

Diploma in Financial Management & Accountability

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Course Material



Audit

Paper - VII

Module - IV

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<p style="text-align: center;">UNIT- 9</p> <p style="text-align: center;">SPECIAL ISSUES: FOR AUDIT OF NGOS</p>

9.1. NEED FOR AUDIT OF NGOS

The need for audit in NGOs is more important as:

- a) it deals with the public fund
- b) the fund given to the NGO as donations are exempt from tax and therefore Government has also indirect contribution to the funding of NGOs.
- c) Fund is received for the purpose of beneficiaries who have no direct control in the governance of NGOs.
- d) The person who provides fund also does not have any role in the governance of NGO though they can monitor the funds given by them.

The audit is therefore is the most important tool in the hands of Government, Donors and other Stakeholders to ascertain that the funds received by the NGO are being utilized for the purpose for which these are received.

9.2. REQUIREMENT OF AUDIT

The requirement of audit in NGOs may be classified as follows:

9.2.1. Audit as required by the constitution: In the case of a trust, the trust deed provides for the requirement of audit of the accounts of the trust.

9.2.2. Statutory Audit: Audit of an NGO performed under various statutory laws is called statutory audit and it includes :

- (a) Audit required under Societies Act : The organization registered under Societies Act or the Companies Act are required to get its account audited under the Societies Registration Act or under the Companies Act, 1956.
- (b) Audit required under Income tax Act, 1961 : Income tax Act provides for audit of the accounts if the total income of the charitable institution exceeds the maximum amount which is not chargeable to Income Tax in any previous year.
- (c) Audit under Foreign Contribution (Regulation) Act (FCRA): An audit is also required under FCRA for the foreign contributions received and utilized by the organization.

9.2.3. External Audit: External audits are audits which are required by the various funding agencies by the auditors appointed by them.

9.2.4. Internal Audit: Internal audits are the audits which are initiated by the management by appointing auditors.

In addition to the above audits the NGOs are also subject to financial evaluation and assessment by the various resource sharing agencies.

9.3. APPOINTMENT OF AUDITORS

The person conducting the audit is known as auditor. In case of a charitable institution registered as a trust the authority of appointing the auditor vests with the trustees whereas in the case of charitable institutions registered as a society or as a company, the appointment of statutory auditor vests with the members of the organization.

The person who can be appointed as auditor - Most of the statutory enactments applicable to NGO provides for appointment of a Chartered Accountant as the Auditors of the organization.

9.4. SPECIFIC ISSUES

9.4.1. Propriety Audit: Propriety Audit refers to an audit in which various actions & decisions examined in order to find out whether these are in the interest of the beneficiaries or whether they meet the standard of conduct.

It is essential and inherent function of an auditor to bring to light not only cases of clear irregularity but also every matter which in his judgment appears to involve improper expenditure or waste of public money even though the accounts themselves may be in order and no obvious irregularity has occurred. Propriety Audit, extends beyond the formality of the expenditure to its wisdom, faithfulness and economy". It is thus not sufficient to see that rules or orders of competent authority have been observed, it is also of equal important to see that the broad principles of orthodox finance are borne in mind not only by persons responsible for payment but also by sanctioning authorities.

No precise rules can however be laid down for regulating the course of audit against propriety. Its object is to support a reasonably high standard of public financial morality, of sound financial administration and devotion to the financial interests of the organization. Audit staff in the performance of their duties should, in any case, apply the following general principles which have for long been recognized as standards of financial propriety:

- a) The expenses should not be prima facie more than the occasion demands. Every person of trust is expected to exercise the same vigilance in respect of expenditure incurred from institutional funds as a person of ordinary prudence would exercise in respect of expenditure of his own money.
- b) No authority should exercise its powers of sanctioning expenditure in a manner which will be directly or indirectly to its own advantage.
- c) Institutional money should not be utilized for the benefit of a particular person or section of the community unless :

- i) the amount of expenditure involved is insignificant
 - ii) the expenditure is in pursuance of a recognized policy or custom.
- d) The amount of allowances, such as traveling allowances, granted to meet expenditure of a particular type, should be so regulated that the allowances are not on the whole a source of profit to the recipients. The proper discharge of duties by an audit staff in this field is a very delicate matter and requires much discretion and tact.

9.4.2 Efficiency Audit: Besides the scrutiny of individual transactions with a view to detect cases of improper, extravagant wasteful or uneconomical expenditure, an important function of the auditor is to examine how far the agency or authority whose transactions are under audit is adequately discharging its financial responsibilities in regard to the various projects undertaken by it. It is essential that expenditure incurred on different projects should be examined in audit to ascertain whether:

- i) such projects are being executed and their operations conducted economically; and
- ii) they are producing the results expected of them.

In regard to (i) above, some of the broad lines of examination would be to ascertain:

- a) whether technical estimates or detailed programme and cost schedules are being framed and that the same are adhered to; if not, whether there are adequate reasons for excesses, delays ,etc., or whether these are occasioned by inefficient handling, waste etc. or due to indifferent preparation of original estimates.
- b) whether there have been serious avoidable delays (due to inefficient handling, planning and coordination or the work) in the progress of

works or schemes resulting in increase in the total cost of the scheme or any loss of revenue due to delayed execution or of holding up of other connected schemes;

- c) whether there has been any wasteful expenditure including that resulting from lack of co-ordination amongst several wings of the scheme, such as, staff having been engaged a long time before the procurement of machinery required for running a centre or vice versa;
- d) whether there has been any waste due to some of the facilities (e.g. building, equipment, staff, etc.) on which expenditure has been incurred under the scheme proving unnecessary or going unutilized;
- e) whether the performance/cost compares with the result obtained in respect of similar schemes.

In order to examine in audit as to how far a particular activity is producing results expected of it, it would be necessary inter alia to ascertain :

- a) how far the physical targets (e.g. completion of certain construction work setting up of Village Sangams, Health Care Centres etc.) have been achieved within the estimated time;
- b) how far any returns, where these were anticipated are accruing and
- c) how far the final purpose or objects of the expenditure have been achieved, e.g. in the case of irrigation projects it should be ascertained if the estimated supply of water for irrigation purposes has actually become available as a result of the completion of the Project and whether their actual utilization is to the extent anticipated. Similarly, whether the anticipated number of persons is being trained every year in a technical centre and getting absorbed in the trade concerned to the extent anticipated.

9.4.3. Issue of comparability as a technique of audit: In NGO the funds are received to implement various programmes and/or for distribution of various benefits to the beneficiaries. Though the financial transactions as recorded in the books of accounts are subject to audit but at the same time NGO also maintains records to document the implementation of various programmes like training register to document the conducting of trainings, Master Roll to document the distribution of benefits to the beneficiaries etc. While conducting the audit the auditors should compare the expenses as recorded in the books of account with the quantum of activity implemented as per the various operational records maintained by the organisation to document the implementation of programme.

9.4.4. Issue of identification: Most of the NGOs have more than one funding agencies either implementing the same nature of programmes or for the different types of programmes. It is, therefore, very much required by the auditor to understand the present system being followed by the organisation for maintaining identification of each funding arrangements so that all the receipts and expenses can be identified to a particular funding arrangement and the possibility of overlapping is remote. This issue should be reviewed by the auditor through study of present accounting and internal control system adopted by the organization.

9.4.5. Spending vs. utilization: In NGO utilization is more important than spending. For example if an organization have purchased medicines after making necessary payments then the organization has spent the money. However until & unless these medicines have been used for the beneficiaries these are not being utilized. The auditor should therefore while doing the audit should also focused on utilization of the goods or services being procured instead of only verifying the payments with the supporting documents.

9.5. SELF ASSESSMENT QUESTIONS

- i) Why the need for audit is different in NGOs with the need for audit in Business enterprises?
- ii) What are various types of audit in an NGO?
- iii) Who appoint the following auditors -
 - a) Statutory auditor of a society registered under Societies Registration Act
 - b) Statutory auditor of a society registered as a charitable trust
 - c) Internal Auditor
- iv) Why propriety audits are necessary while conducting audit of NGO?
- v) Discuss the concept of efficiency audit.
- vi) How the issue of comparability as a technique of audit is relevant for an NGO?
- vii) What is the difference between spending & utilization?