

Accounting and Auditing aspects of Charitable Organisations



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 - Income Tax Act, 1961
 - Foreign Contribution (Regulation) Act, 2010

CHARITABLE ORGANISATIONS





Introduction -

- Charity is an age old activity.
- Over the years, there has been growth in charitable activities.
- India has also witnessed a spurt in such activities.
- New generation looks at charitable activities as an option in career.
- Government in National Policy framed in 2007 has looked at partnership between NPO and Government for distribution of benefits of government policy reaching lower strata of society



Accounting Aspects

- Accounting aspect of every organisation largely is common.
- Charitable Organisations however, are governed by different laws as well as different forms of organisations also necessitate different accounting aspects to be complied.
- Projects undertaken by a Charitable Organisation may also necessitate consideration.



Accounting Aspects

- Depending on Forms of Organization:
 - Public Trust
 - Society
 - S. 8 Company (Companies Act, 2013)
 - Co-operative Society
 - Multi State Co-operative Society
 - Autonomous Body functioning with Government Aid



Accounting Aspects

- Depending on regulating laws:
 - Maharashtra Public Trusts Act, 1950
 - Societies Registration Act, 1860
 - Maharashtra Co-operative Societies Act, 1960
 - Multi State Co-operative Societies Act, 2002
 - Income Tax Act, 1961
 - Foreign Contribution (Regulation) Act, 2010
 - Format of Accounts prescribed by MoF, GoI



Accounting Aspects

- Accounting Standards applicable prescribed by ICAI
- Indian Government Accounting Standards (IGAS)
- Indian Government Financial Reporting Standards (IGFRS)
- International Public Sector Accounting Standards (IPSAS)
- Accounting for Local Bodies



Accounting under Maharashtra Public Trusts Act

- Applicable Provisions –
- Maharashtra Public Trusts Act, 1950
 - S. 31 – Submission of Budget to Charity Commissioner
 - S. 32 – Maintenance of Accounts
 - S. 33 – Balancing and auditing of accounts
 - S. 34 – Auditor's duty to prepare Balance Sheet
- Bombay Public Trust Rules, 1951
 - Rule 17 – Maintenance of Accounts
 - Rule 18 – Certain powers facilitating audit
 - Rule 19 – Contents of audit report
 - Rule 20 – Fee for Special Audit
 - Rule 21 – Time for audit and submission of audit report



Accounting under Societies Registration Act

- Applicable provisions –
- Societies Registration Act, 1860
 - S. 12D – Maintenance of Accounts and Balancing and auditing
 - S. 12E – Auditor's duty to prepare Balance Sheet and report irregularities
- Societies Registration (Maharashtra) Rules, 1971
 - Rule 9 – Maintenance of Accountants
 - Rule 10 – Audit
 - Rule 11 – Manner of Audit
 - Rule 12 – Time limit



Accounting under Companies Act, 2013

- Applicable Provisions –
- Companies Act, 2013
 - S. 8 – Formation of Companies with Charitable Objects
 - S. 128 – Books of Accounts etc. to be kept by company
 - S. 129 – Financial statement
 - S. 133 – Central Government to prescribe Accounting Standards
 - S. 134 – Financial Statements, Board report
 - S. 137 – Copy of financial statement to be filed with Registrar
- The Companies (Accounts) Rules, 2014



Accounting under FCRA

- Applicable Provisions –
- Foreign Contribution (Regulation) Act, 2010
 - S. 19 – Maintenance of Accounts
 - S. 20 – Audit of Accounts
 - S. 23 – Inspection of Accounts
 - S. 24 – Seizure of Accounts or records
- Foreign Contribution (Regulation) Rules, 2011
 - Rule 11 – Maintenance of Accounts
 - Forms – Requiring Certification by Chartered Accountant
 - FC-6
 - FC-7
 - FC-8



Accounting for Autonomous Bodies

■ Applicable Provisions –

- Indian Government Accounting Standards
- Indian Government Financial Reporting Standards
- Common Format of Accounting prescribed by Government

[Refer Government Accounting Standards Advisory Board (GASAB) website for more details]



Accounting depending on Activities

- Applicable Provisions –
- Depends on activities undertaken – e.g.
 - Hospitals
 - Educational Institutions
 - Schools, Colleges
 - Medical Aid Society
 - Hostel
 - Libraries
 - And likes . . .

Audit of Charitable Organisation

- An audit is common for all the organisation with general definition being given in
- It is different for charitable organisations depending upon the registrations obtained by the respective organisation under different laws.
- Specific compliances are necessary apart from general audit compliances.

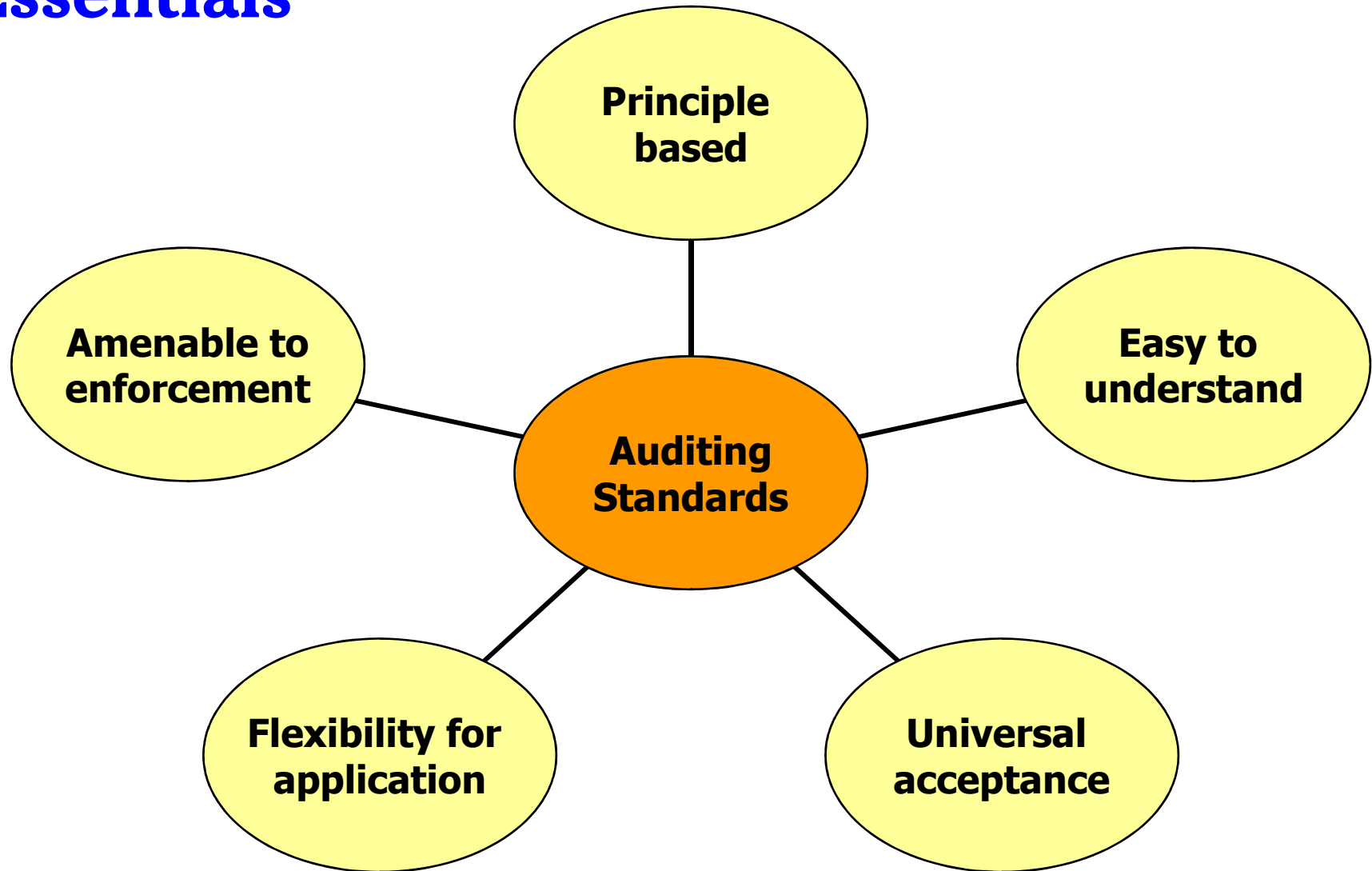




Why Auditing

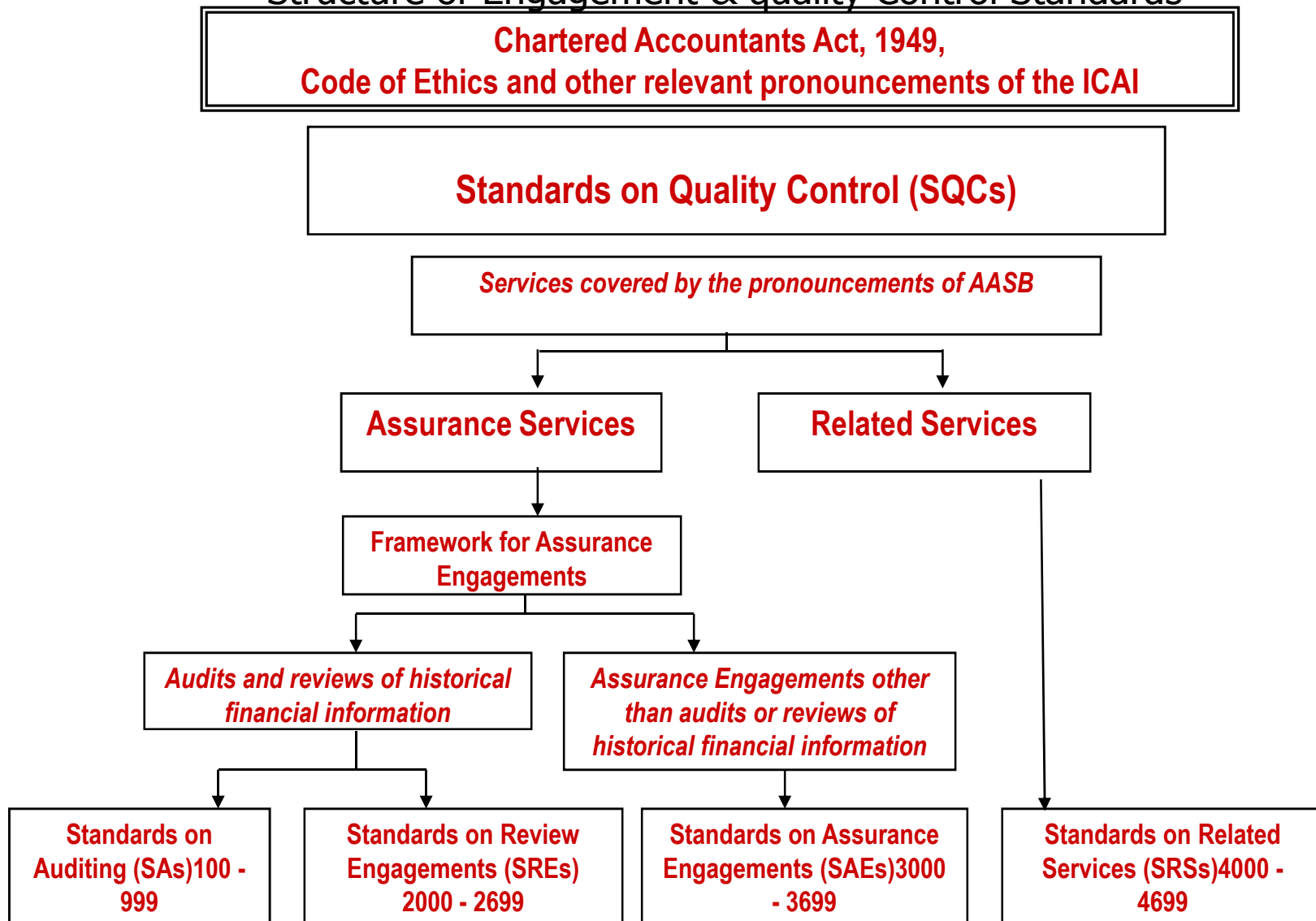
- Economic consequences – Impact of using unreliable information
 - Enhancing credibility of financial information
 - Conflict of interest – Users vs. Preparers
 - Remoteness – Physical, Legal
- (A vital part of Economic Infrastructure)

Effective Auditing Standards - Essentials



A New Framework

Structure of Engagement & quality Control Standards





Compliance with SAs

- Compliance with SAs
 - Mandatory
 - Departure only if alternate audit procedures achieve objective of SAs
 - Document reasons for departure
 - Document alternative procedures
 - Report to draw attention

- SA not applicable if situation outlined in SA is absent.
 - Document alternative procedures performed

Accounting and Auditing of Charitable Organisations under Different Acts





Audits under Different Acts

- Audit under Companies Act, 2013
- Audit under Maharashtra Public Trusts Act, 1950
- Audit under Societies Registration Act, 1860
- Audit under Income Tax Act, 1961
- Audit under Foreign Contribution (Regulation) Act, 2010



Audit under Companies Act, 2013

- Charitable Organisation formed as Company u/s. 8.
- Principles of Audit as normally applicable to any other limited company are equally applicable with certain exceptions.



Company u/s. 8

- **Applicability of Accounting Standards**
 - NOT APPLICABLE
 - Unless, any part of activity includes an activity of commercial, industrial or business nature.
- [Refer: Clarification issued by ICAI and published in September 1995 issue of the journal]



Company u/s. 8

- All the other provisions of Company Audit shall be applicable.
- The format of report is given in the 'Technical Guide on Accounting and Auditing of NPO' issued by ICAI.

Audit under Maharashtra Public Trusts Act, 1950

- Any organisation registered under Maharashtra Public Trusts Act, 1950 is governed by Chapter – V of the act covering provisions on ‘Budget, Accounts and Audit’.





Audit under Maharashtra Public Trusts Act, 1950

Section 31A, 32, 33(2) and 34(1) and Rules 16A, 17, 19, 20 and 21 deal with accounts and audit of public trusts.

Accounts:

- a) Every trustee of a public trust shall keep regular accounts.
- B) Such accounts shall be kept in such form as may be approved by the charity commissioner and shall contain such particulars as may be prescribed.



S. 31A –Filing of Budget

- Compulsory for every Public Trust to prepare and file with the Charity Commissioner at least 1 month before the commencement of each accounting year, a BUDGET showing probable receipts and disbursements of the Trust during the following year.



Accounts and Audit

- S. 32 – Maintenance of Accounts
- S. 33 – Accounts shall be audited every year by a Chartered Accountant within the meaning of Chartered Accountants Act, 1949

OR

- By such persons authorised by State Government
- Provided that, NO SUCH PERSON is in any way interested in ; or connected with, the Public Trust.



S.34 – Duty of Auditor

- IT IS THE DUTY OF THE AUDITOR OF A PUBLIC TRUST TO PREPARE A BALANCE SHEET AND INCOME AND EXPENDITURE ACCOUNT AND TO FORWARD A COPY OF THE SAME TO THE CHARITY COMMISSIONER.
- 1A. IT SHALL BE THE DUTY OF THE TRUSTEE TO FILE A COPY OF THE BALANCE SHEET AND THE INCOME AND EXPENDITURE ACCOUNT FORWARDED BY THE AUDITOR BEFORE THE CHARITY COMMISSIONER.
- THE AUDITOR SHALL IN HIS REPORT SPECIFY ALL CASES OF IRREGULAR, ILLEGAL OR IMPROPER EXPENDITURE, OR FAILURE OR OMISSION TO RECOVER MONEY OR OTHER PROPERTY BELONGING TO THE PUBLIC TRUST OR OF LOSS OR WASTE OF MONEY OR OTHER PROPERTY THEREOF AND STATE WHETHER SUCH EXPENDITURE, FAILURE, OMISSION, LOSS OR WASTE WAS CAUSED IN CONSEQUENCE OF BREACH OF TRUST, OR MISAPPLICATION OR ANY OTHER MISCONDUCT ON THE PART OF THE TRUSTEES. OR ANY OTHER PERSON.



Rule 19 – Contents of Audit Report

- WHETHER ACCOUNTS ARE MAINTAINED REGULARLY AND IN ACCORDANCE WITH THE PROVISIONS OF THE ACT AND THE RULES;
- WHETHER RECEIPTS AND DISBURSEMENTS ARE PROPERLY AND CORRECTLY SHOWN IN THE ACCOUNTS;
- WHETHER THE CASH BOOK AND VOUCHERS IN THE CUSTODY OF THE MANAGER OR TRUSTEE ON THE DATE OF AUDIT WERE IN AGREEMENT WITH THE BOOKS OF ACCOUNTS;
- WHETHER ALL BOOKS, DEEDS, ACCOUNTS, VOUCHERS OR OTHER DOCUMENTS OR RECORDS REQUIRED BY THE AUDITOR WERE PRODUCED BEFORE HIM;
- WHETHER A REGISTER OF MOVEABLE OR IMMOVABLE PROPERTIES IS PROPERLY MAINTAINED, THE CHANGES THEREIN COMMUNICATED FROM TIME TO TIME TO THE REGIONAL OFFICE, AND THE DEFECTS AND INACCURACIES



Audit Report under Rule 19

- Report is not in the nature of averments and expressions of the opinion on maintenance of accounts, true and fair view, etc.
- Report is in the form of questionnaire.
- In order to answer these questions properly, an auditor has also to verify certain records and provide comments.



Audit Report under Rule 19

- Whether the report under Rule 19 will fall under Audit or Review engagement under new framework of auditing standards?
- Whether the Form in Schedule IX-C, which is Statement of Income liable to contribution for the year requiring signature of Auditor is a part of Audit or Compilation?




Role of Auditor

- Apart from Audit, he is expected to perform additional verifications/certifications and some other duties.
 - Certifying Statement of Contribution
 - Certifying the 'Corpus Donations' u/s. 58
 - Issuing 'Utilisation Certificate' for various grants received
 - Guiding trustees for routine secretarial work



Audit under Societies Registration Act, 1860

- Rule 12D and Rule 12E inserted by Government of Maharashtra in 1968
- Govern maintenance of accounts and audit.
- A society registered under Bombay Public Trusts Act, 1950 is also required to comply with latter act.



Rule 12D - Contents

- Every governing body is entrusted with the duty of maintenance of proper accounts.
- Society Registrar to prescribe the format and contents of such accounts.
- Accounts to be balanced every year on 31st March.
- Accounts to be audited by a Chartered Accountant or such other person as authorised by State Government.



Rule 12E - Contents

- It shall be the duty of the Auditor to prepare a Balance Sheet and Income and Expenditure Account and forward the same to the Registrar.
- Auditor shall specify all cases of irregular, illegal or improper expenditure or failure or omission to recover monies or other property belonging to society or of loss or waste of money or other property thereof.
- He shall also report whether such expenditure or waste was caused in consequence of breach of trust or misapplication or any other misconduct on the part of governing body.



Audit under Income Tax Act, 1961

- In addition to respective acts, an audit under provisions of Income Tax Act, 1961 is also applicable as under –
 - U/s. 12A(b)
 - U/s. 44AB
 - U/s. 35AC



S. 12A(b) of Income Tax Act

- Where the total income of the Trust as computed without giving effect to the provisions of S. 11 and S.12 exceeds the maximum chargeable to tax in any previous year, the accounts of the trust for the year shall be audited by a Chartered Accountant.



Report

- The report shall be in Form 10B as prescribed under Rule 17B of Income Tax Act, 1961.



Contents of Audit Report

- Form 10B is in 2 parts.
- Part 1 – Audit Report expressing opinion on true and fair view in respect of Balance Sheet and Profit and Loss Account.
- Part 2 – Annexure requiring the auditor to state the year's surplus, accumulation of income, utilisation of income (application); and whether any income or property was used for the benefit or specified (excluded categories) persons.



Audit Report in Form 10B

- This report is to be furnished along with the Return.
- It is possible to have the accounts audited by one auditor and to get the report in Form 10B from another auditor.
- Format of Audit Report in Form 10B is different from the one prescribed SA 700 [Old AAS28]



S. 44AB - Audit

- It would apply only if the trust has income chargeable under the Business head.
- However, other view is that section will apply if a trust carries on a business irrespective of the fact that the income there from may continue to enjoy exemption.
- ICAI supports the latter view as per the publication 'Issues on Tax Audit'.



S. 44AB - Audit

- S. 145 as to the Method of Accounting (cash or accrual) also applies to Trust.
- ICAI has recommended insertion of 2 paragraphs in the audit report where cash basis is followed.



S. 35 & Rule 5D – Income Tax

- An institution carrying out scientific research and claiming eligibility for deduction u/s. 35 of Income Tax Act, 1961 is also required under Rule 5D to get its accounts audited from Chartered Accountant.



S. 35 & Rule 5D/5F – Income Tax

- Such institution is also required to maintain a separate statement of donations and amount applied for scientific research and a copy of such statement duly certified by the auditor shall be submitted along with the audit report. Similar provision exists in Rule 5F.



Audit – Foreign Contribution Regulation Act, 2010

- It governs acceptance and utilisation of foreign contributions or foreign hospitality by certain persons or associations.
- This act is a national security legislation.
- The act and its implemental are in the administrative control and domain of the Ministry of Home Affairs, Government of India, New Delhi.
- One should exercise extreme care and caution in dealing with foreign contribution from the time of its receipt to its final utilisation.



Foreign Contribution - FCRA

- Foreign Contribution is the contribution, donation, gift, presentation or transfer of a like nature received from a foreign source – not being an Indian Citizen nor from Indian Association, organisation, society, trust, money (in the form of either Foreign currency or Indian Currency), foreign security or an article given as gift.



Foreign Contribution - FCRA

- The main idea behind this regulation is not to ban or prohibit any foreign contribution for really genuine purposes but only against those meant for influencing our elections, our government or our electoral representatives or any other individual or association in important areas of our national life.



Registration under FCRA

- Once an organisation is registered under the act, there are many things the organisation should do regularly to ensure continuity of registration which include, inter alia, maintenance of proper books of accounts and audit thereof as also filing of prescribed returns periodically.



Accounts & Audit - FCRA

- S. 13 – Maintenance of Accounts by receipt of Foreign Contribution.
- S.14 & 15A – Inspection of Accounts
- Form FC 3 – Account of Foreign Contribution with the Certificate by Chartered Accountant (Rule 4a)



Form FC – 3

- The form contains a Statement of Foreign Contributions received during the year with the breakup of the same purpose wise as well as donor wise.
- Name and Address of donor, purpose for which the contribution is given, date of receipt and amount of receipt is also required to be given



Form FC – 3

- Country wise break up of the foreign contribution received should be furnished.
- In regard to individual donors, foreign contributions during the financial year received exceeding Rs. 1 Lakh are to be reported.
- Chief Functionary who is an officer bearer should make out the application in his name.
- Chartered Accountant should certify the contents of the Form.



Form FC – 3

- Annual Form FC – 3 is required to be filed on or before 31st July every year for the previous financial year.
- In addition, following documents should be submitted –
 - Audited Balance Sheet and Receipts & Payments Account
 - Country wise and donor wise receipts of Foreign Contributions
 - To be filed in duplicate with the Home Ministry.



Form FC – 6

- This form is required to be maintained for receipt and utilisation of articles received as Foreign Contribution.
- Its particulars form part of Form FC – 3.
- Hence, this is also required to be checked by the Auditor.



Other significant Laws

- By virtue of type or location or any other factor, there are other laws, which are also applicable to the NPO.
- For.eg. Muslim charitable trust falling under Wakf Act, Society in Rajasthan coming under Rajasthan Societies Registration Act, 1958.
- Literary/scientific/charitable society in Kerala falling under The Travancore Cochin Literary Scientific and Charitable Societies Registration Act, 1955.
- Compliances under such relevant laws also needs to be observed.



Issues in accounting and auditing of Charitable Organisations

- In spite of promulgation of various regulations, standards, guidance notes and amendments from time to time, the accounting and auditing of charitable organisations gives rise to certain issues.
- The issues may have been dealt with in a number of ways by various entities but in view of introduction of CSR in Companies Act, 2013, the issues would arise in larger proportion and would certainly deserve application of mind.
- Some of them are dealt with here after.



Issues

- Issues in application of Accounting Standards (AS) –
 - AS-1 Accounting Policies
 - AS-3 Cash Flow Statements
 - AS-5 Net Profit or Loss, Prior period items
 - AS-10 Fixed Assets
 - AS-6 Depreciation
 - AS-12 Government Grants
 - AS-17 Segment Reporting
 - AS-18 Related Party Disclosure
 - AS-22 Taxes on Income
 - AS-23 Investment in Associates in Consolidated Fin Stmt
 - AS-24 Discontinuing Operations
 - AS-27 Financial Reporting in JV



Issues

- Application of accounting standards
 - Accounting policies are still not disclosed in many cases and insufficiently or improperly disclosed in certain other cases.
 - Interest accounting inconsistent from year to year.
 - Depreciation accounting and capitalisation of costs for fixed assets still differ from year to year.
 - Cash v Accrual.
 - Accounting for Govt. Grants is not in compliance with AS 12.
 - Improper disclosure of donations received in kind for distribution to poor segment of society and undistributed stock of such items.
 - Valuation of foreign exchange assets as on date of Balance Sheet or surplus/deficit due to fluctuation in currency rates not accounted satisfactorily.



Issues

- Application of Standards on Auditing
 - Insufficient documentation
 - Absence of appointment letter for year under audit
 - Insufficient working papers
 - Absence of qualification in cases of non compliance with AS or format of accounts
 - Improperly drafted audit report under SA 700
 - Casual approach in preparation of Financial Statement
 - Audit plan, Check List, Engagement letter, Management Representation letter and such other documents not available
 - Insufficient compliance with regulating laws as regards maintenance of records or other compliances by charitable organisation and casual approach by auditor.
 - In view of applicability of Right To Information Act, 2005 (RTI) to organisations substantially financed by government, auditors' liability increases.



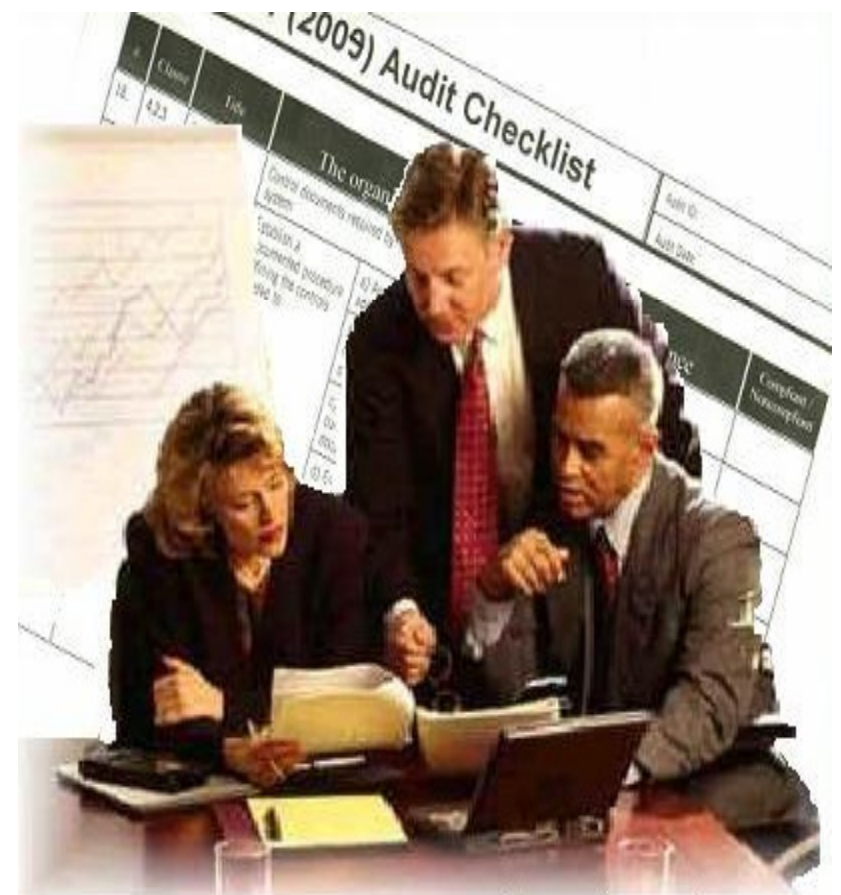
Issues

- Charitable Organisation related issues –
 - Insufficient manpower
 - Casual approach towards objects of the entity
 - Insufficient resources
 - Non awareness in respect of changes in accounting and auditing compliances and government regulations
 - Differences in members of Management
 - Lack of awareness in respect of tax laws and their compliance
 - NPOs may be exempt from tax but not from laws like FCRA, PMLA and Income Tax Act in KYC and such matters. Hence, improper accounting may pose problems to management and auditor as well.
 - In view of lack of proper internal control, employees take advantage by resorting to malpractices and organisations face music.
 - The list is growing and issues rising lest timely proper action is taken. . . .

Practice Management-I

Environmental Pressure

- Competition Pressures
 - To acquire and maintain clients
 - Cutting costs where integrity is impaired
 - Provision of non-audit services to clients
- Timing of completion of Audit Work
- Audit Fees Vs Cost of Compliance
- Heighten Regulations



Practice Management-II

- Maintaining Adequate Documentation
- Implementation of Standards
- Time Management





Audit Documentation

- Legal Defence for a practitioner
- Standardisation of working papers –
 - Checklist
 - Specimen letter
- Document profile of client
- Document significant observation
- Cost of Documentation




Implementation of Standards

- Prepare a checklist
- Update checklist regularly
 - Hold group meeting
 - Attend study circle meetings
 - Read literature
- Record compliance in respect of each client

Time Management

- Time Recording
- Matching actual time spent with budgeted time
- Holding meetings with client after completion of audit





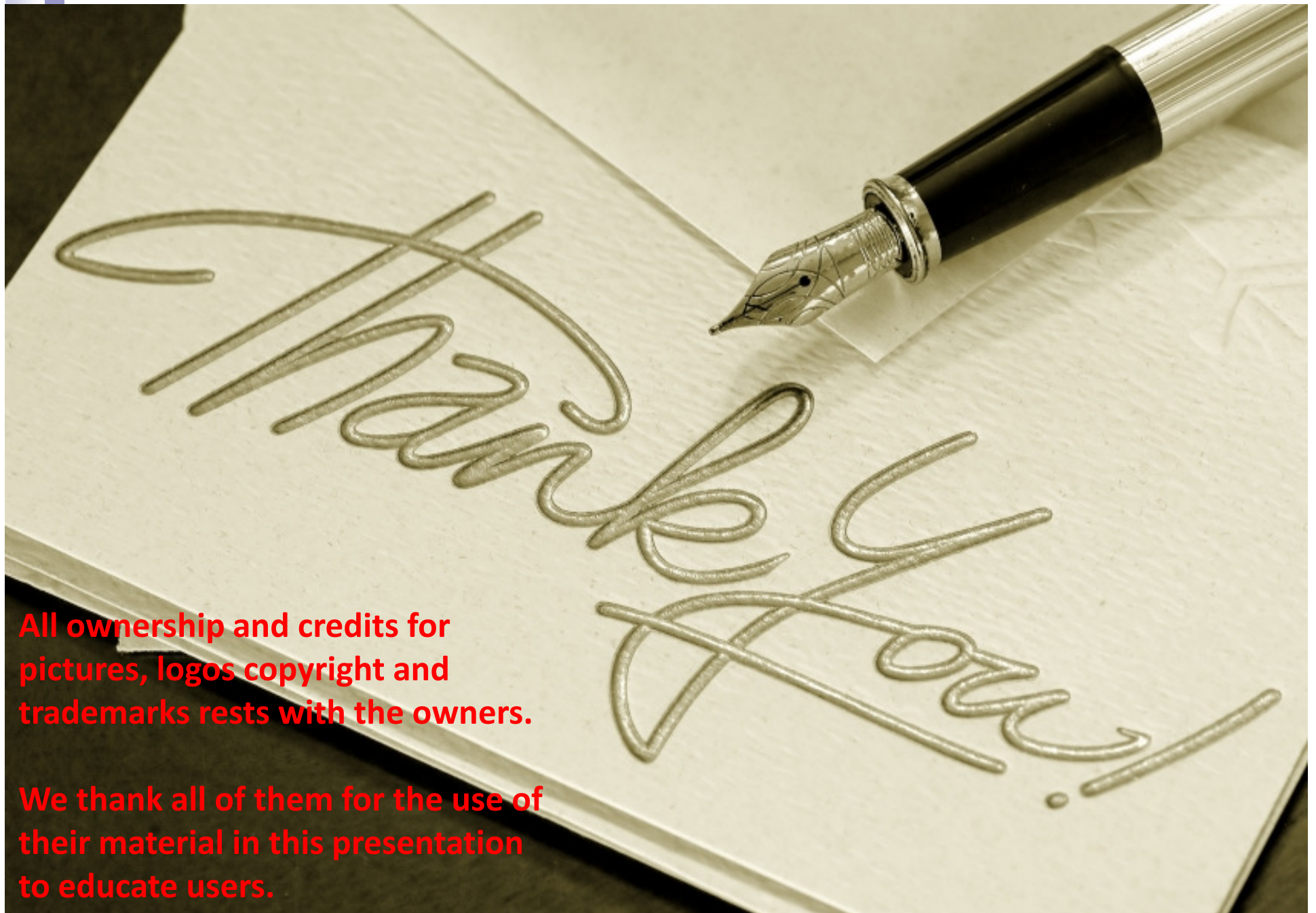
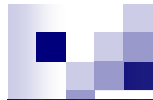
Concluding Observations

- Apply Professional Judgment
- Technical knowledge, skill and experience
- Intuitive skills – To deal with any situation
- Nose for Truth
- Auditor Responds – Auditee reciprocates

It is better to be careful lest it costs you

Final Thoughts....





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