AccountAble™

Accounting for Project Grants — Issue # 86; Dec-02; Released: Jul - 03

In this issue

Non-profit organisations in India raise funds for their work in three main ways: 1. Fees from services or sale of products; 2. Donations from public; and, 3. Grants from Government or donor agencies. Some organisations also receive income from assets (such as land or buildings) or investments.

Of these sources, grants form a major source of funds for most mainstream NGOs. Grants may be project grants, capital grants or core-support grants. The present issue discusses accounting and disclosure for project grants in NGO accounts.

What are Project Grants?

Project grants are meant for specific activities. Quite often, these are detailed in a project document and the accompanying budget. In some cases, NGOs also receive core-support grants. Here the NGOs are free to spend the money as they wish, so long as the spending is within the broad parameters of the NGO's objectives.

How are these grants accounted and presented in final accounts? Current practices show three variations:

1. Grants as liability

Under this method, any project grant is treated as a liability and taken to the Balance Sheet. Expenditure incurred during the year is shown as a deduction from this. The unspent balance is carried forward, for spending in the following year.

The presentation under this method is shown in figure 1. Note how the Income & Expenditure does not show the program expenses incurred during the year. This

Balance Sheet as at 31-Mar-03

Liabilities		Rs. (Lakhs)	Assets	Rs. (Lakhs).
Corpus		20.00	Building	18.00
Surplus		0.30	Cash & Bank	10.30
Grant from XYZ				
Opening Balance	5.00			
Add: Recd. this year	20.00			
Less: Spent this year	17.00			
Closing Balance		8.00		
Total		**28.30**	**Total**	**28.30**

Income & Expenditure Account for year ended 31-Mar-03

Expenses	Rs. (Lakhs)	Income	Rs. (Lakhs).
Office rent	0.50	Membership fees	0.25
Salaries	0.60	Donations	1.05
Other expenses	0.05	Misc. Income	0.15
Surplus	0.30		
Total	**1.45**	**Total**	**1.45**

Receipts & Payments Account for year ended 31-Mar-03

Receipts	Rs. (Lakhs)	Payments	Rs. (Lakhs).
Opg. Balance	7.00	Program Exp.	17.00
Grant from XYZ	20.00	Office rent	0.50
Membership	0.25	Salaries	0.60
Donations	1.05	Other expenses	0.05
Misc. income	0.15	Closing Balance	10.30
Total	**28.45**	**Total**	**28.45**

Figure 1: Grants as liability

may mislead people into thinking that the NGO is not very active.

2. Grants as income

Under this method, any project grant is treated as income for the year and credited in full to the Income & Expenditure Account. Expenditure against this grant may be incurred over one or two years. The difference between the grant and expenditure is shown as surplus or deficit.

If this method is followed, then the financial statements may appear as shown in figure 2. The Receipts and Payments Account is not affected, and is not shown again

Note how this method shows a higher figure of surplus for the year. The difference of Rs.3 lakhs is the unspent grant money from XYZ. This presentation gives a misleading impression that this money is available to the NGO for spending.

This method results in a situation where the income of the organisation may go up and down like a wildly bucking horse. This is shown in the line chart. In reality, this surplus is part of ear-marked funds granted by a donor. The NGO can not spend it for a different purpose without the donor's consent. The funds do not belong to the NGO.

In a subsequent year, the NGO may show a deficit, when it spends the unused grant from XYZ. This is shown in figure 5 on the last page. As observed earlier, the surplus and deficit figures do not show the actual financial position.

Balance Sheet as at 31-Mar-03

Liabilities		Rs. (Lakhs)	Assets	Rs. (Lakhs).
Corpus		20.00	Building	18.00
Surplus:			Cash & Bank	10.30
Opening Balance	5.00			
Add: for the year	3.30			
Closing Balance		8.30		
Total		**28.30**	**Total**	**28.30**

Income & Expenditure Account for year ended 31-Mar-03

Expenses	Rs. (Lakhs)	Income	Rs. (Lakhs).
Program Exp.	17.00	Grant from XYZ	20.00
Office rent	0.50	Membership fees	0.25
Salaries	0.60	Donations	1.05
Other expenses	0.05	Misc. Income	0.15
Surplus	3.30		
Total	**21.45**	**Total**	**21.45**

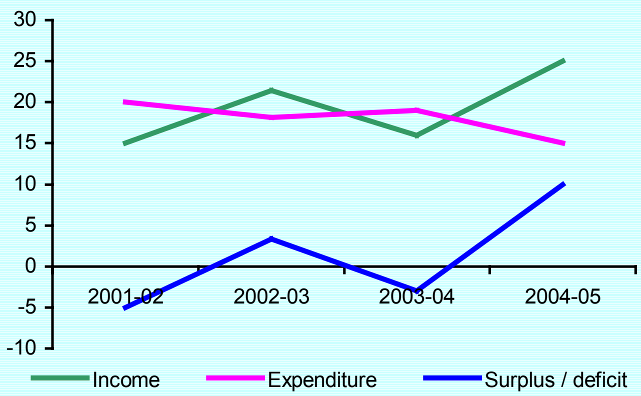

Figure 2: Grants as income (2002-03)
(Receipts & Payments Account same as in Figure 1)

3. Grants as conditional income

Under this method, any project grant is treated as income for the year to the extent it is actually spent during the year. The balance amount is carried forward to the next year as unspent grant.

If this method is followed, then the financial statements may appear as shown in figure 3 below.

Balance Sheet as at 31-Mar-03

Liabilities	Rs. (Lakhs)	Assets	Rs. (Lakhs).
Corpus	20.00	Building	18.00
Surplus	0.30	Cash & Bank	10.30
Unspent grants:			
- XYZ	8.00		
Total	**28.30**	**Total**	**28.30**

Income & Expenditure Account for year ended 31-Mar-03

Expenses	Rs. (Lakhs)	Income		Rs. (Lakhs)
Program Expenses	17.00	Grant from XYZ		
Office rent	0.50	Received this year	20.00	
Salaries	0.60	*Add*: unspent balance brought forward from previous year	5.00	
Other expenses	0.05	*Less*: Unspent balance at end of year carried forward	8.00	
Surplus	0.30	Balance grant for the year		17.00
		Membership fees		0.25
		Donations		1.05
		Misc. Income		0.15
Total	**18.45**	**Total**		**18.45**

Figure 3: Grants as conditional income
(Receipts & Payments Account same as in Figure 1)

Which is better?

Let us now look at how the three alternative approaches present the financial picture. The comparative analysis (Figure 4) gives a broad overview. It shows how the assets, liabilities, income and expenditure would appear in the financial statements under the three alternative approaches.

It is clear from the table that the third method presents a fairer picture:

Tax management…

Apart from fairer disclosure as shown above, another advantage of the third method is that it makes income tax management easier for NGOs. This is because unspent grant balances (from project grants) are not credited to Income & Expenditure Account, but are carried forward. Only non-earmarked income is taken to the Income & Expenditure Account. This way, the NGO is able to see exactly how much it needs to spend[1] in any particular year.

ICAI recommends…

ICAI[2] also recommends the third method in its latest technical guide:

"Since NPOs receive large volume of grants to meet certain revenue expenses, it is recommended that both the grant (*to the extent utilised during the period*) and the relevant expense should be disclosed separately in the Income and Expenditure Account. Such a disclosure would be useful in appreciating the operations undertaken by the NPO during the period." [3]

[1] Tax-exempt organisations in India have to spend at least 85% of their annual income each year.

[2] Institute of Chartered Accountants of India

[3] Page 76; Technical Guide on Accounting and Auditing in Not-for-Profit Organisations. Feb-2003. Emphasis added.

Items	Grants presented in Financial Statement		
	As Liability (method 1)	As Income (method 2)	As Conditional Income (method 3)
Assets are	Shown fairly	Shown fairly	Shown fairly
Liabilities are	Shown fairly	Understated	Shown fairly
Income is	Understated	Overstated / understated	Shown fairly
Expenditure is	Shown fairly	Shown fairly	Shown fairly

Figure 4: Comparative Analysis

Balance Sheet as at 31-Mar-04

Liabilities		Rs. (Lakhs)	Assets	Rs. (Lakhs).
Corpus		20.00	Building	18.00
I & E Account:			Cash & Bank	7.30
Opening Balance	8.30			
Less: Deficit for the year	3.00			
Closing Balance		5.30		
Total		25.30	Total	25.30

Income & Expenditure Account for year ended 31-Mar-04

Expenses	Rs. (Lakhs)	Income	Rs. (Lakhs).
Program Exp.	17.50	Grant from XYZ	14.00
Office rent	0.50	Membership fees	0.25
Salaries	0.60	Donations	1.00
Other expenses	0.40	Misc. Income	0.75
		Deficit	3.00
Total	19.00	Total	19.00

Receipts & Payments Account for year ended 31-Mar-04

Receipts	Rs. (Lakhs)	Payments	Rs. (Lakhs).
Opening Balance	10.30	Program Exp.	17.50
Grant from XYZ	14.00	Office rent	0.50
Membership	0.25	Salaries	0.60
Donations	1.00	Other expenses	0.40
Misc. income	0.75	Closing Balance	7.30
Total	26.30	Total	26.30

Figure 5: Grants as income (2003-04)

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