

CHAPTER 03

Accountability Aspects of Fund Accounting

03.01 NGOs generally work in fiduciary capacity while implementing developmental projects. The term, 'fiduciary' has been defined¹ as

“a trustee or a person holding the character of a trustee or a character analogous to trustee”.

And the term 'fiduciary capacity' has been defined¹ as

“ One is said to act in a 'fiduciary capacity' or receive money or contract a debt in a “fiduciary capacity”, when the business which he transacts, or the money or property which he handles, is not his own or for his own benefit, but for the benefit of another person as to whom he stands in a relation implying and necessitating great confidence and trust on the one part and a high degree of good faith on the other part. The term is not restricted to technical or express trusts, but includes also

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¹ From 'The Law Lexicon', The Encyclopaedic Law Dictionary – Wadhwa & Company Nagpur, India

such offices or relations as those of all attorney at law, a guardian, executor, or broker, a director of a corporation, and a public officer”.

03.02 The legal connotation of the term ‘fiduciary’ refers to somebody who is entrusted to hold or manage properties or fund for another. In strict legal parlance, NGOs work in fiduciary capacities for donor agencies. Therefore, they have a donor-wise accountability to manage records and report on the basis of individual projects and funds. Because the normal reporting is done as per the law of the country, which does not require project-wise or fund-wise reporting. The statutory audited statements reflect the true and fair view of the NGO as a whole. It does not necessarily reflect the state of each and every individual fund and project. But since NGOs works in fiduciary capacity they are accountable individually to the specific donors apart from the formal accountability towards the state and other stakeholders.

03.03 Fiduciary activities always come with operational accountabilities. When a person manages or utilizes fund on behalf of somebody else he/she has to ensure the following:

- the funds were utilized strictly in compliance with the project agreements and contracts
- the cost of services provided or the administrative component is reasonable and does not involve any element of profit
- in case of investment and properties their title, safety and return are prudent and are as per the project agreement
- project-wise and fund-wise reporting is made as per the project agreement

03.04 A true trustee should provide account of every penny of fund spent or retained and such account should be to the satisfaction of the donor agency.

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03.05 NGOs deal in various kinds of project activities and various kinds of fund are also held at any given point of time. Each project and a fund may have a distinct legal identity and compliance thereof. It is necessary to understand the legal implications of all projects and other funds. Some instances of legal accountability/compliance are as under :

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03.05-1 Corpus Fund : A corpus fund enjoys legal privileges for instance it is totally exempt from tax under Indian Tax Laws. All other voluntary contribution are subject to tax unless 85% is utilized. A corpus fund is not required to be spent under the law but corpus fund being a distinct fund legally created needs to be accounted for as a distinct entity on principles of fund accounting.

03.05-2 Restricted Funds : The project grants received for restricted purposes are bound by the contractual obligations of the project agreement. Therefore, in order to comply with the project agreement fund accounting becomes necessary.

03.05-3 Project Assets : Project assets belong to the donors, subject to the terms of the project agreement. Separate accounting for the assets of each project is necessary in order to meet the legal obligation of the project agreement at the end of the project period.

03.06 The doctrine of *Cy pres* means that the general intent of the donor should prevail, therefore if a definite function or duty cannot be done in exact conformity with a desire of the donor then it should be

performed with as close an approximation to that scheme as is reasonably practicable.

03.07 The Supreme Court of India defined the doctrine of *Cy pres* in *Ratilal Panachand Gandhi v. State of Bombay*, AIR [1954] SC 388, 394 as under :

‘*Cy pres*’ means in some way as nearly as possible when the particular purpose for which a charitable trust is created fails, or it cannot be carried out in whole or in part, the court would not allow the trust to fail but would execute it ‘*cy pres*’ that is to say, in some way as nearly as possible to that which the author of the trust intended.”

03.08 The doctrine of *Cy pres* is an important legal principle for the NGOs, which means that if a charitable activity cannot be done in particular way specified by the donor then it may be done in a way as close as possible. This doctrine was evolved largely in context of the performance of charitable trusts. A trust once created is bound by the trust deed and even the settlor of the trust cannot make any changes. But, suppose some clauses of the trust deed are not possible to be performed then the court may permit to change the objectives through some other similar objectives.

03.09 The doctrine of *Cy pres* provides a strong legal principle about the legal accountability of public fund. NGOs have to work strictly in conformity with the deed or agreement based on which the funds are received. Legally it is not possible to deviate from the project agreement.

03.10 The Indian Trust Act, 1882 is not applicable to public charitable trusts but for procedural purposes, even

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today, the Indian Trust Act, 1882 is one of the most relevant statute. A trust, in fact, is born on the undercurrents of fund accounting. The three certainties of a trust are as under :

- i) Certainty of intention to create Trust
- ii) Certainty of the objects and the beneficiaries
- iii) Certainty of the subject matter of the Trust
i.e. fund or properties must be specified and settled in the deed.

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03.11 It can be seen that having a property or fund is one of the certainties of a trust without which it cannot come into existence legally. And such trust would be null and void. So a public trust is created on the basis of a fund (trust property), which is entrusted to the trustees to be managed as per the trust deed. The trust deed is like an 'endowment fund' where the income generated from such fund is used for the purposes of the trust. The trust as a legal entity comes into existence for maintenance of a fund or a property and it exists as long as the subject matter of the trust i.e. the fund or the property remains intact.

03.12 In today's world an NGO is an enlarged version of the trust as envisaged in the Indian Trust Act, 1882. An NGO simultaneously handles a large number of trusts each one having its specific subject matter or fund. Therefore, the onus is on the NGO to ensure that each fund is maintained individually and independently of other funds.

03.13 The legal creation of an NGO, is in the spirit of a custodian of public money which is precisely what fund accounting tries to capture and present. All the public money at the disposal of the NGO are individually recorded and handled as per the desire of the donor or the conditions fixed by the board or the management.
