Financial statement of Not-for-profit Organizations

1 CHAPTER

Meaning of NPO

Not-for-profit organization also known as non-profit organizati0ons refers to those organizations that are set-up for the welfare of the society and are set-up as charitable institutions which function without any profit motive. Non-profit organizations are separate legal entity not owned by any individual or an enterprise. Examples of non-profit organizations are clubs, hospitals, schools, libraries, societies for promotion of sports, arts and culture, etc.

Features of NPO

1. **Main Aim is Service :** The basic aim of non-profit organizations is to serve the society. They are working for the benefit of the society as a whole.
2. **Not For Profit Motive** : Non-profit organizations are formed for some idealistic purposes such as religious, charitable or providing education etc. Earning of profits can never be their aim.
3. **Surplus not Distributed among its Members** : Though earning profit is not the criterion for non-profit organizations, yet there may be excess of income over expenditure or excess of expenditure over income. The former is known as 'surplus' and latter is known as 'deficit'. Unlike other business, surplus or deficit of non-profit organizations is not distributed among its members. They are adjusted in the capital fund of such organizations.

4. **Separate Entity** : The separate entity concept is equally applicable to non-profit organizations. Such organizations are treated as a separate entity distinct from its members.
5. **Management by Elected Persons :** These organizations are run and managed by elected members.
6. **Major Funds from Contributions and Donations :** Usually, non-profit organizations are not self sufficient to run their activities with the revenue generated from their own sources, so they depend upon the subscriptions, donations and grants received from various government departments.

Distinction between profit organization and not-for-profit organization

Profit organization	Not-for-profit organization
A profit organization is operated with the sole aim of earning profit from the business activities.	A not-for-profit organization is operated with the primary objective of benefiting the society as a whole.
A profit organization can be a sole proprietorship partnership or a body corporate.	A not-for-profit organization is an association of person, which can be a club, trust, public hospitals, etc.
The management of a profit organization managed and controlled by a sole proprietor, partner or director.	The management of a not-for-profit organization is managed and controlled by the board of directors, trustees, committees or governing bodies.
The major source of income is from the sale of goods and services.	The major source of income is from donation, subscription, membership fee, charity etc.
The financial statement includes trading account, profit and loss account and balance sheet.	The financial statement includes includes receipts and payments account, income, and expenditure account and balance sheet.
Profit or loss is distributed among the owners i.e. transferred to capital account.	Surplus/deficiency is adjusted in capital fund.

Receipts and payments account

The Receipts and payments account is the summary of cash and bank transactions which helps in the preparation of income and expenditure account. It is prepared at the end of the accounting period and is a summary of cash book, classifying receipts and payments under various heads along with cash and bank balance in the beginning and at the end of the accounting period.

Receipts are recorded on the debit side and payments are recorded on the credit side of the account the account is maintained on cash basis of accounting.

Every receipts and payment, whether capital or revenue irrespective of the period is recorded in this account .The purpose of preparing this account is to ascertain cash in hand and cash at bank at the end of the year.

Salient features of receipts and payments account

1) Nature Receipts and payments account is a real account in nature. It is basically a summary of the cash book. Cash receipts are recorded on the debit side, while cash payments are entered on the credit side.
2) Period in this account, all receipts and payments irrespective of the period to which they pertain are shown.
3) Capital and revenue all cash receipts and cash payments whether of capital nature or of revenue nature are included.
4) Distinction No distinction is made in receipts/payments made in cash or through bank. With the exception of the opening and closing balance, the total amount of each receipt and payment is shown in this account.
5) Adjustment of non-cash items non-cash items such as depreciation, outstanding expenses, accrued income, etc, are not shown in this account.
6) Opening and closing balance it begins with opening balance of cash in hand and cash at bank (or bank overdraft) and closes with the year end balance of cash in hand/cash at bank (or bank overdraft). In fact, the closing balance in this account (difference between the total amount of receipts and payments) which usually a debit balance reflects cash in hand and cash at bank unless there is a bank overdraft.

Limitation of receipts and payments accounts account

1) No Adjustments As the receipts and payments account is not prepared on accrual basis, therefore no adjustments are made in it.
2) Does not show income and expenditure income and expenditure is not shown by this account.
3) No Particular Accounting period Receipt and payment account does not show the amount received or paid only for a particular period.

Format Of Receipts And Payments Account

Receipts	Amt (Rs.)	Payments	Amt (Rs.)
To balanced b/d (opening balance)		By balance b/d (opening)	…
Cash in hand	…	(In cash of bank overdraft)	
Cash at Bank	…	**Revenue Payments**	
Revenue receipts		By salaries	…
To subscriptions (Present, past and	…	By rent	…
future)	…	By postage expenses	…
To entrance fees (in recurring	…	By advertisement expenses	…
nature)	…	By newspapers and magazines, etc.	…
To general donations	…	By repairs	…
To lockers rent	…	By audit fee	…
To general grants	…	By entertainment expenses	…
To sale of newspapers, grass, etc.	…	Bt maintenance expenses	…
To interest on Investments	…	By insurance	…
To sale of old used sports materials	…	By secretary's honorarium	…
To interest on investments	…	By lecture's honorarium	…
To proceeds from entertainment	…	By municipal tax	…
To income from concerts/lectures	…	By gardening	…
To receipts from show	…	By prize distributed	…
To dividends	…	By office expenses	…
To rent	…	By expenses on shown	…
To interest		By miscellaneous payments	…
To miscellaneous receipts	…	**Capital Payments**	
Capital receipts	…	By purchase of fixed assets (e.g.	…
To life membership fees	…	furniture)	…
To subscriptions for specific purpose	…	By sports equipment	…
To donation for specific purpose	…	By investments	…
To grant for specific purpose	…	By books	…
To entrance fees (non-recurring)	…	By loan (repayment)	…
To legacies	…	By building construction	
To endowment fund	…	By balance c/d (closing balance)	…
To sale of fixed assets	…	Cash in hand	…
To sale of fixed assets	…	Cash at Bank	
To receipts on account of special	…		
fund,			
i.e. match fund, prize, etc.			
to balance c/d (closing) (in cash of	…		…
bank overdraft)			

Income and expenditure Account

Income and expenditure Account it is the summary of income and expenditure for the accounting year. Income and expenditure account is a nominal account in nature and serves the same purpose as the profit and loss account of a business organization does. Income and expenditure account is prepared at the end of accounting period to ascertain the net operating results. All the revenue items relating to the current period are shown in this account, the expenses and losses on the expenditure side and income and gains on the income side of the account. It shows the net operating result in the form of surplus (i.g. excess of income over expenditure) or deficit (i.e. excess of expenditure over income) which is transferred to the capital fund shown in the balance sheet. The income and expenditure account is prepared on the accrual basis.

Features if income and expenditure accounts Nature it is a nominal account.

1. No capital items No capital items are entered in this account
2. Debit and credit sides its debit side includes all the expenses pertaining to the particular period and credit side includes all the income pertaining to the same period.
3. Opening and closing balances no opening and closing balances are recorded in it.
4. Only current period items no items either revenue or expenditure pertaining to the past period or the future period is entered is entered in this account.
5. Similar to profit and loss account this account is prepared in the same manner in which a profit and loss account is prepared.
6. Surplus/deficit credit balance is called excess of in income over expenditure', i.e. surplus and debit balance is called' excess of expenditure over income', i.e. deficit.

Format of income and expenditure account

Income and expenditure account
Dr. for the year ending… Cr.

Expenditure	Amt (Rs.)	Income	Amt (Rs.)
To salaries …		By subscriptions …	
(+) Outstanding at the end …		(+) outstanding at the end …	
(-) outstanding in the Beginning …	…	(+) Advance in the Beginning …	
To rent	…	(-) outstanding in the Beginning …	
To insurance premium …		(-) advance at the end …	…
(-) Prepaid …	…	By entrance fees (only that amount Which is treated as revenue)	….
To audit fees	…		
To printing and stationary	…	By donations	….
To honorarium	…	By sale of old newspapers	
To telephone Expenses	…	By hall rent	…
To repairs	…	By sundry receipts	…
To depreciation on Building	…	By deficit (Excess of expenditure	…
To sports material used	…	over income)*	…
To surplus (Excess of income over expenditure)*	…		…
	…		…

Balance sheet

Balance sheet it is prepared by not-for-profit organizations to ascertain the financial position of the organization. It is prepared on the same pattern as that of the business entities. Balance sheet is prepared at the end of the accounting period after preparing income and expenditure account.

Sometimes, balance sheet needs to be prepared at the beginning of the year in order to find out the opening balance of the capital/general fund. The balance sheet shows assets on the right hand side and liabilities are shown on the left hand side along with capital fund or general fund.

The capital fund or general fund is in place of the capital and the surplus or deficit as per income and expenditure account shall be added to/deducted from this fund.

1. Format of balance sheet

Balance sheetAs at

Liabilities	Amt (Rs.)	Assets	Amt (Rs.)
Capital fund		Fixed assets	
Opening balance…			
(+) surplus [or (-) Deficit] …		Building	
…		Opening balance …	
(+) Entrance fees		(+) additions …	
(Capitalised amount …	….	…	….
		(-) depreciation (…)	
Building fund			
Opening balance…		Furniture …	
(+) donation for building …		Opening balance …	
Income from building fund	….	(+) additions …	…
Investment …		(-) depreciation (…)	
		Sale (…)	…
Sports fund			….
Opening balance …		Current assets	…
(+) donation for sports fund …		Cash in hand	…
Interest on sports fund		Cash at bank	
Investments …	….	Subscriptions in arrear	…
….		Accrued interest	…
(-) sports prize awarded (…)		Investments	
Current liabilities		Building fund investments	…
Outstanding expenses		Sports fund investments	…
Rent …	….	Prepaid Expenses	
Salaries …	….	Insurance	
Electricity/water charges …		rent	
Subscriptions received in advance	….		….

Fund based accounting

Fund based accounting the accounting where receipts and incomes relating o a particular fund are credited to that particular fund and payments and expenses are debited to that particular fund, it is known as fund based accounting. These funds are created for specific purposes, e.g. prize fund, sports fund, library fund, building fund, endowment fund, etc. if the fund account has a credit balance, it is shown in the balance sheet on the liabilities side. If the fund account has a debit balance, i.e. the fund is less than the balance, it is transferred to the debit of income and expenditure account.

2. Classification of funds
   Funds may be classified as
   i. Unrestricted funds
   ii. Restricted funds
   Various types of restricted funds are as follows:
   (a) Endowment fund (b) Annuity fund (c) Loan fund (d) Fixed assets fund (e) Prize fund

3. Subscriptions it is the membership fee paid by the members on annual basis. It is the main source of income of non-profit organizations. Subscriptions relating to the current year whether received or not, are shown in the credit side of income and expenditure account. Subscription not received, i.e. outstanding are shown on the assets side of a balance sheet. Subscriptions received in advance for the following year are shown on the liabilities side of a balance sheet.

4. Table showing calculation of subscriptions

Particular	Amount (Rs.)
Subscriptions received during the year (whether in respect of previous, current or future period) as shown in receipts and payments account	….
(+) subscriptions outstanding at the end of the year…	….
Subscriptions received in advance on the beginning of the year …	
(-) subscriptions outstanding in the beginning of the year (…)	
Subscriptions received in advance at the end of the year (…)	….
Subscriptions to be shown in the income and expenditure account	

5. Donations are often received by charitable institution. It is a sort of gift in cash or property received from some person or organization. Donation can be for specific purposes or general purposes.
6. Specific donation When donations received are to be utilized for a specific purpose say, extension of the existing building, construction of a new computer laboratory, creation of a book bank, etc it is called specific donation. It should be capitalized and shown on the liabilities side of a balance sheet.
7. General Donation When donations are utilized to promote the general purpose of the organization, they are called a general donations. They treated as revenue receipts, as it is a regular source of income. It is shown on the income side of the income and expenditure account of the current year.
8. Legacies The amount received by a non-profit organization as per the will of a decreased person is termed as legacy. It is treated as a capital receipt and shown on the liabilities side. However, legacies of small amount may be treated as income and shown on the income side of the income and expenditure account.
9. Entrance Fees Entrance fee also known as fee is paid only once by the member at the time of becoming a member. As entrance fee is paid by member only once, it is argued that it should be treated as a capital receipt and transferred to capital fund. However, it

should be treated as revenue receipt and credited to the income and expenditure account, when the amount is small to cover the expenses of admission.

10. Life membership fees when lump sum amount is paid by the members instead of paying periodic subscription, it is termed as life membership fees. It is treated as a capital receipt and added to the capital fund/general fund on the liabilities side of a balance sheet.
11. Sale of old assets book value of an assets is credited to the asset account. Any profit on sale of an asset is credited and any loss on sake of an asset is debited to income and expenditure account.
12. Sale of periodicals it is an item of recurring nature and shown on the credit side of income and expenditure account.
13. Sale of Sports Material Sports materials are consumable assets. Sale of sports material (used materials like old ball, bats, nets, etc) is the regular feature with any sport club. It is usually shown as an income in the income and expenditure account.
14. Payment of Honorarium Honorarium is the amount paid to the person who is not an employee of the institution and has voluntarily undertaken a service. It is debited to income and expenditure account.
15. Endowment Fund It is a fund arising from a bequest or gift, the income of which is devoted for a specific purpose. Hence, it is a capital receipts and shown on the liabilities side of the balance sheet as an item of a specific purpose fund.
16. Government Grants Various institutions like schools, colleges, public hospitals, etc. depend on government grant for their activities. Grants which are recurring in nature are treated as revenue receipt and credited to income and expenditure account. However, grant of capital nature such as building grant are treated as capital receipt and transferred to building account.
17. Special funds Certain special funds are created for certain purposes/activities, eg. Prize funds, math fund, sports fund, etc. the income earned from such funds is added to the respective fund and not credited to income and expenditure account and also the expenses incurred on such specific purposes are also deducted from the special fund.
18. Special Receipts when there is a receipt of amount by non-profit organizations for special occasions, it is referred to as special receipts, such amounts are credited to a separate account and expenses against these receipts are debited to it. The balance is transferred to the credit side of income and expenditure account.
19. Sale of Old Newspaper Amount which is realized by selling of old newspapers is treated as income and credited to income and expenditure account.
20. Revenue Receipts Revenue receipts are shown on the credit side of income and expenditure account. E.g. rent, interest on investment, proceeds from concerts, shows, etc.
21. Revenue Expenses Revenue expenses are the expenses which are incurred for performing day-to–day activities or expenses which are recurring in nature, e,g. salary, rent, etc. it also includes expenses incurred on the maintenance of fixed assets. E.g. repairs, depreciation, etc.
22. Capital Expenditures Capital expenditures are shown on the assets side of balance sheet, e.g. expenditure on purchase of books, furniture, investments, building, etc.
23. Calculation of the Cost of Consumable Goods Consumable goods are the items which are consumed during the year such as stationery, sports material, foodstuff, medicines, postage, etc.

Non-profit organizations have stock of consumable goods at the end of the year. The income and expenditure account will show correct surplus/deficit, only if the goods consumed are debited to income and expenditure account and closing stock is shown in the balance sheet.

The amount of goods consumed during the year is calculated as follows:

Particulars	Amt (Rs.)
Opening Stock of consumable goods (+) Purchases During the year (-) Closing stock Balance (it is to be shown in the income and expenditure account)	

24. Preparation of the income and expenditure account and the balance sheet from the receipts and payments account with the additional information

Step 1. Prepare the opening balance sheet to find out the balance of capital fund (in cash it is not given) taking and liabilities given in additional information. The differenced between the assets and liabilities is the capital fund or general fund or accumulated fund.

Step 2. Identify from the receipts side, i.e. debit side of the receipts and payments account the revenue receipts and the capital receipts,

i. Capital receipts are shown in the appropriate assets and liabilities account and then incorporated in the balance sheet.
ii. Record the revenue receipts on the income side, i.e. credit side of income and expenditure account after making suitable adjustments so that all revenue receipts for the current year are shown.

Step 3. From the receipts and payments account, identify the revenue and capital payments from the payments side i.e. credit side.

i. Capital payments are shown in the appropriate assets and liabilities account and then incorporated in the balance sheet.
ii. Record the revenue payments on the expenditure side, ie. Debit side of the income and expenditure account, for the current year after making necessary adjustments.

Step 4. There are certain items which do not appear in receipts and payments account are to be recorded and income and expenditure account. They are depreciation on fixed assets- it is to be shown on the debit side, loss on sale of fixed assets- to be shown on the debit side, profit on sale of fixed assets-to be shown on the credit deficit.