

Donor Due Diligence

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Understanding Organisation Due Diligence for Donor Funding

https://open.spotify.com/embed/episode/1Np9guGt58nlO3lzlCxYv4?utm_source=generator

<https://www.youtube.com/embed/xTk8cZTfY74?si=1oFNOltdF4-V0xzP>

Session layout

1. Donor landscape in India
 2. Overview, rationale, importance, process, being ready
 3. Institutional areas covered during due diligence viz.,
 - Constitutional
 - statutory and regulatory
 - Mission, Vision and core values
 - Governance
 - Policies and procedures
 - Audit and assurance
 - state of health-financial statements
 - Visibility & Reputational
-

Social sector investment in India

- Total social sector investment (expenditure) in FY 2023: Rs. 23 lakh cr (8.3% of GDP) showing annual growth rate of 13% versus need of Rs.35 lakh cr as per Niti Aayog social funding target at 15% of GDP.
 - Govt sector: 95%
 - Private Sector:5%
- Total private funding: Rs.1,21,000 cr in 2023E with category breakup as follows:
 - CSR-23%-Rs. 28k cr
 - *HNI/UHNI-28%-Rs.34k cr
 - Retail-30%-Rs.36k cr
 - Foreign-19%-Rs.23k cr

(Source: India Philanthropy Report 2024-BAIN & Co)

*HNI/UHNI includes Family Foundations

-HNI-net worth of Rs. 5 cr, -VHNWI-net worth between Rs. 5 cr and Rs.25 cr, -UHNI-net worth above Rs. 25 cr

So which are the donor categories in India

- Government
- Family foundations
- CSR
- Retail
- Foreign contribution

Donor due diligence is imperative for all above funding entities also considering specific regulations maybe except retail.

What donors look for before funding NPOs

- **Cause**-where do you find them-s.2(15) Income Tax, Schedule VII to Section 135 for CSR, Purpose under FCRA-CREES, charitable activity defined in GST Notification, permitted

activities for SSE regn

- **Transparency**-see through
- **Safety**-desired results through funds-fiduciary
- **Communication**-interface, understanding
- **Measurable results**-tangible and evidence based
- **Sustainability**-desired behaviour firmly seeded among beneficiaries/TG

Due diligence

1. Literal meaning of due diligence is '**required carefulness**' to **avoid harm or loss**
2. Due diligence is universal whether it is for profit or not for profit
3. In donor funding parlance, due diligence **is scrutiny/evaluation** of an organization and its work by a donor for **selection to partner** on an **engagement**.
4. The key areas evaluated during donor due diligence
 - Organizational due diligence
 - Programmatic due diligence
5. Common scenarios for donor-donée engagement
 - Donor reach out to organization directly
 - Organization reach out to donor directly
 - External agency hired by donors reach out to organization
 - Organizations apply for grants against EOI/RFP placed in public domain

Rationale for org due diligence

Objective for org due diligence

- Understand the organisation to determine **suitability** for making grant award
- Mitigate **risk**
- Ensure funds are used **effectively** for the intended **purpose**
- **Remove bias** in decision making
- Opportunity to build mutual **trust** and lay out **expectations**

- From the point of grantee, it is an opportunity to **showcase, understand** and **overcome shortcomings**

Data collection for due diligence

Methodologies for data collection for due diligence

1. Desk review through secondary data
2. Data obtained from organisation
3. Self-assessment checklist obtained from NGO
4. Scrutiny of audit/assurance reports of past/current donors
5. Onsite visit/meeting org leadership for org due diligence
6. Field visit for programmatic due diligence for a pending grant proposal

The exercise maybe conducted by donor staff or third-party professionals

Process of org due diligence

1. Begins once a proposal is submitted against EOI or standalone as pre-award activity of the grant management life cycle
2. Conducted by grantor before formal engagement with a grantee
3. Involves detailed scrutiny for various aspects of compliance, finance etc
4. Hard and soft due diligence-quantitative data vs qualitative factor

Areas covered during Org due diligence

1. Constitutional
2. Statutory and Regulatory
 - Registration/approval
 - Compliance
 - Registration related
 - Constitution related
3. Mission, Vision and core values

4. Governance
5. Policies and Procedures
6. Audit and Assurance
7. State of financial health-financial statements
8. Visibility

Constitutional

1. Type of charitable organisation permitted in India as per applicable law:

- society
- trust
- section 8 company

Each type of entity has its unique features. We are talking of public charitable or religious cum charitable institution but not private or religious institution. Mere constitution does not entitle the entity to benefits like tax exemption, FC receipts etc unless compliance of such specific laws is ensured.

2. Registration/incorporation documents-MOA C RCR for society, Trust deed for trust and MOA and AOA for section 8 company

These documents is charter and rules and procedures for running the entity

3. Mandatory provisions-name, state, geography, objects, General body, Governing body, Powers and Duties, Accounts, Banking, Audit, Dissolution, irrevocability for trust.

Very important that constitution documents are complete

4. Registration of constitution documents with appropriate authorities as per statute and state procedures-sub registrar or charity commissioner for trust deed, deed and not trust is registered, Registrar of society or as prescribed for society and ROC for section 8 company both for section 8 License and COI

5. Knowing your registration no and date is crucial-like for a trust

- Modification of incorporation documents and compliance for such modification under various laws-constitution related authority, Income Tax, FCRA etc

- Renewal of registration as maybe required by state law-applicable mainly for society form of organisation
- Vintage of organisation matters

2a. Statutory Registration/Approval

- Registration/approval for Income exempt from tax-new regime wef 1.4.2021:
 - 12AB registration and period of validity-10A objects mentioned is important
 - 80G approval and period of validity
 - 10(23C) approval cases merged with section 11-13 wef 1.10.24, 10(46), 35 for scientific, social, statistical research, still some donors are asking about 35AC registration (revoked in 2016 and no benefit post 31.3.2018)
 - Form 10A as filing application and Form 10AC as approval for re/registration/approval of existing
 - charitable entities for tax exemption under Income Tax Act
 - Understanding provisional and regular registration and related provisions very important since validity itself comes into question.
 - Form 10AB as filing application and Form 10AD as approval for renewal-3 years for provisional registration/approval and 5 years for regular registration/approval, modification of objects clause.
 - Institutional areas covered during due diligence-2- Compliance
 - Each registration/approval will be unique to a particular section
 - Very important to understand and adhere to terms and conditions of issue of registration/approval since any adverse decision could pose exertional risk to the organisation .
- FCRA registration
 - Nature of activity-ensure congruity between charter, 10A and FC-3A/C regarding objects/purpose
 - Period of validity of registration
 - Organisation of Political nature, public servant on Board
- EPF, ESIC, PT, SCE Act
 - EPF and ESI registration based on threshold although there is greyness about applicability of ESI Act to charitable establishments, PT registration in concerned

state and SCE license and display for SCE Act. PT and SCE are state acts

- NGO Darpan Registration
 - Obtain UIN by registering on Niti Aayog's Darpan portal. Mandatory for NGOs-seeking govt grants, FCRA registration and reporting, opening and operating bank accounts which is responsibility of the Bank/FI under PMLA and for 80G approval
- PAN, TAN
 - For deduction and payment of income tax
 - See date of incorporation in PAN matches with constitution document. For section 8 company, CIN, PAN and TAN all mentioned in COI
- GSTIN
 - Registration for making incidental business-taxable supply (threshold) unless exempt by Notification
 - Notification No 12/2017 provides for exemption when (a) org is registered under section 12 A of income tax act and is undertaking charitable activity defined as per GST
 - Understanding what constitutes commercial activity is important else it can jeopardise the charitable status itself
 - Donors specially CSR need not setup service contracts and insist on GST and TDS since grants are not within the definition of taxable supply under GST Act
- URN for CSR-local area preference
 - Form CSR-1 with MCA to receive CSR funds wef 1.4.2021.
 - Eligibility for CSR funding as implementing agency
- Registration of contract under Apprenticeship Act 1961 if employee strength is above 30
- Registration with SSE-to register and list securities on social stock exchange. Valid for 1 year and renewed thereafter

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Areas of Internal controls which are focus during Donor Financial Due Diligence

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Why adhere to filing requirements?

2b (i). Compliance-Regulatory (Reporting)

1. Income tax filing
 - Form 10B/10BB-Annual Audit Report
 - Form ITR-7-annual income tax return
 - Form 10BD-statement of donation
 - Form 10BE-Donation receipt/certificate
 - Form 9A/10 for deemed application/accumulation
 - Form 15CA/CB for making remittance abroad
2. Income tax proceedings-ITR-7 acknowledgement, IT assessment-143(1) and (1A), 143(2), 143(3) etc
3. FCRA
 - Annual Return in Form FC4

- changes through forms FC-6A to 6E-change in name, objects, FC bank, office bearers
 - Renewal in Form FC-3C if covered through blanket permission (31.12.24 at present)
4. TDS/TCS related
 - Monthly challan -Quarterly return
 5. EPF/ESI-ECR for EPF and payment challan for ESIC-15th of following month. Six monthly ESI return (Apr-Sep-11 Nov, Oct-March-12 May)
 6. PT payment as per state requirement
 7. SCE-reporting as per specific state act including annual reporting as required
 8. GST-monthly payment challan based on GSTR-3B, Monthly or quarterly return and Annual GST Return
 9. Gratuity-GGS policy premium based on actuarial calculation for compliance with Payment Gratuity Act
 10. Annual disclosure requirements as per Listing Obligations & Disclosure Regulations (LODR) of SEBI if registered on SSE

2b (ii). Compliance-constitution related

Annual reporting to registration authority

- Trust-where no separate state trust act, no annual reporting
- Society-differs from state to state but generally annual reporting relating to list of Governing Body as at AGM and audited financials as approved by general body
- Section 8 company-e Form AOC 4(audited financial statement within 30 days from AGM), MGT 7 (Annual Return-within 60 days from AGM, AGM on or before 30/9), ADT-1 (Auditor appointment-15 days from AGM), Director KYC (by 30/9)

Vision & Values

Mission, Vision & Core Values of an organisation share the purpose of its existence and its direction and culture.

Why? The above helps donors assess whether there is alignment of organisation with their funding priorities and goals

- **Mission:** The organization's purpose, and how it differentiates itself from others in its industry. A mission statement should be specific and show how the organization will meet the needs of its stakeholders.
- **Vision:** The organization's future goals and what it hopes to achieve. A vision statement sets the direction for the organization to meet its mission.
- **Core values:** The organization's core principles and ethics, and how people in the organization should behave. Core values define the organization's defining features and shape its culture.
- Governance-it is about fiduciary duty and risk management
 - Constitution documents lay down governance structure (general body/governing body) and that the **actual** governance structure in line with such provisions-byelaws for society, trust deed for trust and AOA for section 8 company
 - Understanding and Compliance for provisions relating to **conduct of governance**-memberships, meetings, quorum, notice, minutes, inclusion/exclusion, tenure, conflict of interest etc
 - Roles and responsibilities (powers and duties) of General Body, Governing Body and office bearers
- Delegation to sub committees and reporting
- Policies & Procedures

Formulation, revision as org evolves and implementation in letter and spirit as robust internal controls framework. Policies should facilitate action and therefore policies are dynamic documents evolving with the org.

- Statutory
 - POSH-The Sexual Harassment of Women at Workplace (Prevention, Prohibition and Redressal) Act, 2013
 - Apprenticeship policy
 - Child protection policy
- Others
 - Finance & Admin-Travel, Procurement
 - HR
 - DECI (diversity, equity and inclusion) policy
 - Code of Business conduct/ethics

- Conflict of interest
- Risk Management
- IT, Data Security and Data privacy (DPDP Act 2023)
- Whistleblower
- Anti bribery, anti corruption, Lobbying-importantly for international funding
- Terrorism Financing-for US grants-Designated Nationals and Blocked Persons List maintained by the U.S. Treasury

Policies should be in simple language and easy to understand and follow by all staff categories, that is key.

Audits & Assurance

Type of audit conducted for NPOs

- Statutory as required by Income Tax law
- Internal-depending on size and stage of evolution
- Donor-as per grant contract conditions
- FCRA undertaken by MHA
- CCAG mainly for govt and semi govt entities

Are statutory auditors approved by the General Body and with a formal agreement.

Audit process-periodicity, MRL, ML, independent auditor report and financials with Unique Document Identification No (UDIN) no from UDIN portal of ICAI, ATR.

Red flags, adverse observations, litigations etc pointed in audit reports.

Assurance undertaken-broader range of subjects.

Audit and assurance provide proxy indicators to donors on red flags for deciding to fund or otherwise Often, donors do get in direct touch with auditors.

Annual financial statements-separate for FC funds

Provides insights and assurance on 'state of financial health'

Key points:

- Annual financials is top level disclosure to public to **feel the pulse** (present) and **direction** (future) of an org
- Understand your annual audited financials-at times the leadership struggle to read, interpret and respond although they are signatories
- Required generally for 3 financial years to understand trends
- Period of association of auditor-rotation once every 5 years

Key components of audited financial statements:

Balance Sheet-liability and assets of an org as at a point of time

- Unrestricted/own funds-corpus, reserves & surplus/net asset (excess of income over expenditure)
- Unutilised grants/grants receivables
- Loans and Borrowings
- Current Liabilities and Provisions
- Investments-corpus, accumulation
- Fixed Assets
- Cash and Bank
- Deposits and Debtors (receivables)

ICE statement during a time period

- Grants and donations: trend, expansion of donor base, excessive cash donations/subscriptions
- Other income-interest, rent, business incidental
- Expenditure heads-Presentation based on Functional (why) and not natural (what) heads
- Surplus/deficit

RCP (cash) statement

Movement of inflow and outflow of cash

Accounting Policies and Notes to Accounts

Most organisations do not pay attention to this, many times these are not included in financial statements

Accounting policy exhibits the standards followed for arriving at and presenting various items of financial statements. ICAI has prescribed accounting standards to be followed so that the financial statements are standard, comparable and consistent. Notes to accounts is management's explanatory notes for certain important items of financial statements for explaining and clarifying to the reader.

What do the donors look in audited financials?

- Size and volume trend of organisation
- How much net assets or free reserves is available
- Level of investment
- Fixed assets particularly-land and building
- Level of cash in bank
- Unutilised grant or grant receivable amounts
- Proportion of grant and other income including donation
- Breakdown of expenses-program vs admin
- Current assets other than cash vs current liabilities
- Donors require 3 year projection on fund flows for revenue visibility

Visibility & Reputational-Market due diligence

- Website-Placing statutory registrations, AFS (both conso and FC) and AR for 3 years, accreditations as proactive disclosure
- Social media presence for demonstrating scale and delivery of services
- Partnerships and collaboration-strategic
- Awards
- Accreditations
- Publications
- Testimonials
- Intellectual property-trademarks, patents etc
- Address and contact details including Registered office-is it matching with statutory documents
- Name, contact details of Chief Functionary or point of contact

- IEC demonstrating ecosystem engagement and innovation in approach and interventions

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Preparing for a Successful Financial Due Diligence by Donors with Practical Tips

https://open.spotify.com/embed/episode/0N9A8xKMfLV8eiM8Uh9Uqd?utm_source=generator

https://www.youtube.com/embed/ID7IDCstkr4?si=blk_uVeov7Ubu0lt

Risk-control tangle

- Risk: The **probability** and **potential impact** on achievement of objectives while encountering a threat.
- Risk management fundamentals-**Risk Appetite** is risk profile at org level (willingness to take risk to achieve objectives) and **Risk Tolerance** (ability or boundary to take risk/acceptable deviation from risk appetite) for activity/task. Risk appetite is about “taking risk” and risk tolerance is about “controlling risk”
- Risk management approach is how to bridge the gap between risk appetite and tolerance while making informed decisions (risk capacity)
- Unacceptable Risk: actions beyond the risk tolerance
- Residual risk: The risk which inevitably remains after all reasonable mitigation measures have been taken

What are internal controls

Internal controls are rules, procedures and mechanisms that help mitigate risks (risk management) to an acceptable level. Internal Controls are an integral part of an NGO's planning, implementation, monitoring and achieving desired results

Internal controls help with:

- **Compliance:** Ensuring compliance with laws
- **Accountability:** Responsibility for outcomes/performance of organization
- **Fraud prevention:** Preventing loss of assets
- **Improved Operational efficiency:** streamline business processes, reduce redundancies, and optimize resource allocation
- **Attract capital and funds:** Internal controls assures donors that their funds will be effectively utilized for the intended purpose

Examples of Internal Controls

- **Preventive Controls:** Policies and procedures that include approvals, authorizations, verifications, reconciliations, reviews
- **Detective controls:** Designed to identify errors after event have occurred. These include audits and reviews, account reconciliations, and physical inventorying
- **Corrective controls:** Implemented to remedy problems that detective controls have identified
- **Physical controls:** Involve security measures like locks and alarm systems

What donors focus while reviewing Internal controls during due diligence

- Governance and delegation
- Accounts and Finance
- Costs, Budgets and Budgetary control
- Human Resources
- Procurement
- Inventory and fixed asset management
- Grant and Donor management
- Cash and Bank
- Statutory proceedings and penalties
- Program and finance MIS

- Record keeping and retention etc.

Governance & Delegation

- Current general and governing body members-due process of appointment, change or rotation as per rules with proper documentation. Too long holding of positions is a negative
- Founder as Chief functionary for long duration is evaluated against strategic contribution during such periods
- Key office bearers-Chairman, Secretary and Treasurer-their association,past track record in discharging of roles and responsibilities
- Direct blood relative/relative is a negative-independence of Board is questionable
- Specified person as per section 13 of IT Act-transactions and benefits thereof
- Any beneficial relations with other organisations
- The governing body members list is duly updated with registering authority, Darpan and FCRA
- Number and periodicity of Meetings of general body and governing body as per constitution documents or as per law
- Attendance and Minutes of meetings maintained in minutes register and should be with CEO
- Member Register
- Meetings take up items of business as per roles and duties/responsibilities of the respective body laid down in constitution document

Governance & Delegation

- Sub committees delegated Board responsibility should be as per constitution documents and recommendations through such delegation are duly approved by the governing body. Sub committees could be FAC, HR, Grantee selection etc
- Demonstration of strategic guidance, compliance and internal controls through policies in place
- Public servants on governing board/ executive committee
- Political affiliations of organisation or any of its directors/ trustees
- Affiliations with religious/faith based bodies/organisations

- Does the organisation work attract the definition of political nature/party politics?
- Does the organisation understand the boundaries if its work relates to Advocacy, Rights C Entitlements, Activism etc

Accounts and Finance

- Fund based accounting
- Finance policy and systems in accounts and finance function and implementation in letter and spirit
- Accounting software
- Basis of accounting
- Accounting records-vouchers, supporting bills/invoices for exp, PO/contract, approvals, printouts, filing
- Monthly and Annual Closing of books
- Delegation matrix for approvals
- Maintenance of books of accounts and other records as per Rule 17AA of Income Tax Act
- Qualification and vintage of accounts/finance staff
- Segregation of duties/checks and balances
- Separate accounting for local, FC and business incidental operations
- Data security, Backup and audit trail, Rectification entries in succeeding period
- Concurrent and internal audit
- HO-branch accounting and reconciliation

Costs, Budgets and Budgetary Control

- Understanding the concept of costs-functional and natural heads
- Policy framework for budgeting costs-HR, travel, utilities mainly
- Common cost apportionment as per common cost policy
- Budget formulation and approval process-annual master budget including all projects
- Templates may vary for donors but the basic principles of formulation are same-LOE, unit of measurement and unit cost for an activity, budget by activity and budget line
- Budget monitoring process-budget vs actual derived from software

- Expenditure reporting vis-à-vis budget estimates to donor-rolled up or detailed
- Budgetary control process-propose action based on tolerance/variance permitted which may vary by donors

Human Resources

HR policy is a key policy that donors look for which details

- Mission, Vision C Values
- Org structure-updated
- Processes for Recruitment, selection, engagement contract
- Employee vs consultant vs contractual dilemma
- Compensation and breakup-compliance with social security laws
- Employee benefits-leave, insurance, gratuity
- Payroll and allocation of employee costs for shared HR
- Attendance records (timesheet for foreign donors) by donor projects
- Performance appraisal
- Disciplinary action
- Employee strength currently including in finance function vs org structure

Understanding of various social security laws-central and state is essential so that policy and procedures are as per law

Team due diligence: leadership, experience, alignment with mission, vision and culture values, transparency etc

Procurement

Procurement Policy

- Donors fund assets and inventory also in grant budgets
- Sample procurement transactions insisted by donors to validate policy implementation

- Team's understanding and compliance of Procurement Policy for goods, services and works
- Does donor insist on following its own procurement policy/Guidelines
- Dedicated admin staff to handle procurement in organisation
- Conflict of interest, ethics and transparency issues

Fixed asset and inventory management

- Distinction between asset and inventory understood by staff
- Acquiring asset and inventory following procurement process laid down in policy
- Recoding, marking, issue and return, upkeep, depreciation, verification, loss, sale due to obsolescence of FA
- Recording, issue and return, verification, disposal of inventory not needed/useful
- Insurance of assets to cover loss
- Recording of land and building in books
- FA presented separately in FC audited financials and annual reporting for FC assets in FC-4

Cash and Bank

- Petty cash-custody, administration and replenishment. Restrict petty cash to meet small payments not feasible using banking channels.
- Reduce cash handling and transactions to bare minimum necessary as good practice
- Bank:
 - Provisions on banking in constitution document-at times it is only nationalised bank, SB account be insisted with Banks
 - Local, FCRA accounts-do's and don'ts
 - See your member list is updated on NGO Darpan
 - Dedicated bank account for grants
 - Recording and treatment of interest in pool account
 - Signatory to bank accounts- see constitution documents-dual signatories, signatories non-related, prefer net banking.
 - Bearer payments-40A(3) provisions
 - Bank reconciliation and follow-up
 - Minimise visit to branch-sometime one person is engaged for banks only

- Bank statements copy for past 2 years insisted by donors to ascertain operations are using banking channels.

Grant and donor management

- Current status of grant funding. Donor funding is a factor of annual budgets and spends for past few years
- Besides historical audited data, donors obtain projections of grants and income in future 3 years also
- Understanding the donor is essential for positioning your organisation
- Understanding and internal dissemination of grant contract
- Grant compliance checklist since accounting, utilisation and reporting will be different for donors-FC, CSR, others
- Accounting for grant-cost centre basis with dedicated accounting staff for big ticket grants
- Program C financial Reporting very crucial-template, periodicity etc for each grant contract
- Timely request for course correction and revision
- Community contribution, leveraging, cost matching help build your case
- Communication is key

Statutory proceedings and penalties

- Income Tax-assessments, proceedings
- TDS deposit and return filing related
- FCRA related
- Social security laws-PF, ESI, PT, Gratuity
- GST related
- Proceedings against chief functionaries and Board members

MIS and software related

- Accounting, TDS, Assets

- HR-Payroll, timesheet, leave, travel etc
- Audit
- Program MIS
- Grant Management for donor entities

Integrated MIS where all parts are on the same app.

Mandatory accounting Record and Retention

- For books of accounts and other documents, there is specific law now regarding what records to maintain, in what form, where and for the period to be maintained and consequences for non compliance since August 2022 vide Rule 17AA by Income Tax Department

The specified books of accounts shall include:

- cash book
- ledger
- journal
- copies of serially numbered receipts, original copy of invoices, etc

Other documents

- Record of all the projects and institutions run by the organisation
- Record of income of the organization during the previous year
- Record of application out of the income during the year
- Record of specified application out of the income of preceding years
- Record of voluntary contribution with a specific direction to form Corpus
- Record of contribution received under 80G(2)(b) being treated as corpus
- Record of Loans and Borrowings
- Record of properties held by the assessee
- Record of specified persons, as per section 13 (3) of the Act
- Any other document

- Form-written form or electronic form or digital form or print-outs or any other form of electromagnetic data storage device.
- Place-shall be kept and maintained at its "registered office". If not at regd office or at various project locations, intimate Assessing Officer in writing, giving full address of the other places supported by resolution of the board
- Period-Kept and maintained for a period of ten years from the end of the relevant assessment year

Donors may stipulate record retention clauses in their respective grant contracts. For other records, specific provision maybe made in policy

Tips for making your organisation due diligence ready

- Understand the background, focus areas and causes funded by potential/prospective donor
- Donor credentials is important-PRC, sin goods etc
- Develop understanding of regulatory framework applicable to donor category
- Ensure all kinds of compliance we have learnt in previous sessions to maximum extent possible. This maybe done in phased manner but dedicatedly and per a plan
- Continuous education of organisation key members on statutory and regulatory changes and action required
- Risk management framework in place
- Be proactive and manage adverse proceedings regarding organisation, staff office bearers and have latest update ready
- Use technology and tools-lot of them are freely available
- Spread your work through social media-low cost and high impact and reach. Show your competitive edge.
- Be progressive, innovative and forward looking (latch on to new ideas and new ways) as environment is evolving)
- Ensure internal controls specially key policies are actually followed and demonstrated in action and on record

- Chief functionary and key staff should have clarity on vision, mission and values of the organisation and its demonstration
- Be prepared upfront-Have a folder of all documents and details that are likely to be asked during org due diligence and also updating them. The folder should have different sections covering the areas that we have studied in past sessions
- Use a generic checklist for org due diligence and make your folder containing sections using the generic checklist. This can be prepared basis past checklist you have received from donors.
- Avoid scrambling for information during donor due diligence exercise
- Reduce undue reliance on auditor or reference to auditor by donor, it adversely affects your chance to qualify.
- Auditors role in due diligence in conveying a message is very crucial. Sit down and have a dialogue with your auditor-it can make or break.
- Be careful in terms of your working style-while donors need you, you need to handle them and their staff with care and that understanding and skill needs to be inculcated among key staff who facilitate due diligence.
- Try to build a new business development team in a gradual manner as your organisation grows. Till a team is setup, have a dedicated staff to facilitate donor due diligence. This brings focus on new business and sharpens your chance of success in fund mobilisation going forward
- If you are too small and cannot pilot/handle fund mobilisation, take help of professionals

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Understanding, Owning and Sharing a Donor Grant Contract Among Internal Stakeholders

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Session layout

- Grant, Grant Management & Pre requisites for a good GMS
 - Fund accounting and fund types
 - Cost and cost types
-

What is a Grant

- Funds given from one entity to another for a public benefit/charitable purpose
- Usually given to a charitable entity or NPO
- Is not an automatic entitlement, it is for an obligation to be discharged
- Grant is trust money-grantor, grantee (trustee with fiduciary responsibility to grantor and beneficiary) and beneficiary

- Grantor does not get direct benefit and grantee is not expected to payback if utilised for the intended purpose
- Grant comes in different forms from different sources-govt (grant-in-aid), retail, corporate, foundation
- Are awarded directly or through a competitive process

Exchange transaction vs Grant

1. Exchange transaction (as per GST Act) involves:
 - Supply of goods and services
 - Consideration
 - In course of furtherance of business
2. Grant is not exchange transaction since there are
 - No specific beneficiaries
 - Nothing in return from beneficiaries or benefit derived by grantee
 - Not for furtherance of business

Understanding above for grant contract is crucial otherwise contributions maybe considered as exchange transactions inviting GST and TDS implications and also charitable status maybe jeopardised

Grant Management

1. Involves two key players-
 - Grantmakers-grantor/donor
 - Grantseekers-grantee/donee
2. Grant management is a system that includes identifying, applying for and securing grants, adhering to grant conditions, evaluating outcomes.
3. Grant management process in grant management system (GMS) is the grant management lifecycle

Grantmaker vs. grantseeker



Grantmaker

Responsible for **creating grants** and includes setting strategic goals, evaluating regulations, and awarding grants.



Grantseeker

Responsible for **seeking grants** and involves identifying needs, collecting internal information, and applying for grants.

The grant management process



Grant Management Life Cycle

1. Pre award

- Planning-need identification, SWOT, due diligence preparatory etc
- Scout Funding opportunity
- Grant application & review-eligibility and Qualification

2. Award

- Award Negotiation
- Award Decision
- Award Notification/Contract

3. Post Award

- fund request-advance, reimbursement etc,
- Implementation
- Reporting-program and finance
- Post award amendment-key changes and approval, budget realignment, NCE
- Performance/impact
- Closeout
- Reapplication

Principles of grant management

- Accountability, Transparency & Trust for grant funds
- Efficiency & Effectiveness with grant funds
- Compliance with laws of the land
- Adherence to terms and conditions of Grant Agreement
- Necessary Internal controls in place
- Communication & Timely Reporting-narrative and financial as per grant contract

Pre-requisites for robust grant management system

1. Policies & Procedures (Finance & HR)-ensuring strong internal control environment
2. Accounting-ICAI Technical Guide on accounting for NPOs (Jan 2022)-framework
 - Fund based accounting
 - Accrual basis of accounting
 - Maintenance of books of accounts and other records
 - Accounting Standards as framework for recording, reporting and presenting in financial statements
3. Segregation of duties-checks and balances, dedicated finance staff

4. Encourage audit and assurance-risk mitigation

Fund Accounting

NGOs follow Fund Accounting for managing grants

- Fund accounting is an accounting system for recording and tracking project resources (fund) whose use is limited/restricted by specific conditions by donor through a grant contract
- This accounting system emphasizes accountability/productivity over profitability which is the accounting basis for for-profits

Features:

- Separate funds (buckets/compartments)
- Restriction on use
- separate budget established for each fund/project and income credited and expenses debited from the fund
- Transparency
- software for recording
- good internal controls
- monitoring and Reporting mechanisms ensures fund accounting

Type of funds for NPOs

Grant word is not comprehensively defined in Indian laws, referred to as

Voluntary contribution/donation (VC) in Income Tax law. FC under FCRA and CSR fund under CSR law

ICAI has classified funds for NPOs in its Technical Guide on Accounting for NPOs:

1. Unrestricted funds-Funds with no specific restrictions on use (purpose)/time

- Corpus (acknowledged in IT law)-non-refundable, non reducible, reinvestment obligation.

Corpus only

- when specific donor direction that it be treated as corpus by donor
- not income but capital per IT Act
- to be invested in section 11(5) modes of investment
- considered application when replenished
- not application if given to another charity.
- Corpus income shown in I&E
- Donations i.e. no obligations attached, a gift
- Designated/earmarked funds-appropriated and set aside for specific purpose/future, self imposed by management and not binding in law
- General funds-surplus/deficit transferred from I&E which are not designated. Free reserves

2. Restricted funds: funds with conditions/restrictions

- Project/program grants-to be utilized as per terms and conditions of award, Restriction-by purpose and by time. There could be other conditions/restrictions.
Principle of fund based accounting
- Endowment: fund amount cannot be utilized, only income utilized for general/specific purpose as per donor stipulation. The recipient owns it but does not control it.
- Restricted funds maybe:
 - Permanent restriction
 - Temporary restriction: restricts use for a certain period or meeting objectives after which it becomes unrestricted.

Format of financial statements as per ICAI

BALANCE SHEET AS AT_____			
SOURCES OF FUNDS (LIABILITIES)	Schedule	Current Year	Previous Year

Unrestricted funds			
Corpus Fund/General Fund/Designated Funds			
- Restricted funds: Unutilised Grants (Deferred Revenue), Endowment			
- Loans/Borrowings: Secured/Unsecured			
- Current liabilities & provisions			
TOTAL			
Application of Funds (Assets)			
- Fixed assets: Tangible Assets/Intangible Assets/Capital Work-In-Progress			
- Investments: Long Term/Short term			
- Current assets: Loans, Advances, & deposits. Grant Receivable			
TOTAL			
Significant Accounting Policies and Notes on Accounts			

Net Assets

- In NPOs, net assets is like net worth (share capital+reserves & surplus) in case of for profit entities
- Net assets=Total Assets-Total Liabilities
- Net assets means owner funds (capital) although there are no owners in charitable institutions generally
- In an NPO, net assets mainly include corpus and general funds

Format of financial statements as per ICAI

Name of Entity_____			
Income & expenditure account for the period/year ended_____			
Income Schedule	Schedule	Current Year	Previous Year
Grants & Donations			
Other Income-rent, interest, incidental business Income, Fee & Subscription.			
Total (A)			
Expenditure			
Program Exp			
Administrative and General Expenses, Finance costs			
Depreciation & Amortisation Expenses			
Total (B)			

Excess of Income over Expenditure (Surplus) or excess of Exp over Income (Deficit)(A-B) (Net Income in for profit entity)			
Balance Being Surplus (Deficit) Carried to Balance Sheet- General Fund, Transfer to Designated fund, Building fund/ Others (specify)			

Accounting for grant recognition by NGOs in India

Practise followed as per convention-no legal directive:

Option 1: Gross grant treated as income

Option 2: Gross grant routed through Balance Sheet only-asset and liability side settled

Option 3: Grant treated as income to the extent of expenditure while unutilised grant is a liability-- hybrid method

- AS 9 mentions income recognition to the extent of expenditure for grants applicable if there is business/commerce etc
- Follow the principle of prudence in selecting the option for recognition.

Recipient, Sub-recipient and Vendor

Recipient is the organization receiving the grant. A recipient is sometimes called the Prime recipient because it has full responsibility for grant funds. The document evidencing this arrangement is grant contract

Sub-recipient is involved in substantive activities of the award project. The recipient passes on some or all of its duties to the sub-recipient called sub award. All the terms and conditions from the grant award flow down to sub-recipients through a document evidencing it called sub grant contract

Vendor/service provider provides goods/services to the recipient so the recipient can accomplish the project's purposes. Selected terms and conditions might be passed through to the vendor. The document evidencing is a goods/service contract

Cost-Key concepts

- Cost-amount spent to acquire an asset
- Expense-amount spent on regular operations

Classification of expense for NPOs

- Natural expense head—**WHAT** (type of expense) the funds are being spent on- salary, rent, hotel accommodation etc
 - The natural expenses are grouped into group heads like HR cost, Travel, capital cost, office exp, legal & professional etc
 - Group head-Travel-natural expense-conveyance, airfare, meals, accommodation etc
 - Group head-HR-natural expenses-salary, HRA, PF, Gratuity
- Furcation expense head—**WHY** (purpose of expense) the funds are being spent. These include
 - Program cost (program implementation, MEL)
 - Support cost (Accounting, Admin, Fund raising)

NPOs should follow functional expense head for presenting reports, that is what is the basis for their constitution and work. Broadly the functional heads are two-Program/service delivery and Support/Admin & General

Costs for a project for NGO

1. Direct costs (100% direct traceability to a program/support function) to benefit the beneficiary as per project design. No cost if no project.
2. Common/Shared costs-benefit multiple projects
 - shared cost apportionment based on time, space, no of employees/beneficiaries/no of project locations

Understanding and computing direct and shared cost crucial for correct and realistic budget formulation

Apportionment method and share of common cost included in common cost policy

Common cost be reviewed every year within the purview of common cost policy

1. Total cost for a project:
 - a. Direct cost+
 - b. Common Direct cost
 - c. Shared cost apportioned to the project
2. Institutional/Management cost/indirect cost if permitted basis donor grant management policy to address contingency/create a reserve

Other types of cost

Capital & Revenue cost:

Capital Costs: Capital costs are one-time fixed assets purchases that will be used for revenue generation over a longer period- more than one year.

Revenue Costs: are referred to as operating expenses are short-term expenses that are used in running the daily business operations.

Fixed and Variable Costs:

Fixed cost is one that does not change in total within a reasonable range of activity. Since the fixed cost remains constant in total, the fixed cost per unit of activity decreases when the volume increases and vice versa.

Variable cost or expense is where the total cost changes in proportion to changes in volume or activity.

- Historical cost: original cost of asset when it was purchased.
- Sunk cost: money spent that cannot be recovered.
- Marginal cost: change usually decrease in the cost of producing one more unit or serving one more customer.
- Opportunity cost: value of next best alternatives when taking a decision given the resource constraint.

Cost Principles in grant budgeting for NPOs

Costs budgeted for a project grant should be

- **Allowable cost:** costs which are not subject to any restrictions/limitations in the grant award.
- **Allocable cost:** costs which are incurred specifically for the attainment of the objective of the grant.
- **Reasonable cost:** cost which is generally recognized as necessary to be incurred by a prudent person in the conduct of normal business
- **Consistent:** cost applied in same fashion throughout the grant
- **Unallowable cost:** those costs that cannot be incurred and paid under the grant.

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Successfully Managing a Grant Contract End-to-End with Practical Tips

https://open.spotify.com/embed/episode/7CILYYkJM1pOWlqR6AjzKY?utm_source=generator

https://www.youtube.com/embed/-SkbVaxwACU?si=Sm6f_Txlwb-K0GxG

Session layout

- Budget, types, budget monitoring and control
- Grant contract terms and condition
- Challenges and Tips for grant management

Budget basics

- A budget is estimation of revenue and expenses over a specified future period, usually the project period for a grant.
- It is financial plan (blueprint) of the project plan. One need to budget the plan and not vice versa.
- Budget is a Planning (align with objectives) Tool, Control (within policy framework) Tool, Compliance (ceiling) Tool and Mirrors the Financial Report
- A budget covers quantitative, qualitative and cost aspects.

The purpose of budget is to:

- Ascertain reasonable estimation of costs for interventions/activities in a grant proposal/award.
- Segregates costs-direct/common/indirect or OH costs
- Cost matching/sharing (co-financing) for multi donor grant, in kind match.
- Is a framework for donor-donee in a grant award
- Enables course correction based on measurement of actual achievements versus estimates
- Statement of SOF and Estimated Costs
- Enables Recognition-activity, group, period, income, expenditure, deficit, surplus

Pre requisites

- Organisation structure
- Data
- Chart of accounts
- Managerial support
- Formal process for formulation

Types of Budgets:

Activity budget

Activity based budget as the name suggests, covers the costs required for implementing a project activity. In ABB, one looks at resources required for completing an activity and the resources cost

For example, if project strategy is to build capacity of civil society leaders, workshops is an activity. Workshops costs would be towards hiring resource persons, booking a venue, transportation cost, food, lodging and materials and handouts.

Activity Budget for Conducting a Workshop

Particular of Expense	Rate per unit	No of Units	Total in Rs
Trainer Fees	@ Rs 1000 per day	3 days	3,000
Venue	@ Rs 500 per day	3 days	1,500

Particular of Expense	Rate per unit	No of Units	Total in Rs
Rental for Furniture	@ Rs 500 per day	3 days	1,500
Rental for Equipment	@ Rs 100 per day	3 days	300
Catering Exp for Lunch and tea two times	@ 100 per person	55 persons X 3 days = 165	16,500
Conveyance paid to attendees	@ Rs 50 per person per day	50 attendees x 3 days = 150	7,500
Printing of handouts	@ Re 1 per page	50 pages x 50 copies = 2500 pages	2,500
Grand Total			32,800

Line Item Budget

- A Line-item budget presents the budget under broad heads
- It lists income and expenses by category
- Major donors like USAID, European Commission prefer to have their budget templates by line items.
- It helps better tracking for trends in major cost categories

Line Item Budget

Expenses	Unit	# of Units	Unit rate (\$)	Cost (\$)
Human Resources:				
CEO	Per day	3	350	1050
Trainer Fees	Per day	2	200	400
Subtotal Human Resources				1450

Expenses	Unit	# of Units	Unit rate (\$)	Cost (\$)
Travel:				
Trainer Airfare	Per person	1	300	300
Participant Transportation	Per person	30	10	300
<i>Subtotal Travel</i>				600
Equipment and Supplies:				
Materials and hand-outs	Per person	30	15	450
<i>Subtotal Equipment and Supplies</i>				450
Other Costs and Services:				
Venue	Per day	2	300	600
Catering	Per person	30	15	450
<i>Subtotal Other Costs and Services:</i>				1050
Subtotal				3550
Overhead (10%)				355
Total				3905

Other Types of Budget

Incremental budget: Next year's budget prepared by making marginal changes to the current year's budget. The current budget is used as a base to which incremental assumptions are added or subtracted from the base amounts to determine new budget amounts.

Value Proposition Budgeting focuses on allocating the ideal amount of financial resources that provides the highest value to the customer. Another name for Value Proposition Budgeting is Priority Based Budgeting or value based budgeting.

Zero-based budgeting (ZBB) based on efficiency and need at that point rather than budget history. Formulation starts from scratch that only includes operations and expenses essential, no expenses are automatically added to the budget. Cost rationalization

Performance based budget (PBB) considers input of resources and the output of services. The goal is to link funding to results delivered, thus called Outcome based budgeting

Fixed Budget: not modified for variation in actual activity and costs.

Flexible budget: budget changes in response to activity level and costs.

Budget Justification Note

Separate word document to explain the budget nos

- For each line item and activity, provide complete details so that it can be referred for direction and validation during implementation.
- Provides narrative clarification of each budget item demonstrating the necessity of the costs and how they relate to the program activity.
- Provide justification of the calculation of the estimated costs. Note that the estimation should be based on real costs.

Balanced, Surplus and Deficit budgets

- A balanced budget is a budgeting process where total expected revenues are equal to total planned spending.
- A budget deficit occurs when expenditures surpass revenue.
- A budget surplus means there is additional money to spend at the end of the accounting period

Budget Monitoring & Budgetary Control

Budget Monitoring is the process:

- Record actual expenditure versus budget estimates at the line/activity level in books.
- Measure variance using a budget variance report to ascertain positive/negative deviations.
- The workplan delivered helps budget monitoring at a particular point of time.
- Tally software can setup budget and record expenditure. So, the Variance report is real time.

Budgetary Control is the process to:

- Evaluate results of budget monitoring i.e. actual income and expenditure versus original/revised (realigned) budget through variance report.
- Deviation/tolerance triggers action.
- Budgetary control ensures timely action/approvals i.e. budget realignment, reallocation, NCE.

Interest apportionment

- With a single bank account for multiple projects, interest apportionment for reporting to donor has to be made as per well defined method
- Interest apportionment not applicable for dedicated bank account
- Interest can be additive or deductive from grant as specified in grant agreement.

HR cost allocation

- Staff cost for shared HR in a grant should be allocated and charged to donor grants as per project grant in line with common cost allocation policy

- Monthly salary register/sheet with salary allocation of staff to donor projects, deductions/adjustments, variance versus previous month with reasons and banking streams for payout. This is required for donor verification and audit
- Payment of salary out of FC and local funds
- Applicability of time sheets in donor contracts

Robust Grant Monitoring System

Grant monitoring is a process to measure/review performance during grant period. It assesses physical & financial progress, identify risks and corresponding mitigation measures, ensure that funds are used as intended and programs achieve desired outcomes and impact.

Important Tools and Process:

- Complete understanding of terms and conditions of Grant contract
- Budget and LFA clearly known to both finance and programme teams
- Periodic Budget Variance/Deviation Analysis by finance, program team and management review
- Timely course correction through realignment etc through addendum in grant contract.
- Timely reporting-narrative and financial reports as stipulated in grant contract

Grant Contract: General Conditions

MOU versus grant contract/agreement distinction

- Recitals/Preamble
- Definitions
- Grant amount and purpose (including prohibited/disallowed use)
- No Pledge
- Complementary funding
- Designated contacts-for various aspects of the grant
- Conflict of interest and ethical conduct
- Confidentiality
- Term and termination

- Notice of Changes
- Compliance with laws
- Indemnity
- Publications and Licenses
- Visibility, Publicity
- Force Majeure
- Relationship of parties
- Governing Laws
- Notice
- Waiver
- Severability-any clause not enforceable does not make other clauses non enforceable
- Assignment/Delegation
- Acknowledgement-understand and consent
- Counterparts
- Entire agreement
- Arbitration
- Jurisdiction
- Remedies-injunctive relief from court

Grant Contract: Operational Conditions

- Scope of Work
- Deliverables
- Budget
- Eligible Costs
- Grant Disbursement/Reimbursement
- LogFrame and Work Plan
- Basis of accounting
- Separate Books of Account for the project
- Separate Bank Account for Grant Funds
- Bills and Voucher separately and defaced with mention of project
- Limit on Cash Expenditure.
- Treatment of interest
- Procurement rules

- Program/Financial reporting-Often there are templates for interim and final reports
- Input Tax credit
- Monitoring/Evaluation Audit
- Recovery
- Treatment of Fixed Assets-templates in case FA are not allowed to be retained automatically
- Income generated from project activity
- Sustainability
- Closure of grant
- Record and retention

Grant Management Challenges

- Building consistent relationship with grantor
- Turnover and lack of experience of key grant staff
- Use of technology
- Non robust program and finance MIS
- Timely decisions
- Audit findings and Reputational loss

How to manage grant effectively

Managing grant is about maximising impact through

- A thought out project plan
- Clear communication and transparency
- Robust financial management system and practices
- Monitoring mechanism-physical and financial progress
- Compliance with grant terms and conditions
- Final reporting and audit
- Grant closeout
- Impact and Sustainability
- Grantor relationship-Communication is key, be honest
- Create a grant/project calendar
- Create a resource library/repository

- Review before submitting a proposal-a mentor
- Collaborate
- Be on top of your costs while budgeting
- Never say die-Never give up or think others only will get it
- PAVE-Performance, Accountability, Value, Empathy
- What is your unique story, not just chase funding
- Objectivity vs Subjectivity

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