

Overview of Financial Statements of NGOs

Need for financial reporting framework for NGOs

- Financial reporting should provide true and fair view of state of affairs in conformity with generally accepted accounting principles (GAAP).
 - This confirmation is provided by an external auditor as per its opinion in the auditor report.
 - Financial reporting (statements) should provide uniformity, clarity and common understanding to various stakeholders.
 - For NGOs, lack of awareness and uniform applicability, inconsistency in basis of accounting, non-uniform terminology etc. results in financial statements being neither standard nor comparable.
 - Financial reporting framework for NGOs is detailed in *Technical Guide on Accounting of NGOs (Jan 2022)* by ICAI for uniformity and standardisation.
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Components of Accounting Framework as per Technical Guide

(a) Elements of financial statements

- Identify and define the items that should be considered as income, expenses, assets and liabilities in NPOs.

(b) Principles for recognition of items

- These principles lay down the timing of recognition (when) in the financial statements.

(c) Principles of measurement

- These lay down at what amount items should be recognised.

(d) Presentation and disclosure principles

- These explain the manner of presentation and disclosures required.

Note: a, b and c are sector-neutral, while presentation and disclosure differ for not-for-profit and for-profit sectors.

Accounting Terms

Accounting Transaction: A monetary activity recorded in account books with monetary effect on the financial statements.

Sales: Products/services are transferred from sellers to buyers for cash or credit.

Purchases: Transactions to obtain materials and services to accomplish goals.

Receipts: Payments received for providing services or goods.

Payments: Payments made for availing goods/services from vendors, staff etc.

More Accounting Terms

Assets

- Resources/items that the NGO owns. Measurable in monetary terms.
- Two categories: Fixed Assets and Current Assets.

Liabilities

- Legal financial obligations or debts to be settled over time.

- Two types: Long-term and Short-term.

Equity/Capital

- Amount an NGO would return to shareholders after assets are liquidated and debt is paid.

Expenses

- Costs incurred to generate revenue. Examples: wages, payments, equipment depreciation.

Revenue/Income

- Income from normal business operations.
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What is a Financial Statement?

- Collection of summary-level reports:
 - a. Balance Sheet
 - b. Income and Expenditure Account
 - c. Receipt & Payment Statement (cash flow)
 - d. Accounting Policies and Explanatory Notes
 - Accompanied by Auditor Report.
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BS, I&E, R&P

- **Balance Sheet:** Shows assets and liabilities (what you own and owe).
 - **Income & Expenditure Statement:** Income earned and expenses incurred.
 - **Receipt & Payment Statement:** Actual cash receipts and payments.
 - **FCRA Note:** Separate FCRA financial statements required for FC operations.
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Key Points for Preparation of Financial Statement

- Accrual system of accounting recommended.
 - Prepared annually.
 - Include comparative information for at least one year.
 - Different from donor reporting or taxation.
 - Reflect restricted and unrestricted funds separately.
 - Format: Schedule III of Companies Act (used even by charitable organisations).
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MRL and ML

Management Representation Letter (MRL)

- Issued by the client to the auditor during audit as audit evidence.
- Clarifies separation of responsibilities.

Management Letter (ML)

- Sent by auditor to Governing Board highlighting control weaknesses and suggestions.
 - Board should respond and confirm compliance.
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Maintaining Books of Accounts for NGOs

- No prior regulation till FY 21-22.
 - Section 12A(1)(b)(i) added wef AY 23-24.
 - Books must include:
 - Cash book, ledger, journal
 - Receipts (serially numbered), invoices etc.
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Other Required Documents

- Records of projects, income, application of income, voluntary corpus contributions, 80G corpus, loans, properties, specified persons (section 13(3)), etc.
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Bookkeeping Guidelines

1. **Form:** Books can be in written, electronic, digital or print-out form.
 2. **Place:** Kept at registered office. If kept elsewhere, AO must be informed.
 3. **Period:** Maintain for 10 years from end of relevant assessment year.
 4. **Note:** Entities under section 11(4) and 11(4)(a) must keep separate books for that income.
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Accounting Standards

- Necessary for uniformity in preparation and presentation.
 - Prescribed by ICAI.
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AS-1: Disclosure of Accounting Policies

- Fundamental assumptions: Going concern, Consistency, Accrual.

Considerations

- a. Prudence – Do not anticipate profits, provide for all known liabilities.
 - b. Substance over Form – Economic substance over legal form.
 - c. Materiality – Disclose material items that influence user decisions.
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AS-1 Points to Remember

- Disclose accounting policies: depreciation, valuation, employee benefits, etc.
 - Any change affecting financials must be disclosed.
 - If fundamental assumptions are not followed, disclose in statements.
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AS-10: Accounting for Fixed Assets

1. Gross and net book values
 2. Construction/acquisition expenditure
 3. Revaluation method, appraisal year, valuer involvement
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AS-13: Accounting for Investments

- Assets held for income, appreciation or other benefits.
 - Follow classification, cost, disposal, reclassification norms.
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