & Presentation
IAS 33	-	Earnings Per Share
IAS 34	-	Interim Financial Reporting
IAS 35	-	Discounting Operations
IAS 36	-	Impairment of Assets
IAS 37	-	Provisions, Contingent Liabilities and Contingent Assets
IAS 38	-	Intangible Assets
IAS 39	-	Financial Instruments: Recognition and Measurement
IAS 40	-	Investment Property
IAS 41	-	Agriculture

The IAS set out in bold have been discussed subsequently in conjunction with US GAAP and Indian Accounting Standards

Not-for-Profit Organisations' Perspective and Issues

Not-for-profit organisations have several characteristics that distinguish them from business organisations. They are :

A) NPOs exist to provide goods and services without the objective of generating profit.

B) The ownership interest of NPO is unlike that of business organisations because the owner cannot remove resources from the entity for personal use or gain.

C) NPOs obtain most resources from others that share its desire to serve a chosen mission and not by conducting exchange transactions as in the case of a business organisation.

Accounting Standards for NPOs

Though there are no specific International Accounting Standards for NPOs, adherence to certain standards would definitely enhance the quality of the Financial Statements of NPOs.

Most International NPOs are following relevant Accounting Standards applicable to their respective countries or International Accounting Standards, to the extent applicable.

The US Generally Accepted Accounting Principles (GAAP) have pronounced certain specific Statements of Financial Accounting Standards (SFAS) for NPOs. They are:

SFAS 93 - Recognition of Depreciation by NPOs

SFAS 116 - Accounting for Contributions Received and Contributions Made.

SFAS 117 - Financial Statements of NPOs.

SFAS 124 - Accounting for certain Investments held by NPOs

SFAS 136 - Transfers of Assets to a NPO or Charitable Trust that raises or holds contributions for others

Statement of Position (SOP)

SOP 94-3 - Reporting of Related Entities

SOP 98-2 - Accounting for Costs of Activities of NPOs and State & Local overnmental Entities that include Fund Raising

The specific SFAS issued by US GAAP for NPOs, read in conjunction with the relevant International Accounting Standards and Indian Accounting Standards are being discussed herein below:

Recognition of Depreciation by NPOs

SFAS 93-Recognition of depreciation by NPOs- requires NPOs to depreciate their long lived assets & to disclose balances for the major classes of assets, depreciation for the period, accumulated depreciation and the organisation's policy for computing depreciation.

IAS 16 Property, Plant and Equipment - Specifies that the depreciable amount of an item of property, plant and equipment should be allocated on a systematic basis over its useful life. The depreciation method used should reflect the pattern in which the asset's economic benefits are consumed by the enterprise. The depreciation charge for each period should be recognised as an expense. Thus, IAS 16 requires the financial statements to disclose, for each class of property, plant and equipment:

- the measurement basis used for determining the gross carrying amount of the assets.
- the depreciation methods used.
- the useful lives or the depreciation rates used.
- the gross carrying amount and the accumulated depreciation at the beginning and end of the period.
- a reconciliation of the carrying amount at the beginning and end of the period

AS 6 - Depreciation Accounting and AS 10 - Accounting for Fixed Assets as prescribed by ICAI is also in line with the International Accounting Standards and specifies similar disclosures.

Applicability to NPO

There is no difficulty in applying the above standard to NPOs. Depreciation is an important item of expense and its non-provision would vitiate the true & fair view of the financial statements. The accounting for Fixed Assets can also be done by NPOs as per the Standard. Peculiar situations with regard to *Properties acquired free of cost, donated properties* have however to be kept in mind while applying the above standard.

Accounting for Contributions Received and Contributions Made.

SFAS 116, Accounting for contributions received and

contributions made requires contributions to be recognised as revenue at the time of the gift and measured at the fair value of the contributed assets regardless of the form of assets contributed. The difference between donor imposed *restrictions* and donor imposed *conditions* have to be kept in mind for timing the recognition of revenue. Whereas the donor imposed restrictions, or the absence of them, do not change the timing of recognition of a contribution, the donor imposed conditions affect the timing of recognition. Donor imposed restrictions affect only a contribution's classification as an increase in permanently restricted net assets, temporarily restricted net assets or unrestricted net assets. A conditional contribution would not be recognised till the condition of the contribution has been met. Unconditional promises to give cash or other assets are recognised in financial statements when the promise is made or received, provided that there is evidence in the form of verifiable documentation.

Volunteer services are recognised in certain circumstances. Contributed services that create or improve a non-financial asset are recognised as revenue either by valuing the hours of service received or by measuring the change in the value of the non-financial asset created or improved.

Gifts received are recognised as revenues and measured at the fair value of assets received.

IAS 18 - Revenue.

The International Accounting Standard IAS 18 is basically applied in accounting for revenue arising from the transactions of:

a) sale of goods
b) rendering of services and
c) the use by others of enterprise assets yielding interest, royalties and dividends.

The above transactions normally do not constitute the activities of NPO as services etc., are not rendered for monetary exchange.

IAS 20 - Accounting for Government Grants and Disclosure of Government Assistance

IAS 20 specifies that Government Grants, including non-monetary grants at fair value, should not be recognised until there is reasonable assurance that:

a) the organisation will comply with the conditions attaching to them; and

b) the grants will be received

Government grants should be recognised as income over the periods necessary to match them with the related costs which they are intended to compensate, on a systematic basis.

AS 9 Revenue Recognition and AS 12 Accounting for Government Grants issued by ICAI are also on similar lines of International Accounting Standards and specifies similar disclosures.

Applicability to NPO

There is limited applicability of the IAS to NPOs. However, the SFAS 116 issued by US GAAP is more specific. The Grants/ contributions from Government agencies, donor agencies can be recognised on the basis of duly approved donor letters in terms of the IAS 12 and SFAS. The interest, royalties, dividend earnings can be recognised in accordance with IAS 18.

Financial Statements of NPOs

SFAS 117, Financial Statements of NPOs, requires all NPOs to present a statement of financial position, a statement of activities, a statement of cash flows, and notes to the financial statements any time it purports to present a complete set of financial statements.In most ways, the content and format of these financial statements are similar to the statements prepared by business enterprises.However, two major differences between NPOs and business enterprises cause differences in the content and format of financial statements. These are:

A) There is no profit motive in the NPO sector, and thus no single indicator of performance comparable to business enterprise's bottom line. In fact, the best indicators of the performance of a NPO are generally not measurable in Rupee terms, though Rupee is the language of financial reporting. All revenues, expenses, gains and losses are reported in a single statement rather than being divided between an income statement and a statement of comprehensive income.

B) NPOs receive contributions, a type of transaction that is without counterpart in business enterprises. Those contributions often have donor-imposed restrictions/ conditions which can affect the types and levels of service that a NPO can offer. Thus the NPOs need to reflect the nature and extent of donor-imposed restrictions and changes in them.

Net Assets and Changes in Net Assets - The nature and extent of donor-imposed restrictions are reported in the statement of financial positions of net assets that are permanently restricted, temporarily restricted, and unrestricted. Separate line items on the face of the statement or details in the notes to financial statements are used to meet the requirement to disclose the amounts for different types of permanent and temporary restrictions.

Reporting Revenues - Revenues are reported in the statement of activities as increases in unrestricted net assets unless the use of the resources received is subject to a donor imposed restriction. Revenues from most exchange transactions are classified as unrestricted.

Reporting Expenses - Expenses are recognised in the statement of activities as decreases in unrestricted net assets. Expenses must be reported by functional classification either on the face of the statement of activities or in the notes to financial statements.

IAS 1 Presentation of Financial Statements specifies that this Standard should be applied in the presentation of all general purpose financial statements prepared and presented in accordance with International Accounting Standards. It also states that the Standard uses terminology that is suitable for an enterprise with a profit objective. Non-profit organisations seeking to apply this Standard may need to amend the descriptions used for certain line items in the financial statements and for the financial statements themselves.

Components of Financial Statements (as applicable to NPO):

a) Balance Sheet
b) Income statement
c) Cash flow statement
d) Accounting policies and explanatory notes.

Fair Presentation and Compliance with IAS:

- Financial Statements should present fairly the financial position, financial performance and cash flows of an organisation.
- An organisation whose financial statements comply with IAS should disclose that fact.
- Inappropriate accounting treatments are not rectified either by disclosure of the accounting policies or by notes to accounts.

Accounting Policies: Management should select and apply an organisation's accounting policies so that the financial statements comply with all the requirements of each applicable IAS.

Going Concern: Financial Statements should be prepared on a going concern basis.

Accrual Basis of Accounting: An enterprise should prepare its financial statements, except for cash flow, under the accrual basis of accounting.

Consistency of Presentation : The presentation & classification of items in the financial statements should be retained from one period to the next.

Materiality : Each material item should be presented separately in the statements. Immaterial amounts should be aggregated with amounts of a similar nature & need not be presented separately.

Offsetting : Assets and liabilities/ items of income and expenses should not be offset unless required by another IAS

AS 1, Disclosure of Accounting Policies prescribed by ICAI is applicable to all organisation. It is also on similar lines of IAS 1 as discussed earlier.

Applicability to NPOs

This standard is applicable to all NPOs. All significant accounting policies adopted in preparation and presentation of Financial Statements should be so disclosed so as to promote a better understanding of the financial statements of a NPO and to facilitate a more meaningful comparison between financial statements of different NPOs.

Accounting for certain Investments held by NPOs

SFAS 124, Accounting for certain Investments Held by NPOs, requires investments in equity securities with readily determinable fair values and all debt securities to be reported at fair value. The gains & losses (both realised and unrealised) are to be reported in a NPO's statement of activities.

Investment and endowment funds

Endowment funds generally are established by gifts from donors who desire to provide support for the organisation permanently (a permanently restricted endowment fund) or for a specified period of time (a term endowment fund). The net assets of an endowment fund are classified in accordance with the restrictions placed on the resources by donors, if any. Because a donor can place different restrictions on each source of the net assets (original gift, investment gains and losses, and investment income), each source must be examined separately to achieve the proper classification.

AS 13, Accounting for Investments issued by the ICAI specifies that all enterprises should disclose in their financial statements:

- Current Investments and Long term Investments distinctly
- Investments classified as current investments should be carried at lower of cost and fair value.
- Investments classified as long term investments should be carried at cost.

However, provision for diminution should be made to recognise a decline, other than temporary, in the value of the investments, such reduction being determined and made for each investment individually.

- Classification of investments should disclose, where applicable, investments in:

a) Government or Trust Securities
b) Shares, debentures or bonds
c) Investment properties
d) Others-specifying nature.

- The accounting policies for determination of carrying amount of investments should be disclosed in the financial statements.

Applicability to NPO

The standard should be followed in their entirety by NPOs.

Transfers of Assets to a NPO or Charitable Trust that raises or holds contributions for others

SFAS 136, Transfers of Assets to a NPO or Charitable Trust That Raises or Holds Contributions for Others, establishes standards for transactions in which a donor makes a contribution by using an agent, trustee or intermediary.In general, a recipient organisation reports a liability if it accepts assets from a donor and agrees to use those assets on behalf of or transfers those assets to another organisation or individual specified by the donor. When it subsequently spends the assets on behalf of or transfers the assets, their return, or both to the beneficiary, the NPO reduces the liability it recorded earlier.

Reporting of Related Entities

SOP 94-3, Reporting of Related Entities

Different combinations of control and economic interest determine the appropriate accounting for relationships with other NPOs. Control is defined for purposes of this SOP as the direct or indirect ability to determine the direction of management and policies through ownership, contract, or otherwise.Economic interest is an interest in another entity that exists if

(1) the other entity holds or utilises significant resources that must be used for the purpose of the reporting organisation, either directly or indirectly by producing income or providing services or

(2) the reporting organisation is responsible for the liabilities of the other entity. Depending on control and economic interest between the organisations, consolidation of accounts would be required. Consolidation is not required if control is likely to be temporary. If consolidated statements are not presented, the NPO must disclose the identity of the other organisation, the nature of the relationship, and summarised financial data.

IAS 24, Related Party Disclosures requires the standard to be applied in dealing with related parties. The requirements of this standard apply to the financial statements of each reporting enterprise.

Related Party: Parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial and operating decisions.

Related party transaction: a transfer of resources or obligations between related parties, regardless of whether a price is charged.

Disclosure

- Related party relationships where control exists should be disclosed irrespective of whether there have been transactions between the related parties.

- If there have been transactions between related parties, the reporting enterprise should disclose the nature of the related party relationships as well as types of transactions and the elements of the transactions necessary for an understanding of the financial statements.

- Items of a similar nature may be disclosed in aggregate except when separate disclosure is necessary for a better understanding.

IAS 27, Consolidated Financial Statements and Accounting for Investments in Subsidiaries is to be applied in preparation and presentation of consolidated financial statements for a group of organisations under the control of a parent.

Control (for the purpose of this standard) is the power to govern the financial and operating policies of an organisation so as to obtain benefits from its activities.

Group is a parent and all its subsidiaries.

Consolidated financial statements are the financial statements of a group presented as those of a single organisation.

Consolidated financial statements should be prepared using uniform accounting policies for like transactions and other events in similar circumstances. If it is not practicable to use uniform accounting policies, the fact should be so disclosed together with the proportions of the items to which different accounting policies have been applied.

AS 18 Related Party Disclosure and AS 21 Consolidated Financial Statements issued by ICAI is on similar lines of the IAS discussed above.

Applicability to NPOs

A related party relationship could have an effect on the financial position and operating results of the reporting organisation. NPOs should, therefore, disclose the related party relationships and transactions as required by the Standards.

An NPO may control another organisation either through ownership of more than one-half voting power or through control over governing body of the organisation. In such case, the Standards for Consolidation of Financial Statements may be applicable.

Accounting for Costs of Activities of NPOs that include Fund Raising :

Many NPOs solicit contributions as part of activities that also serve their programme or management and general functions. When a fund raising activity is conducted in conjunction with an activity that serves a program or other support service, the activity is referred to as joint activity.

SOP 98-2, Accounting for Costs of Activities of NPOs that include Fund Raising, establishes standards for reporting the costs of joint activities. It begins with a presumption that the costs of a joint activity should be reported as fund-raising expenses.

Costs of a joint activity should be charged as follows:

Costs identifiable with a particular function should be charged to that function.

- Joint costs should be allocated between fund raising and the appropriate programme or management & general function.Joint costs are the costs of conducting joint activities that are not identifiable with a particular component of the activity. (like salaries, professional fees, printing, postage, telephone etc.)SOP 98-2 requires that the method used to allocate the joint costs be rational & systematic and that it results in a reasonable allocation of costs. The method selected should be applied consistently.

No particular method of allocation is required by the SOP, but three allocation methods are illustrated:

- Physical units method
- Relative direct cost method
- Stand-alone joint-cost-allocation method.

Adequate disclosure requirements for allocating joint costs are necessary.

International Accounting Standards for NPOs

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The importance of financial reporting in the case of Non-Profit Organisations (NPOs) is being felt worldwide. There were times when people felt that accounting standards and standard accounting practices are not applicable for NPOs where the purpose is more people-oriented than profit-oriented. But, many development in the East and also in the West have changed the environment and it is felt in the concept of governance the NPOs should also be atleast equal to others and one of the parameters is financial reporting.

The financial statements produced in one country is being used in other country and hence harmonization of statement of accounts and application of international standard of accounting becomes important. There are certain initial difficulties like differences in the economic, political, legal and cultural environment between the countries. But, developing and applying uniform standard accounting practices may narrow down these differences.

Some of the global accounting harmonisation are:

- International Accounting Standard Board (IASB) – which issues International Accounting Standards (IAS).

- The International Accounting Standards Committee (IASC), a private sector independent body was established in 1973 by professional bodies in the U.S. and 8 other countries. This IASs are high-quality standard that require accounting practices which are acceptable and valuable to the users. They have published 41 standard of accounting which are however not accepted.

- Generally Accepted Accounting Principles (GAAP) includes i) accounting rules, ii) procedures, iii) accounting standards, iv) accepted accounting practices and v) conventions both promulgated and non-promulgated.

- Combination of statements/opinion/ interpretation issued by the following main organisations of US are terms as **US GAAP**.

- Securities and Exchange Commission (SEC) – Ultimate authority to set US Accounting and Financial Reporting Standards. SEC delegated this responsibility with

  - Financial Accounting Standard Board (FASB) – so far issued about 142 statements of financial accounting standards.
  - American Institute of Certified Public Accountants (AICPA).
  - Emerging Issues Task Force (EITF)
  - Interpretations of Financial Accounting Standard Board (FIN) – Implementation and guidance.

A summary and analysis of important accounting pronouncement under IAS, US GAAP, Indian GAAP is presented in the following table:

Subject	IAS No.	Indian GAAP	US GAAP
Presentation of financial statements	IAS 1	AS 1	FAS-117 Financial statements for NPO
Cash flow statements	IAS 7	AS 3	FAS-95
Net profit or loss, fundamental error and changes in accounting policies	IAS 8	AS 5	APB-20 Accounting charges APB-21 Interest on Receivables and payable
Events after balance sheet date	IAS 10	AS 4	FAS-5
Segment reporting	IAS 14	AS 17	FAS-131
Revenue recognition	IAS 18	AS 9	FAS-48
Employee benefits	IAS 19	AS 15	FAS-87
Accounting for government grants	IAS 20	AS 12	
Effects of foreign exchange rates	IAS 21	AS 11	FAS-52
Related party disclosure	IAS 24	AS 18	FAS-57
Interim financial reporting	IAS 34	AS 25	FAS-3

Comparative Position of basic concepts of IAS

	IAS	AS in India	US GAAP
Fixed assets	Fixed assets are carried at historical cost	Fixed assets are carried at historical cost	Fixed assets are carried at historical cost
Depreciation	Depreciation is based on economic useful life of the assets	Depreciation is based on economic useful life of the assets	Depreciation is based on economic useful life of the assets
Revenue recognition	Accrual basis is followed	Accrual basis is followed	Accrual basis is followed

We discuss below certain important summary of FASB.

Summary of Statement NO.117 – FASB

Financial Statements of Not-for-Profit Organisations (Issued 6/93)

Summary

This statement established standards for general-purpose external financial statements provided by a not-for-profit organisation. Its objective is to enhance the relevance, understandability and comparability of financial statements issued by those organisations. It requires that those financial statements provide certain basic information that focuses on the entity as a whole and meets the common needs of external users of those statements.

This statement requires that all not-for-profit organisations provide a statement of financial position, a statement of activities and a statement of cash flows. It requires reporting amounts for the organisation's total assets, liabilities and net assets in a statement of financial position; reporting the change in an organisation's net assets in a statement of activities; and reporting the change in its cash and cash equivalents in a statement of cash flows.

This statement also requires classification of an organisation's net assets and its revenues, expenses, gains, and losses based on the existence or absence of donor-imposed restrictions. It requires that the amounts for each of three classes of net assets-permanently restricted, temporarily restricted and unrestricted-be displayed in a statement of financial position and that the amounts of change in each of those classes of net assets be displayed in a statement of activities.

This statement amends FASB Statement No.95, Statement of Cash Flows, to extend its provisions to NPOs and to expand its description of cash flows from financing activities to include certain donor-restricted cash that must be used for long-term purposes. It also requires that voluntary health and welfare organisations provide a statement of functional expenses that reports expenses by both functional and natural classifications.

Summary of IAS 1

IAS 1 defines overall considerations for financial statements:

- Fair presentation
- Accounting policies
- Going concern
- Accrual basis of accounting
- Consistency of presentation
- Materiality and aggregation
- Off setting
- Comparative information

Four basic financial statements: IAS 1 prescribes the minimum structure and content, including certain information required on the face of the financial statements:

- Balance sheet (current/non-current distinction is not required)
- Income statement (operating/non-operating separation is required)

- Cash flow statement (IAS 7: Cash flow statements sets out the details)
- Statement showing changes in equity.

Other matters addressed:

- Notes to financial statements
- Requires certain information on the face of financial statements
- Income statement must show:
  - Revenue
  - Results of operating activities
  - Financial costs
  - Income from associates and joint ventures
  - Taxes
  - Profit or loss form ordinary activities
  - Extraordinary items
  - Minority interest
  - Net profit or loss
- Offsetting (netting)
- Summary of accounting policies
- Illustrative financial statements
- Disclosure of compliance with IAS
- Limited "true and fair override" if compliance is misleading
- Requires compliance with interpretations
- Definitions of current and non-current

Summary of IAS 7

- The cash flow statement is a required basic financial statement.
- It explains changes in cash and cash equivalents during a period.
- Cash equivalents are short-term, highly liquid investments subject to insignificant risk of changes in value.
- Cash flow statement should classify changes in cash and cash equivalents into operating, investing, a financial activities.
  - **Operating**: May be presented using either the direct or indirect methods. Direct method shows receipts from customers and payments to suppliers, employees, government (taxes), etc. Indirect method begin with accrual basis net profit or loss and adjusts for major non-cash items.
  - **Investing**: Disclose separately cash receipts and payments arising from acquisition or sale of property, plant, and equipment; acquisition or sale of equity or debt instruments of other enterprises (including acquisition or sale of subsidiaries); and advances and loans made to, or repayments from, third parties.
  - **Financing**: Disclose separately cash receipts and payments arising from an issue of share or other securities; payments made to redeem such securities; proceeds arising from issuing debentures, loan; notes; and repayments of such securities.
- Cash flows from taxes should be disclosed separately within operating activities, unless they can be specifically identified with one of the other two headings.
- Investing and financing activities that do not give rise to cash flows (a non-monetary transaction such a acquisition of property by issuing

debt) should be excluded from the cash flow statement but disclosed separately.

The technical guide suggest the following illustrative list of accounting policies that an NPO could disclose as per Indian Standards AS 1:

- Method of depreciation
- Basis of recognition of major types of expenses and revenue including goods.
- Accounting for income from and expenditure on specified activities
- Valuation of inventories
- Valuation of instruments
- Treatment of retirement benefits
- Valuation of fixed assets
- Treatment of contingent liabilities

There are changes in other countries after the experiences of the Enron, Worldcom. The statute like Sarbones Oxley Act has been introduced. The European Commission has been formed, "The Statutory auditors independence in the EU – a set of fundamental principles." UK also issued a detailed guideline "Auditors Independence: Guidance on Best Practice."

Indian accounting standards are still in their formative stage, and The Institute of Chartered Accountant of India has come out with a detailed technical guide. NPO's in India has to make most dramatic changes to cope with the guide. Even FASB has given time for small NPO's one year upto the end of December 1995 in certain cases. It is essential we grow upto the international level, but we have to take all, and hope sufficient time will be given and organisations like FMSF will impart more training so that we can reach the level easily.

International Accounting Standards for NPOs

Tejas Merh
ACA
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We at GIVE Foundation constantly try to raise ourselves to higher benchmarks. Almost three years back we decided to create a database of NPOs through which we wanted to create a rating system applicable to the sector. The research, wherein we collected and studied balance sheets of almost 10,000 trusts, societies and NPOs, led to a conclusion that it is not possible to compare any two organisations' Balance Sheets because the accounting practices used by the NPOs were nowhere similar. Thus, the Balance Sheets that were created using these accounting practices were not comparable. We realised that we were putting the cart before the horse. We decided to concentrate on the basics, the rules and standards which were used to record transactions and prepare the Balance Sheet. Internally, we felt that the sector needed special accounting standards but before we went on to advocate for that we decided to do our own research on the existing accounting standards in India and the world for NPOs. We studied the accounting standards of US, UK, Canada and the International Accounting Standards to understand what they prescribed as best practices for NPOs.

Based on this research, this paper presents various aspects of the International Accounting Standards as applicable to NPOs. We have taken up various accounting issues that we feel are important for the sector today and have tried to present the standards applicable to these issues as prescribed by the International Accounting Standards Board (IASB). We will then examine the relevance of these standards to the NPO sector.

About the International Accounting Standards Board

The International Accounting Standards Board is an independent, privately-funded accounting standard setter based in London, UK. Board Members come from nine countries and have a variety of functional backgrounds. The Board is committed to developing, in the public interest, a single set of high quality, understandable and enforceable global accounting standards that require transparent and comparable information in general purpose financial statements. In addition, the Board cooperates with national accounting standard setters to achieve convergence in accounting standards around the world (mission statement quoted from **www.iasb.org.uk/aboutus)**. The IASB is continuously working on and amending the accounting standards based on the changes happening internationally. There are various countries which have adopted the IAS either in toto or in part as their statutory accounting standards. The various accounting issues pertaining to NPOs on which the International Accounting Standards have made a mention, directly or indirectly, are enumerated below.

1. Accounting for Grants –

The basic question here is :

Whether Grants are to be taken as Income or Liabilities? Whether a grant is treated as part of shareholders' funds or a grant is taken to income.

IAS 20: Accounting for Government Grants and Disclosure of Government Assistance.

- The International Accounting Standards follows the "income" approach (IAS 20.12-19). This leads to the grant being recognised as income in a manner that matches it to the costs being compensated. Grants may not be credited directly to equity.

- Even if there are no conditions attached to the assistance specifically relating to the operating activities of the organisation (other than the requirement to operate in certain regions or industry sectors), such grants should not be credited to equity

This basically means that whatever grants are received have to be matched with expenses/ costs. Only that much of the grant has to be brought into revenue as is spent by the organisation.

2. Revenue Recognition –

We are dealing with :

How and when are Revenues recognised by Not-for-Profit organisations?

IAS 20 establishes the basic principle that a government grant should not be recognised until there is reasonable assurance that the organisation will comply with the conditions attached to the grant and that the grant will be received. The grant is then required to be recognised as income over the periods necessary to match it with the related costs it is intended to compensate or, if the grant relates to an asset, either as a deduction from the carrying amount of the asset or as deferred income. IAS 20 also addresses how to account for repayments of grants and the disclosures that need to be made for both government grants and government assistance.

Scope

IAS 20 should be applied in accounting for government grants. IAS 20 also prescribes disclosure requirements for government grants and other forms of government assistance.

Key Principles

- **Government Grants:**

Government grants are assistance by government in the form of transfers of resources in return for past or future compliance with conditions relating to an organisation's operating activities.

- **Government Assistance:**

Government assistance is action by government designed to provide economic benefits when qualifying criteria are met by an organisation.

- **Accounting for Government Grants:**

A government grant should not be recognised until there is reasonable assurance that:

- the organisation will comply with the relevant conditions attached to the grant; and

- the grant will be received.

Government grants should be recognised as income over the periods necessary to match them with the related costs which they are intended to compensate. They should not be credited directly to equity.

Government grants that compensate for past expenses or losses or that are provided for the purpose of giving immediate financial support are to be taken to income immediately.

Disclosure

The following information must be disclosed:

- the accounting policy adopted for government grants;
- the nature and extent of government grants recognised;
- other forms of government assistance from which the organisation has directly benefited; and
- unfulfilled conditions and other contingencies relating to government assistance that have been recognised.

This means that the grant should be brought into the books as revenue when

- resonable assurance is there that the organisation will comply with the conditions attaching to the grant.

- reasonable assurance is there that grant will be received

On this basis we can reasonably argue that in case of certain grants it would be correct if we bring it into the books only when they are actually received because until then we **do not have the reasonable assurance that the grant will be received.** This specifically happens in case of Government projects.

3. Valuation by which we mean :

What value would one put to a donation or a grant in kind? Fair market value or the net cost of asset?
How would one account for Assets given on a concessional rate OR assets donated?

The IASB is silent on this aspect. In IAS 20, this aspect is not covered.

4. Reporting of Expenses, specifically this relates to :

Should expenses be reported by functional categories (programmes, management and general, and fundraising) rather than by natural categories?

AS 1 Presentation of Financial Statements

Defines overall considerations for financial statements:

- ***Fair presentation***
- ***Accounting policies***
- ***Going Concern***
- ***Accrual basis of accounting***
- ***Consistency of presentation***
- ***Materiality and aggregation***
- ***Offsetting***
- ***Comparative information***

Four basic financial statements:

IAS 1 prescribes the minimum structure and content, including certain information required on the face of the financial statements:

- Balance Sheet (current/non-current distinction is not required)
- Income statement (operating/non-operating separation is required)
- Cash Flow Statement (**IAS 7: Cash Flow Statements** sets out the details)
- Statement showing changes in equity. Various formats are allowed:

The statement shows:

* (a) each item of income and expense, gain or loss, which, as required by other IASC Standards, is recognised directly in equity, and the total of these items (examples include property revaluations (**IAS 16: Property, Plant and Equipment**), certain foreign currency translation gains and losses (**IAS 21: The Effects of Changes in Foreign Exchange Rates**), and changes in fair values of financial instruments (**IAS 39: Financial Instruments: Recognition and Measurement**); and

* (b) net profit or loss for the period, but no total of (a) and (b). Owners' investments and withdrawals of capital and other movements in retained earnings and equity capital are shown in the notes.

Same as above, but with a total of (a) and (b) (sometimes called "comprehensive income"). Again, owners' investments and withdrawals of capital and other movements in retained earnings and equity capital are shown in the notes.

- The statement shows both the recognised gains and losses that are not reported in the income statement and owners' investments and withdrawals of capital and other movements in retained earnings and equity capital. An example of this would be the traditional multicolumn statement of changes in shareholders' equity.

This has been derived from the summary of the accounting standard as given on the IASB website. It shows the basic aspects to be included in the financial reports. We can definitely interpret it for NPOs as well but it does not specifically address our question as to how expenses should be reported. As on today some NPOs report expenses in the natural categories and some use functional classification. There are instances of a matrix presentation as well where both methods of classification are used.

5. Accounting of joint costs.

The question here is :

What rules should be used for accounting of joint costs between projects / Grants, etc?

There is no specific discussion in this regard in the International Accounting Standards.

6. Disclosure and reporting formats for NPOs. Specifically :

Whether there can be formats for Income and Expenditure Accounts/ Receipts and Payments Account and Balance Sheet for NPOs ?

Other than the aspects discussed in IAS 1, in regard to Presentation of Financial Statements discussed in point 4 and IAS 7 which discusses Cash Flow Statements, the specific aspects of disclosure and reporting for NPOs has not been discussed by the IASB.

7. Accrual Accounting/ Cash Basis Accounting or Hybrid Accounting:

Can we prescribe one of these as the best method?

While IASB has not mentioned anywhere SPECIFICALLY that only accrual method of accounting is to be used and not the cash method of accounting, it is prudent and obvious from the statements issued by these boards that accrual method is better. Accrual is the preferred standard because it more accurately shows the relationship between an expense and the revenue which pays for it. It also gives the reader of the statements a more correct view of the state of affairs of the business. But how practical it is for NPOs to use this method needs to be seen.

8. Depreciation on Assets.

Depreciation is a charge against income in the corporate sector because of the Fixed Assets revenue generating capacity. In the NPO sector neither (profit motive or revenue earning capacity) holds true. So what depreciation rates will apply for the NPO sector?

Though depreciation is a charge against the income, it also accounts for the wear and tear on the assets and is equally applicable to organisations without a profit motive or revenue earning capacity. The IAS does not specifically talk about depreciation standards for the non-profit sector separately. Whatever rates of depreciation are applicable to the corporate sector internationally, is applicable in toto to this sector too.

9. Convergence of Accounting standards

Is it not possible to have same accounting standards across NPOs and industry wise, sector wise financials for NPOs across countries?

The IASB is working on convergence of its standards across countries. We have to first aim at creating similar standards for NPOs within countries. We have a long way to go before can even think of International convergence of standards.

Relevance of IAS to NGOs

NPOs operate all over the globe addressing issues relevant to their countries and areas. One of the most interesting features of NPOs is that they operate and work with people. Their work is at a very micro level and each has to handle issues which are so specific to their areas and circumstances that it is difficult to replicate startegies and decisions to other organisation no matter how similar their work areas are.

If, in a country like India, it is difficult to find NPOs with similar idealogies and strategies, we cannot even begin to find similarities in NPOs across countries or continents. Globally, the sector has seen a lot of discussions and deliberations between countries through various fora, the most recent being the discussions in Manila in regard to regulatory frameworks for NPOs. But, considering the diversity in terms of social and economic conditions, political situations and laws, it is difficult to reach a common conclusion except that, the sector needs much more transparency and accountability within itself and each country has the freedom to choose the mechanisms and systems to achieve it. The IAS are not a complusion. They are used by many countries, which have not yet graduated to having their own standard creating bodies. Many countries, which have their own standard creating bodies, look towards IAS for guidance in terms of interpretations and understanding. Today, countries, which have their own standard creating bodies like US, UK, CANADA, India, Australia etc., are in the process of working out standards, guidelines, best practices for the NPO sector in their countries. It is perhaps better that this process is done individually. It will not make sense for one country to adopt the accounting standards created by another because the circumstances in which NPOs work in these two countries would be extremely different. Some may say that accounting is a science irrespective of variables in industry practices but this cannot be true, especially for the NPO sector, because of the nature of these organisations and the maturity of the sector.

There is no reason why NPOs cannot use the IAS for their accounting. In fact the International Committee of the Red Cross, in its annual report of 2001, has presented its accounts for the first time in accordance with the IAS. Even in the case of the IAS, interpretations from the point of view of NPOs are possible, as they do lack rules on issues specific to NPOs, such as non-reciprocal transfers , valuation for grants in kind etc. For the normal accountant in the sector who has learnt more from experience than education it is difficult to interpret these standards for specific situations.

Ideally, the process of creating International Standards for NPOs should be bottom up with countries creating their standards individually which can then converge into International Standards which would be accepted globally as the best practices in accounting. But, this has a long way to go. The good thing about it is that the world is now paying attention to this need for the NPO sector and taking slow but steady steps to the right direction.

The Way Forward...

India is fortunate to have an institute like the ICAI who has heard and understood the voice of the sector which demanded attention to the issues of accounting and reporting. The Technical Guide has attempted to simplify the interpretations of the accounting standards for NPOs. Such an attempt has put the NPO sector in India at par with countries like US, UK and Canada who have also begun these processes. Recently France and Switzerland have also joined the movement.

Internationally as well, this need is becoming more profound and we can hope to expect some action in this regard from the IASB in future. What we at our end can do is to refine the guidelines and make them much more specific. Even now, confusions prevail in regard to the very specific issues of accounting like :

- allocation of joint costs – allocation for costs between projects.
- segregation and integration of reports – project wise, area wise etc.
- valuation of goodwill – there are many organisations which spin off from a bigger unit. The goodwill it generated for the mother organisation should be valued at the time of the spin off.
- transfer pricing – many NPOs work together with synergy and take services from each other. Sometimes within one organisation several individual projects derive services from each other. No value can as yet be put to these services.

- accounting and tax treatment of multi-period grants – whether such grants can be disclosed as liability and not offered to tax to the extent not used during the year of receipt.
- accounting of assets purchased from Grants – how to account for assets purchased for the projects when the projects are over.
- cross utilisation of fund – this happens a lot when an organisation has multiple donors and projects. How can we account for such transfers and appropriations from one fund to other so as to keep a track of the cross utilisations?

To address such and many other questions which NPO accountants face everyday, we have to continue the process of deliberations and discussions to continuously refine and improve the accounting practices in India taking into consideration the developments in the sector. Whatever we do, whatever means and mechanisms we use should aim to achieve an end that is symbolised by two words - *"Transparency and Accountability."*

Report

Report on the National Consultation on
"Technical Guide on Accounting and Auditing in Not-for-Profit Organisations"
held at New Delhi YMCA,
on 17th & 18th October, 2003

Background

The Institute of Chartered Accountants of India (ICAI) came out with the Technical Guide on Accounting and Auditing for Not-for-Profit Organisations during early 2003. This guide aims at suggesting standardised framework for preparation and presentation of financial statements and also recommends the accounting standards for Not-for-Profit Organisations (NPOs) to be mandatory. As there are many practical implications for the NPOs in adhering to these recommendations, there was a need to discuss the practicalities in detail with the larger forum of development organisations and also finance consultants as well as auditors associated with NPOs.

As an organisation involved in providing financial management consultancy and capacity building initiatives for development organisations in India, Nepal, Bangladesh and Srilanka, Financial Management Service Foundation (FMSF) decided to hold a National Consultation on the above Technical Guide issued by ICAI in New Delhi.

As the recommendations in the Technical Guide have major accounting implications for NPOs, the consultation aimed at discussing the same at length wherein the representatives and leaders of various NPOs from all over the country had participated. Also eminent chartered accountants involved in the development sector had participated to present their views.

Objectives and Expected outcomes

The National Consultation on the "Technical Guide on Accounting and Auditing in Not-for-Profit Organisations" issued by the Institute of Chartered Accountants of India (ICAI) during early this year, took place on 17th & 18th October, 2003 at New Delhi, YMCA.

Report

The **objectives of the National Consultation** were :

- to bring together the Chartered Accountants / auditors and the NPO leaders / representatives across the country to discuss about the Technical Guide
- to create awareness about the salient features and the implications of the Technical Guide on the work of the NPOs.
- to analyse in detail the recommendations of the Technical Guide and its feasibility in implementing the same.
- to make suitable recommendations to the ICAI
- to have an interface with the representatives from the ICAI .

The **expected outcomes of the National Consultation** were :

- the consultation would arrive at a common understanding on the recommendations
- the suggestions emerging out of the deliberations will be taken into consideration and sent to the ICAI
- if required, to organise regional consultations to invoke further deliberations and consolidate the understanding and views of the NPO sector on the Technical Guide

The consultation was inaugurated by Mr. T. S. Viswanath, former President of the Institute of Chartered Accountants of India.

In his inaugural address, Mr. T. S. Viswanath, stated that this Consultation is timely. He also stated that he is happy that the ICAI has brought out the guide for the NPOs. He said that such initiatives bring the focus and significance of the sector to limelight and aim at enhancing the accounting practices of NPOs. Referring to the corporate sector and the concept of corporate governance, he also asked why it has to be termed as Corporate Governance (which by its name focus only on the Corporate sector) and why not a concept of Good Governance or Institutional Governance which encompass both the profit and non-profit sectors

The ***first technical session*** was on **"NGO Accounting Practices and Need for Standards – A Development Perspective"**. The two panel speakers for this session were Ms. Rosemary Viswanath, a management development expert and Mr. Ajay Mehta, Executive Director and Chief Executive of the National Foundation for India. Both of them analysed the prevailing scenario in the NGO sector in the Indian context and working conditions of the grass root level organisations.

Report

In her presentation, Ms. Rosemary Viswanath stated that Non-profit organisations are basically built on the spirit of service, participation, dialogue and civil society's role in building just and sustainable societies. Regulations are most effective only when they aim to strengthen and not merely to control. In that sense understanding the ethos, realities and spirit of the non-profits is essential to any debate on their accounting and their accountability.

In his presentation, Mr. Ajay Mehta reflected on the transition India is going through as a nation. He mentioned about the new policy of the Indian Government through which certain donor countries are being informed that India no longer wants to be identified as an aid-receiving nation but as an aid-giving nation. He felt that these funds coming from donor countries could be given to civil societies and development organizations in India. He informed that it is not clear yet on the stand that will be taken by the donor countries as some may decide to shift their focus elsewhere and others may decide to quit.

As we see, gradually NGOs are becoming an integral part of the society. The experiences of the voluntary sector in the grass root level are taken into account by the government and they have also been recognised as one of the important players in the development scene in our country. The work being done by NGOs have a great impact on the society at large. Therefore, he felt that the best way was to evolve standards which are relevant to NGOs. The NGO sector needs to evolve a mechanism of self regulation. These regulation and standards should be of highest quality and should also be transparent. There is a need to develop these standards by having extensive research and adequate trial in the field as to its applicability.

The session was chaired by Mr. D. T. Reji Chandra, Director of Palmyrah Workers' Development Society, based in the state of Tamil Nadu.

The ***second technical session*** was on **"Accrual Basis of Accounting and its implications for NPOs"**. The two panel speakers for this session were Mr. K. N. Gupta, a Chartered Accountant by profession having rich knowledge and experience in both corporate and voluntary sectors and Mr. Manoj Fogla, also a Chartered Accountant associated with various other NGOs in India as an experienced consultant. The session was chaired by Ms. Chandra Singh, the Chief Accounts Officer of MYRADA, a well known development organisation in the state of Karnataka.

Report

The speakers presented their views on Accrual System of Accounting and its applicability to NPOs. It was stated that Accrual basis of accounting is the method of recording transactions by which revenues, costs, assets and liabilities are reflected in the accounts in the period in which they accrue.

It was discussed that there is a possibility of misuse of accrual method of accounting and at times it may not be acceptable to the funding agencies. It was also stated that the accrual of project grants is contentious issue where there is a need for lending a greater clarity. This issue becomes more important when one considers that the Income Tax Accounting Standards has deleted the words "In view of the uncertainty attached to future events, profits are not anticipated but recognized only when realized though not necessarily in cash".

The speakers also made a comparison of the requirements with the Foreign Contribution (Regulation) Act, 1976 wherein the receipts and payments are to be made as per Cash Basis of Accounting. Also it was compared with the provisions of the Income Tax Act, 1964 where as per Section 145, the NPOs are required to follow either Cash Basis of Accounting or Accrual Basis of Accounting on a regular basis.

This session brought in more discussion and queries wherein the participants shared their views and various practical implications for the NPOs.

The ***third technical session*** was on **"Accounting Standards & its applicability to NPOs"**. The two panel speakers for this session were Mr. Kandasami, a well known practicing Chartered Accountant in the development sector and Mr. Joselyn Martins, also a practicing Chartered Accountant having long years of experience with the development organisations. This session was chaired by Mr. Sudhir Verma, a qualified Chartered Accountant and a qualified certified Internal Auditor from Florida U.S.A.

The accounting standards especially those having implications on NPOs were shared and explained in detail by the speakers during this session. Also the interactive session chaired by Mr. Sudhir Verma provided opportunity for the participants to raise the related queries. Some of the queries were pertaining to Accounting for taxes on income, Segment Reporting, Related Party disclosures etc.

Report

By the end of the first day of the consultation a task group was formed which was to compile the issues raised during the sessions in the form of a presentation. It was decided that the task group would make a presentation on the next day. The ***Task Group*** formed comprised the following members :

1. Mr. Pradeep Esteves
2. Mr. Daniel Selvaraj
3. Mr. Sudhir Verma
4. Mr. Suresh Kejriwal
5. Mr. Satish
6. Ms. S.P.Selvi, FMSF

The ***final session*** began on the second day with the focusing on the ***"International Accounting Standards for NPOs"*** and the discussion was on those aspects relating it to the Accounting Standards by ICAI.

Mr. K.Shivakumar, a Chartered Accountant and a Cost Accountant having long years of association in the field of NPO sector and Mr. Samir Manocha, a practicing Chartered Accountant from M/s. Ray & Ray, Chartered Accountants and involved with various development organizations were the panel speakers for this session. They shared information about those international accounting standards comparing it with the standards of ICAI and suggested adoption of some of them which are relevant to NPOs. During the interactive session that followed the presentation, participants were able to articulate on the various aspects relating to the international accounting standards and its applicability to NPOs in the Indian context.

Consolidation of issues and inputs by the Technical Director, ICAI

The Technical Director of the Institute of Chartered Accountants of India (ICAI), Dr. Avinash Chander participated in this session. Mr. R. Bhakther Solomon from Development Promotion Group, Chennai and Mr. Fatimson from PACT network, Madurai shared their views about the practicalities involved in adhering to the specified accounting standards. They also shared their concerns specifically to those small grass root level organisations for whom employing a full time accountant itself is a major challenge.

Towards the end of the above four technical sessions and the discussions that followed, a presentation by the task group was made which brought in some of the issues and points of suggestions for consideration by the ICAI. The presentation was made by Mr. Daniel Selvaraj on behalf of the task group.

Report

Dr. Avinash Chander, the Technical Director of ICAI responded to the task group's presentation and expressed that the ICAI is willing to look into the recommendations and points brought in the presentation. Regarding simplification and modification of certain terminologies in the Technical Guide, he stated that a hand book can be published instead of bringing a new set of standards. He appreciated the organisers for organising this useful consultation and put forth the concerns of the sector before ICAI.

Valedictory Function

Mr. N.D. Gupta, former President of Institute of Chartered Accountants of India (ICAI) was the speaker for the valedictory function. In his valedictory address, he emphasized the significance of the NPOs and the development work. He also informed about the significance of certain accounting standards like AS-9 & AS - 12 that he considers as very relevant for NPOs. He expressed his appreciation for the efforts being made by these NPOs towards the cause and upliftment of the poor in the country.

The National Consultation concluded with a vote of thanks by Mr. Sanjay Patra on behalf of FMSF.

Conclusion

The presentation of the task force were later shared with other members for preparation of the paper to be presented to the ICAI. The suggestions and recommendations received were incorporated and the paper has been finalised.

The Paper on Task Group Recommendations is provided herewith.

The paper was presented to the Institute of Chartered Accountants of India during first week of January 2004.

TASK FORCE RECOMMENDATIONS ON THE TECHNICAL GUIDE FOR NPOs

BACKGROUND TO THE ACCOUNTING STANDARDS FOT NOT -FOR-PROFITS

The Institute of Chartered Accountants of India (ICAI) has been striving to bring about a set of accounting standards that would suit the Not-for-Profits (NPO's)[1]. The exercise was necessitated due to the fact that the accounting standards that were in practise addressed to the business or commercial organisations. The assumption here was that NPO's also carried out a small portion of their activities towards income generation thereby needing to abide by the accounting standards as set out by the institute.

With the growing awareness of the practices of the NPO's and the varied accounting practices being followed, there was a need to take a look at the existing accounting standards to assess their applicability to the specific needs of the NPO's. The ICAI through its technical director had participated in a workshop conducted by FMSF (where the Forum for Ethics, Accountability and Transparency [FEAT] was formed) at Goa. A draft of the standards was circulated to the members of the FEAT and a few other NPO actors.

FMSF in order to extend the scope of understanding and need of the NPO's in India called for a National Consultation on Accounting Standards at Delhi during October 2003. Over a hundred participants who included the members of FEAT along with representatives of the NPO's along with representations from the ICAI attended this consultation.

During the two day deliberations various aspects relating to practical realities being faced by the NPO's were highlighted. A task group was formed in order to compile the suggestions and recommendations raised during the consultation. The ICAI representatives on their part were open for the various suggestions and had requested that the suggestions and recommendations be sent to the ICAI in order for them to look into and incorporate them in the Accounting Standards as appropriate.

History and background of the NGO sector

During the National consultation held at Delhi, the representatives from the NPO sector gave an elaboration of the situation and the history of the voluntary movement in the country. Some of the highlights pointed out by them were that the NPO sector had a rich history and evolutionary process and a vast majority of the NPO's were working towards the development of the poor and downtrodden in remote rural areas. The NPO's were by and large dependant on external funding either from the government and/or donors from within the country or elsewhere. These funds which form the main source of income for the NPO's were based on specific projects for a specified period of time, normally ranging from a year to a maximum of three years and this funding income too was not assured. It was also highlighted that the fund flow to the NPO was erratic and irregular and dependant on various factors that were beyond the control of the NPO's. Further it was also highlighted that the NPO's were always under a threat of a ban under the Foreign Contributions Regulation Act (FCRA) due to various reasons. Under these situations one of the questions that was raised at the consultation was whether the fundamental accounting assumption of being a Going Concern was being met by the NPO's. Thereby it was suggested that the definition of a Going Concern needs to be further elaborated by taking into account the peculiar situation of the NPO's.

Further it was also discussed by the participants that most of the statutes required that NPO's follow a cash basis of accounting. The Foreign Contributions Regulation Act specifies that the NPO reports a receipts and payments of account annually, thereby implying usage of the cash basis of accounting.

The Income Tax prescribes under section 145 that an organisation can follow consistently any one of the two methods of accounts i.e. Accrual and Cash basis of accounting. Further, the Income Tax Rules has also notified two accounting standards including the Accounting Standard on the "Disclosure of Accounting Policies". It was discussed and noticed that though the Accounting Standards issued by the Income Tax Department were similar to the Accounting Standard of the ICAI there was some important deviations. Apart from the above, the NPO's are required to utilise 85% of the income during the year of receipt of the funds. While only 15% of the funds are allowed to be accumulated. In this context there is a need for imparting greater clarity with regard to accrual of various income of NGOs. So that, there is no confusion with the perceptions and interpretations of Income Tax Laws and Income Tax accounting standards. The issue becomes more important considering the fact that the accounting standards issued by the Income Tax department has removed the words *" In view of the uncertainty attached to future events profits are not anticipated but recognised only when realised though not necessarily in cash"*, from AS 1.

Apart from the above statutory requirements to be met by the NPO's the specific requirements from the Donors were normally to be reported on cash basis. Most funding agencies primarily require the NPO's that are being assisted by them to submit a financial statement in a prescribed form. These formats would normally require the NPO to report the *actual* receipts, disbursements, utilisation of grant and *unutilised balance*, thereby implying a cash basis of accounting.

A survey finding of a renowned international research institute that was shared at the consultation showed that 73.4 % of the NPO's work with less than one staff while the remaining were found to be volunteers. Thereby highlighting the lack of affordability towards hiring staff and/or also availability of staff to work in the remote locations that a vast majority of the NPO's work in. It also highlighted the fact that the NPO's work was voluntary in nature. During the deliberations it was further highlighted that even if staff were to be found locally, it was an impossible task to get qualified staff to implement the accounting standards. Further it was also shared that it was the experience of NPO's that when they manage to find qualified staff the costs involved in making it attractive for them to stay on and work had been very expensive. Thereby making it very difficult for NPO's with limited funds to implement the accounting standards.

Thereby, it was argued that if an accrual basis of accounting is strictly followed by the NPO's it could prove to be counterproductive, as the NPO's would then have to maintain separate set of books for the various requirements. In order to meet these varied requirements and also taking into account the internal capacities within the NPO's. They have until now evolved systems of accounting varying from pure cash basis of accounting to a mixed (hybrid) account basis in order to satisfy the requirements of its varied constituencies, which also include mainly the beneficiaries that they work with.

A comparison of the International Accounting Standards were also made vis-à-vis the Indian Accounting Standards for the NPO's. While it was pointed out that only a few accounting standards applied for specialised industries. Thereby the Accounting Standards could be refined to make them much more specific for the requirements of the NPO's. It was shared that ideally the process of creating Accounting Standards for NPO's should be bottom up which can then converge into Standards at the national and international levels which would be accepted globally as the best practices in accounting. But this has a long way to go. The good thing is that attention is now being paid to the need for the NPO sector and taking slow but steady steps in the right direction. Therefore, it was felt that a three year period be recommendatory before making the implementation of the AS mandatory. During which time the Accounting Standards could to be evolved for NPO's taking into account the varied and different situations under which the NPO's work in.

However, it was strongly pointed out time and again, that the NPO's wanted accountability and transparency. They have internally by themselves evolved systems that meet these requirements. Their point of view being that in order for accepted and successful implementation of the Accounting Standards, the situation and requirements of the NPO's need to be understood in it totality. As one member pointed out "there is a need to simplify the complexity – otherwise life will remain complicated. There is a need to find a balance and the standards cannot be imposed. The challenge is in simplifying the standards and making it easily adaptable as we have to keep in mind the grass root realities and the availability of skilled personnel in remote locations"

In the background of the above described discussion, the delegates, FEAT and FMSF place before the ICAI the following recommendations for favourable incorporation.

GENERAL RECOMMENDATIONS

NPOs should be given the option of following either cash or accrual basis of accounting, while adequate notes to accounts could be made in the financial statements on the basis of accounting followed.

There is a need to harmonise the accounting standards with the statutory requirements and the inherent characteristics of the NPO's (See General Suggestions given below).

The accounting standard be implemented for NPO's having a gross income of over Rs. 50 lakhs.

Accounting Standard for NPO's could be recommendatory for a three year period before being made mandatory.

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1. Not-for-Profits would include Non-Governmental Organisations, Development Organisations, Voluntary agencies, charitable trusts and institutions and any such organisations that do not distribute profits from their activities.

SOCIETIES REGISTRATION ACT, 1860

Working and Management of a Society

Pooja Bagga

[In continuation with the series of articles dealing with relevant issues of Societies Registration Act, 1860, in this article we are dealing with the topic of "Working and Management of a Society"]

The term Governing Body which is the most commonly used word for the management of a society has not been defined anywhere in the Societies Registration Act 1860.The Governing Body is defined under Section 16 of the Societies Registration Act 1860 as 'Governing Body of a Society to consist of the governors, council, committee, trustees or some other body by whatever name called to whom or to which by the rules and regulations of the society, the management of its affairs is entrusted'. Therefore we can easily say that the Governing Body of the Society is the brain of the society without which it cannot operate.

In absence of any definition in the Societies Registration Act 1860, we draw an interpretation from the definition as per Sec 32 of the English enactment, namely, Literary and Scientific Institutions Act, 1854 which defines *Governing Body* as:

"The Governing Body of the institution shall be the council, director, committee, or other body to whom by Act of Parliament, Charter or the rules and regulations of the institution, the management of the affairs is entrusted; and if no such body shall have been constituted on the establishment of the institution, it shall be competent for the members thereof, upon due notice, to create for itself a governing body to act for the institution thenceforth"

For the regular activities of the society, the management, execution and supervision is done by the governing body. The governing body has to work within the framework of the objects of the society as well as carry out the statutory duties laid down in the Act.

The governing body of the society is a fluctuating body, however, the constitution of the governing body is not affected by the change of the members. The governing body will always exist to manage the affairs of the society whether or not it has been properly constituted in terms of the rules and regulations. The entrustment of the management should be complete to the governing body. The criterion in all cases is 'who is managing the affairs of the society'. Similarly the property of the society vests in the Governing Body and not in the members of the society.

Members and Meetings:

Usually the governing body comprises of members chosen from among the members of the society or in some cases if the Government feels necessary, a nominee can be appointed by the Government in the Governing Body for public interest.

The Annual General Meeting (AGM) of the society is held according to the rules and regulations of the society generally once in a year or as is defined in Sec 4 of the Societies Registration Act. Section 4 of the Societies Registration Act states that:

'Once in every year, on or before the fourteenth day succeeding the day on which, according to the rules of the society, the annual general meeting of the society is held, or, if the rules do not provide for an annual general meeting ,in the month of January, a list shall be filed with the registrar of Joint Stock Companies, of the name, addresses and occupations of the governors ,council, directors ,committee or other governing body then entrusted with the management of the affairs of the society'.

This section regarding the annual general meeting also corresponds to Section 159 of the Companies Act 1956 which deals with the annual return to be made by a company having a share capital. The section 159 of Companies Act says that, 'Every company having a share capital shall, within forty two days from the date on which each of the annual general meetings referred in Section 166 is held, prepare and file with the Registrar a return containing the particulars specified in part I of Schedule V, as they stood on that date, regarding:

a) its registered office
b) the register of its members
c) the register of its debenture-holders
d) its shares and debentures
e) its indebtedness
f) its members and debenture holders, past and present, and
g) its directors, managing director, managing agencies, secretaries and treasurers, managers and secretaries past and present……………..'

similarly in case of societies we interpret that the society shall file a list containing the names ,addresses and occupations of the governors, council, directors, committee or other governing body then entrusted with the management of the affairs of the society to the Registrar of Joint Stock Companies,

- once in a year when the AGM is held
- in case it is not held once in a year then within 14 days on which the AGM is held according to the rules of the society, and
- in cases where the rules do not provide for an AGM, then in the month of January.

(Under State Amendments certain states have replaced the word ' Registrar of Joint Stock Companies' by ' Registrar of Societies' or has been omitted).

Changes in the Managing Body/ Governing Body

Several states have inserted Section 4A, 4B, 4C to the Section 4 of the Central Societies Registration Act, which gives insertions regarding the changes in the managing bodies and the rules of the society to be filed with the Registrar.

These sections of various states generally state that along with the list mentioned in Sec 4(list of governing body) to be submitted to the Registrar, a statement showing changes during the year regarding Governors, Council, Directors, Committee or other governing body to whom the management of the affairs of the society is entrusted along with a copy of the rules of the society corrected up to date, certified by not less than three members of the governing body also has to be filed.

These insertions of section 4A, 4B, 4C have been made in various states like Assam, Bihar, Gujarat, Maharashtra, Nagaland, Orissa, Pondicherry, Uttar Pradesh, and Union Territory- Goa Daman & Diu. (Kindly refer to the respective State Acts for the relevant sections)

Suits by and against the Society

Section 6 of the Societies Registration Act states that every Society registered under this Act may sue or be sued in the name of the President, Chairman or Principal Secretary, or trustees as shall be determined by the rules and regulations of the Society and in default of such determination in the name of such person as shall be appointed by the governing body of the occasion.

However regarding the provisions relating to filing and defending the suits by the Society, Section 7 of the Act provides that no suit or proceeding of a society shall be discontinued in case of death or cessation of office of the person in whose name the suit has been filed. The suit or proceeding shall be continued in the name of or against the successor of such person.

Section 7 states that :

'No suit or proceeding in any civil court shall abate or discontinue by reason of the person, by or against whom such suit or proceeding shall have been brought or continued, dying or ceasing to fill the character in the name whereof he shall have sued or sued by the same suit or proceeding shall be continued in the name of or against the successor of such person .Therefore same proceedings and suit shall continue in the original form and vacancy in the governing body shall not affect'

Minimum members of a Governing Body

There shall be at least 2 members of any governing body. However, if the society is registered in the state of TamilNadu there should be at least 3 members of the governing body.

The members of the governing body are either elected or nominated as per the rules and regulations of the society.

Term of Office

Generally the term of office of the members of the governing body is given in the rules of the society. However if the society is registered in the state of TamilNadu, the TamilNadu State Act gives the term of office of a member of the governing body for a period which cannot exceed more than 3 years.

The rules of society should also generally provide the procedure for retirement and expulsion of the members.

Property of the Society

Trustee of a society is a person in whom the confidence has been reposed under a trust. A Trustee is a person who is owner of the property and deals with it as principal owner and master subject only to an equitable obligation to account to some person to whom he/she stands in relation of trustee.

A Trust is an obligation annexed to the ownership of a property and arising out of a confidence reposed in and accepted by the owners or declared or accepted by him for the benefit of another and the owner thereof.

The members of the governing body are the **Trustees** of the Property of the Society. The property whether movable or immovable vests with the society's trustees .In case there are no trustees for the property of the society, it is deemed to be vested in the governing body of the society. An office bearer of a society may also be the trustee of the property.

In case of any civil or criminal proceedings, the property of society is also described as the property of the governing body of such society.

However, the personal property of the person or the officer who has been named on behalf of the society is not in any case liable for any judgements which have been given against the property of the society. Section 8 of the Act states that *"If a judgement shall be recovered against the person or officer named on behalf of the society, such judgement shall not be put in force against the property, movable or immovable, or against the body of such person or officer, but against the property of the society.'*

Signing Authority

In general all the documents of the society to be filed with the society registrar should be signed by the President or the Chairman or the Secretary of the Society or by any other person specifically authorized in this behalf.

Filing of Documents of the Society

The various documents or the various intimations to the registrar of the society which are to be filed should be signed either by the Chairman or the President, Secretary or by any person specifically authorized in this behalf by the rules and regulations or as authorized by a resolution of the governing body.

Holding Office

There is no specific section or clause in the Societies Registration Act 1860 regarding the qualifications and disqualifications for holding office in a Society Some of the disqualification given specifically by the Section 28 of the West Bengal Societies Registration Act, section 16 of the UP Societies Registration (Amendment) Act and Section 20 (2) of Travancore Cochin Act are:

- A person is disqualified for being chosen as or being a member of the governing body are
  - Person is an undercharged insolvent
  - is convicted of any offence in connection with the formation, promotion, management or conduct of the affairs of a society or a body corporate, or of any offence involving moral turpitude.

Referring to the a.m. sections of the State Acts and also the Companies Act 1956, we can interpret that a person who is insolvent or is of unsound mind or convicted of an offence involving moral turpitude should not be allowed to hold any office of a registered society

Statutory Duties of the Governing Body

Since Governing Body manages the affairs of the Society, the members of the governing body have to comply with the provisions laid down in the statute regarding filing of the documents with the Registrar, maintenance of accounts, managing and applying the funds of the society for carrying out the objects of the society etc. The provisions of the principal act lays down the way the society is required to act and for all purposes it is the governing body which has to fulfill these duties on behalf of the society. The statutory duties which the governing body is required to carry out are:

- Filing of list of the names, addresses, occupations of the Governors, Council, Directors, Committee or other Governing Body at that time entrusted with the management of the affairs of the society, once in a year within 14 days of the annual general meeting (AGM) of the society (or in the month of January if rules do not provide for AGM).
- Holding of annual general meeting at the time prescribed in the rules and regulations of the society.
- Holding of extraordinary general special meeting in case some special business has to be transacted which cannot wait till holding of the AGM.
- Changes in the managing body and the rules of the society have to be filed with the registrar of societies as per the provisions of various state act insertions under Section 4 A ,4 B, 4 C.
- Notice of the situation of the Registered Office and any change thereof has to be filed with the Registrar within one month from the date of registration of society or the date of the change as the case may be.
- Any amendments in the memorandum or bye laws has to be registered with the registrar signed by one of the members of the governing body to be accompanied with a copy of the special resolution relating to the amendment with a fee of Rs.2.
- Ensuring that the notice for the AGM and extraordinary meeting is duly sent to all the members.
- The registered office should supply to its members on application, copy of bye laws, receipts and payment account, balance sheet at a prescribed fee.
- Responsibility for investment and application of the funds and properties of the society.
- aintenance of register of members as per the rules and regulations of the society.
- Display of the name of the society at its place of business and its registered office.
- When required by the Government or the Registrar, the governing body of any society should submit periodical account of income and expenditure and assets and liabilities of the society.
- A copy of the special resolution passed for any purpose, duly signed by an officer of the society authorised by the rules of the society should be filed with the registrar within 20 days from the passing of the resolution.
- The governing body should ensure the recording of the minutes of the proceedings of the governing body or the general body.
- The society should retain the important documents of the society permanently.

To be continued...............

ACCOUNTING STANDARDS FOR NGOs

Valuation of Inventories (AS 2) (Revised 1999)

S.P. Selvi
Rahul Khanna

The Institute of Chartered Accountants of India (ICAI) has recently brought a Technical Guide on Accounting and Auditing in Not-for-Profit Organisations (NPOs) which deals with suggesting the accounting and financial reporting framework for NPO sector for presentation of true and fair view of the state of affairs and the results of the financial statements. The Guide also discusses the salient feature and principal requirements of various Accounting Standards.

In the previous issue we focused on AS-1 – Disclosure of Accounting Policies. Through this issue we deal with AS-2 – Valuation of Inventories and highlight some of the relevant aspects relating to NPOs.

Objective of AS- 2

The Accounting Standard – 2 (Referred to AS – 2 henceforth) is about Valuation of Inventories. The objective of AS -2 is to formulate a method of computation of cost of inventories / stock lying with an organisation on a particular date. It helps in determining the value of such inventories to be reflected in the financial statements of the respective organisation.

Before we look into the other aspects of valuation, we need to understand the meaning of "Inventories" and how this Standard is applicable to Not – for – Profit organizations (NPOs).

What are inventories ?

The dictionary meaning of inventories states it as *"a complete list of goods in stock, house contents etc.,"*

From the accounting point of view, Inventories are assets :

a) held for sale in the ordinary course of business (finished goods);

b) in the process of production for such sale. This may include raw materials and goods which are half-way of the production process called Work – in – Progress.

c) in the form of materials or supplies to be consumed in the production process or in the rendering of services. This includes stores, spares, raw materials, consumables etc.

Inventories do not include :

- As per the objective of the Standard, though inventories include work - in – progress, this cannot be applied to those work-in-progress arising under construction contracts.

- It also does not include shares, debentures and other financial instruments held as stock-in-trade etc.

Applicability of AS-2 to NPOs

It is true that the applicability of this Standard is more relevant to profit making organisations / businesses involved in manufacturing and production of goods and materials, but this is also applicable to not-for-profit organisations as well.

This may be applicable to organisations dealing in publications, relief measures, manufacturing of goods like handicrafts, candles, agarbattis etc.

According to the Technical Guide for NPOs recently issued by ICAI, where an NPO is carrying on any trading / manufacturing activity that results in a stock or inventory of goods, such **inventories should be valued at cost or net realisable value whichever is lower.**

As per AS-2, organisations are required to reflect the value of these inventories in their financial statements at the end of the respective accounting year.

How to calculate Net Realisable Value of Inventories ?

Net Realisable value is the estimated selling price in the ordinary course of business less the estimated cost of completion and the estimated cost necessary to make the sale.

What is the Cost of inventories ?

The cost of inventories, it should be noted that it comprises all *costs of purchase, cost of conversion and other costs* incurred in bringing the inventories to their present location and condition.

- ***Cost of Purchase*** consist of the ***purchase price*** including duties and taxes (other than those subsequently recoverable by the enterprise from the taxing authorities), ***freight inwards*** and other expenditure directly attributable to the acquisition. Trade discounts, rebates, duty drawback and other similar items are deducted in determining the costs of purchase.

- ***Cost of conversion*** includes costs directly related to the units of production, such as direct labour, direct material and direct expenses. They also include a systematic allocation of ***fixed and variable production*** overheads that are incurred in converting materials into finished goods.

- ***Fixed Production Overheads*** are those indirect costs of production that remain relatively constant regardless of the volume of production, such as depreciation and maintenance of factory buildings and the cost of factory management and administration.

- ***Variable Production Overheads*** are those indirect costs of production that vary directly or nearly directly with the volume of production such as indirect materials and indirect labour.

It needs to be noted that Overhead costs are included in the cost of inventories ***only to the extent they are incurred in bringing the inventories to the present location and condition.***

➢ ***Other Costs***

Other costs are included in the cost of inventories only to the extent that they are incurred in bringing the inventories to the present location and condition. For example, costs of designing the products for specific customers in the cost of inventories.

Exclusions from the Cost of Inventories

In determining the cost of inventories, certain costs are excluded and are recognised as expenses in the period in which they are incurred. Examples of such costs are:

a. abnormal amounts of wasted materials, labour, or other production costs;

b. storage costs, unless those costs are necessary in the production process prior to a further production stage;

c. administrative overheads that do not contribute to bringing the inventories to their present location and condition; and

d. selling and distribution costs.

As per AS-2, interest and other borrowing costs are usually considered ***as not relating*** to bringing the inventories to their present location and condition and are, therefore, usually ***not included in the cost of inventories.***

Depreciation as Cost Element :

Depreciation should be included in the inventory cost so far it relates to the fixed assets used in the production process.

Purpose of Inventories / Stock in NPOs

Regarding inventories / stock held by NPOs, generally it is for the following purposes :

* where these ***items are manufactured or purchased for the purpose of distributing them to beneficiaries*** either free of cost or at a nominal amount.

In such instances, these ***items should be valued at the lower of cost or replacement cost, if available.***

* where ***NPOs receive items from donor agencies either free of cost or at a nominal charge for distribution to beneficiaries or for sale,*** some part of such items may remain undistributed / unsold at the year-end.

In such instances, NPOs ***should disclose market prices or estimated net realisable values of such items, lying at the end of year, in the notes to accounts along with quantitative details.***

However, it should be ***ensured that the inventories are not held :***

- for the purpose of sale;
- in the process of production of such sale; or
- in the form of materials or supplies that are to be consumed during the production activity;
- for the purpose of rendering of services of commercial or business in nature;

If so, such items ***cannot be considered*** as inventories within the meaning of AS-2.

Valuation of inventories

After calculating the cost of the inventory, another problem that we face is to value them on a particular date as these inventories would have been procured at different costs at different times. They would have been issued at different times as well for different quantities. Therefore, what would be the cost of inventories remaining as closing stock ?

In order to overcome this problem, various cost formulae are applied in practice in inventory valuation. AS – 2 specifically allows the following formulae :

1. Specific identification method;

In simple terms, this means directly linking the cost with specific item of inventories. This is applicable in case of purchase of items or goods or services specifically segregated for a specific project.

2. **Where Specific identification is not applicable, the following methods can be applied :**

a. First in First Out Method (FIFO) :

As the name indicates, the formula assumes that the items of inventory which were purchased or produced first are consumed or sold first and consequently the items remaining in inventory at the end of the period are those most recently purchased or produced.

b. Weighted Average Cost Method

Under this cost formula, the cost of each item is determined from the weighted average of the cost of similar items at the beginning of a period and the cost of similar items purchased or produced during the period. The average may be calculated on a periodic basis, or as each additional purchase or procurement is made, depending upon the circumstances of the organisation.

What are the disclosures required under AS -2 ?

The financial statement should disclose the following :

- The accounting policies adopted in measuring inventories including the cost formulae used;

and

- The total carrying amount of inventories and its classification appropriate to the enterprise. Common classification of inventories are raw materials and components, finished goods, stores and spares and loose tools etc.

[In the next issue, we will discuss about AS -3 Cash Flow Statements]

Special Announcement ! ! !

This is to inform you that

Financial Management Service Foundation

has shifted to

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w.e.f. 1st June 2004

You are kindly requested to make all the future correspondence at the above address

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