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BETWEEN US

Hari's Boat

Once upon a time in a village named Gandak, there lived Hari who was a boatman and his job was to ferry villagers everyday across the river to the market, the school, and the fields.

For the safety and security of the villagers, the local village council had made a few rules for every boatman. Before crossing, they had to check the ropes, record the passengers, maintain the boat, and keep their accounts properly. Hari found these rules irritating. He was an expert boatman and had never had experienced untoward incidents ever in his career.

"Why so much writing?" he complained. "I am here to carry people, not to fill registers."

As the years passed, the council added more requirements. Hari felt the burden growing. Some days, he spent more time keeping records than rowing his boat.

One monsoon evening, Hari decided to ignore the rules. He had passengers waiting and did not want to waste time on the safety inspection or the passenger register.

Halfway across the river, one of the ropes snapped.

The boat began to drift. Fortunately, another boat rescued the passengers. But when the village council investigated, Hari could not show the required inspection record. Because there was no record, nobody could establish when the rope had last been checked or whether it had ever been checked at all.

Hari was fined heavily, had to repair the boat, compensate the passengers, and temporarily stop operating.

Looking at the empty boat, he said, "I thought compliance was costing me time. I did not realise that ignoring it could cost me the boat."

Friends, many a time, we too find ourselves in Hari's state of vexation. Compliance can feel like a burden especially for organisations that are already stretched for resources, people, and time. But for an NPO, ignoring donor requirements and, more importantly, legal and regulatory obligations can come at a far greater cost. Penalties, loss of funding, reputational damage, and even the loss of the organisation's ability to continue its work are very real consequences.

Compliance may sometimes feel like a burden, but ultimately, it is a responsibility that protects the purpose we exist to serve.

Sandeep Sharma

Executive Director

TABLE OF CONTENTS

1	SHARED LEADERSHIP : THE FUTURE OF INDIA'S CSOS	1
2	STRATEGIC PLANNING FOR EFFECTIVE GOVERNANCE	5
3	IDENTIFICATION & EVALUATION OF RISK TREATMENT STRATEGIES	15
4	ACCOUNTING STANDARD 4: CONTINGENCIES AND EVENTS OCCURRING AFTER THE BALANCE SHEET DATE	22
5	IMPACT ASSESSMENT: MOVING FROM SPENDING COMPLIANCE TO OUTCOME ACCOUNTABILITY	29
6	STRUCTURAL CHANGES IN TAXATION OF NPOS	43
7	OVERVIEW OF TRANSITION TO INCOME TAX ACT 2025	47
8	OVERVIEW OF REGISTRATION FRAMEWORK FOR NPOS UNDER INCOME TAX ACT, 2025	55
9	BOOKS AND RECORDS UNDER INCOME TAX ACT, 1961	64
10	ACCOUNT AND AUDIT PENAL PROVISIONS	73
11	CONDONATION OF DELAY IN 80G RENEWAL AUDIT PENAL PROVISIONS	76
12	CONSOLIDATION OF ACCOUNTS OF A SECTION 8 COMPANY	81

01 SHARED LEADERSHIP : THE FUTURE OF INDIA's CSOs

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Introduction

Funders evaluating civil society organisations often look for evidence of scalability, partnerships with the state and measurable impact. When assessing organisational sustainability, they ask about financial resources, funding diversification and the strength of organisational systems.

But one question that is rarely asked is: What happens to an organisation's leadership when its most important leader is no longer there? Is there sufficient leadership depth to ensure continuity?

The long-term sustainability of a civil society organisation depends not only on its financial resources, programmes or partnerships. It also depends on whether it is building leadership beyond a few individuals. Developing second-line leadership and creating systems for shared leadership can reduce key-person risk, strengthen organisational continuity and create the conditions for greater innovation and resilience.

Many civil society organisations begin with a founder's vision, relationships and personal commitment. In the early years, this concentration of leadership can be an organisational strength. A founder may be able to make quick decisions, build trust with communities and donors, attract early supporters and hold together a small team around a compelling purpose. Over time, however, the same qualities that helped build the organisation can also create dependence on one individual. Too much knowledge, authority, decision-making and external credibility may become concentrated in one or a few people. This creates what is often referred to as key-person risk. The question is not whether founders should continue to lead. Their experience and vision may remain invaluable. The question is whether the organisation is also building the leadership capacity, systems and relationships that allow others to lead.

It isn't as if distribution of leadership is absent from civil society sector. On any given day in an NGO, leadership is exercised in places that rarely feature in organisational charts. A programme coordinator decides how to respond when a community meeting takes an unexpected turn. A finance manager interprets a new compliance requirement and advises programme teams on its implications. None of these individuals may carry a formal leadership title, yet each makes decisions that shape the organisation's effectiveness, credibility and relationships.

This is why the question is no longer whether leadership should be shared. In many organisations—especially civil society organisations—it already is. The more important question is whether organisations are intentionally building the systems, culture and capabilities that allow shared leadership to thrive.

1. What Does Shared Leadership Actually Mean?

Does shared leadership mean removing hierarchy? Does it dilute accountability or slow decision-making because everyone must agree on everything?

A growing body of research has challenged the traditional idea that leadership is primarily the work of a single individual.[1] Research on shared, distributed and collective leadership examines how leadership can be exercised across teams and organisations rather than being concentrated only in formal leadership positions.

These terms are often used interchangeably, although they describe different aspects of how leadership is shared. Participatory leadership is about involving people in decision-making. Distributed leadership asks where leadership is located across people, roles, relationships and situations. Shared leadership focuses on who exercises leadership and influence on a particular issue and at a particular moment. Collective leadership focuses on the capacity of a group to lead together towards a shared purpose.

While these approaches describe different dimensions of leadership, shared leadership brings several of these ideas together in organisational practice. It connects participation with influence, distributed expertise with decision-making, and collective purpose with shared responsibility.

In a shared leadership organisation, authority is exercised intentionally at different levels. Decisions are made by those closest to the issue, while overall direction, accountability and organisational coherence remain clear. This does not mean that everyone makes every decision, or that formal leadership becomes irrelevant. It means that authority and responsibility are placed as close as possible to the knowledge and relationships needed to make a good decision.

Leadership becomes something people do together rather than something that only senior leaders provide.

2. Why Civil Society Organizations Need a Different Conversation About Leadership?

The challenges facing the civil society sector today are different from those of even a decade ago. Organisations are expected to build long-term partnerships with communities, engage constructively with governments, respond to evolving donor expectations, navigate complex regulatory environments, embrace technology and demonstrate measurable impact, all while operating with constrained resources.

No single individual, however capable, can successfully hold all these responsibilities alone. Yet many organisations continue to imagine leadership as something that primarily resides in one individual—usually the founder or chief executive—and continue to operate through centralised leadership structures.

The knowledge and relationships needed to lead, however, are often spread across many people. Programme teams may be closest to communities. Finance and compliance teams may understand institutional risks most deeply. Fundraising teams may hold important donor relationships. As organisations grow, this gap between where formal authority sits and where knowledge, relationships and influence reside can become increasingly difficult to manage.

1 https://www.researchgate.net/publication/331703868_Shared_leadership_Reframing_the_hows_and_whys_of_leadership

If every significant decision begins travelling through one individual, decisions slow down and the organisation's ability to learn and adapt is weakened. Knowledge remains concentrated rather than being used across the organisation. The result is not simply leadership fatigue. It is organisational vulnerability. When leadership is concentrated in one person, organisational resilience is also concentrated in one person.

3. Yet if Shared Leadership is so Important, Why do Organizations Struggle to Build it?

One reason lies in our deeply held assumptions about leadership. Across sectors, individual leaders are often celebrated more readily than collective achievement. Awards recognise founders. Media profiles focus on chief executives. Donors may seek reassurance from a single charismatic leader.

These expectations shape organisational behaviour. Within organisations, the barriers are equally real. Leaders may worry about losing control or consistency. There may be a gap between the capabilities of a founder and those of other staff that needs to be consciously addressed. Staff may hesitate to make decisions for fear of making mistakes. Managers who have themselves grown within hierarchical cultures may find it difficult to encourage decision-making at different levels.

Under pressure, even organisations committed to participation can revert to centralised control because it appears faster. Yet centralisation frequently produces its own inefficiencies. Decisions wait for approval. Innovation slows. Staff disengage.

Perhaps the greatest barrier is the belief that shared leadership will happen naturally as organisations mature. Experience suggests otherwise. Shared leadership requires intentional investment—in people, systems, relationships and organisational culture.

4. Learning From Indian Practice

Across India, some of the country's most enduring civil society organisations demonstrate that leadership can be shared in meaningful ways without losing clarity of purpose.

The Self-Employed Women's Association (SEWA), [2] for instance, has long invested in developing leadership from within its membership. Women who begin as members often assume responsibilities within cooperatives, collectives and federations, strengthening the organization while ensuring that leadership remains closely connected to lived experience.
Similarly, Barefoot College [3] has demonstrated the value of recognising community knowledge as leadership. Rather than positioning technical expertise solely within professionals, it has built systems where local knowledge holders become educators, trainers and problem-solvers in their own communities.

These examples also raise an important question for civil society organisations. While many organisations invest in building leadership among the communities they serve, leadership development within the organisation itself may receive less attention. Leadership may be shared in community-facing roles while decision-making remains highly concentrated in other functions.

As one co-leader in an organisation that experimented with shared leadership reflected, “Co-leadership requires sustained and intentional effort to navigate evolving roles, decision-making and accountability.”

2 https://sewabharat.org/what-we-do/grassroots-leadership/
3 https://barefoot.college/

This is an important reminder that shared leadership does not eliminate the need for clarity. In fact, it may require more deliberate conversations about roles, expectations and decision-making. Without these, shared leadership can create confusion or overlap rather than greater ownership. It also requires teams and individuals to work collaboratively rather than competitively with one another.

There are also organisations that help civil society organisations build the conditions for shared leadership and address some of these challenges. These programmes, work with senior leaders to strengthen leadership capabilities, develop second-line leadership, and build coaching and other organisational processes that support leadership development within the organisation.

Organisations that make progress in building shared leadership often strengthen management systems, clarify decision-making authority, invest in leadership development and deliberately create opportunities for emerging leaders to represent the organisation externally.

5. What can Organisations do Intentionally to Build Shared Leadership?

Shared leadership is less about changing personalities than about redesigning organisational systems.

First, organisations need to clarify decision-making rather than simply encourage participation. Teams need to understand which decisions belong at which levels, where authority genuinely sits and who is accountable for the final decision. Ambiguity often creates more hesitation than hierarchy.

Second, organizations need to invest consciously in second-line leadership. Leadership development should not begin only when succession becomes urgent. It should become an ongoing organisational process that includes mentoring, coaching, cross-functional learning and opportunities to lead strategic initiatives.

Third, organisations can broaden external representation. Donors, government officials, partners and networks should increasingly interact with multiple organisational leaders rather than a single spokesperson. This strengthens institutional credibility, develops confidence within teams and reduces dependence on one individual.

Fourth, organizations need systems that support learning. Reflection, experimentation and honest discussion of mistakes can help cultivate leadership throughout the organization. People are more likely to contribute ideas, raise concerns and take responsibility when they feel safe to do so.

Finally, shared leadership requires a shift in organisational culture. Leaders must increasingly see their role not as solving every problem but as creating the conditions in which others can solve problems effectively.

The question, then, is not whether civil society organisations need leaders.. Nor is it whether formal leadership and accountability remain important. The more important question is whether organisations are willing to recognise that leadership already exists in many places—and nurture it to better navigate complexity, respond to change and remain resilient beyond the tenure of any one individual.

02 STRATEGIC PLANNING FOR EFFECTIVE GOVERNANCE

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Introduction

Strategic planning is a crucial component of effective governance in Non-profit Organizations (NPOs). It provides a structured approach for defining the organization's mission, vision, goals and strategic priorities, enabling informed decision-making and the effective allocation of resources.

A well-designed strategic planning process helps organizations align their activities with their mission, respond to changes in the operating environment, and establish a clear direction for achieving their long-term objectives. This article examines the key aspects of strategic planning in NPO governance, including its importance, the frequency of strategic planning, the stakeholders who should be involved, the strategic planning process, and the principles and frameworks that can strengthen the planning exercise.

1. Strategic Planning as Key to Effective Governance in Non-profit Organizations

The link between strategic planning and effective governance in a Non-profit Organization (NPO) is fundamental to the organization's success, impact, and sustainability.

Non-profit Organizations (NPOs) play a vital role in addressing societal needs, advocating for social change, and promoting the common good. At the heart of their success lies the symbiotic relationship between strategic planning and effective governance. Strategic planning serves as the compass guiding an NPO toward its mission-driven goals, while effective governance ensures the prudent stewardship and oversight necessary for sustainable impact.

Strategic planning in NPOs involves the intentional process of defining organizational goals, allocating resources, and crafting action plans to fulfill the mission and vision. It serves as a visionary roadmap that charts the course for the organization's future, providing clarity on its purpose, priorities, and desired outcomes. A well-crafted strategic plan establishes the foundation for informed decision-making, aligning the organization's activities with its core values and overarching objectives.

Governance in NPOs represents the framework of policies, structures, and practices that guide decision-making, ensure accountability, and safeguard the organization's integrity. Effective governance involves a dynamic interplay of leadership, oversight, and transparency, and it is strategically intertwined with the organization's planning processes.

The link between strategic planning and effective governance in NPOs is the linchpin for achieving enduring impact. As strategic planning charts the course for

mission-driven goals and objectives, effective governance provides the oversight and leadership necessary to navigate this trajectory successfully. Together, they form a powerful synergy that propels NPOs toward sustainability, relevance, and the fulfillment of their vital societal roles. As stewards of the public trust, NPOs must recognize and leverage this critical nexus to amplify their impact and contribute meaningfully to the well-being of communities and the advancement of social causes.

In essence, the integration of strategic planning and effective governance is about creating a cohesive and purposeful approach to achieving the organization's mission. It ensures that the organization is guided by a clear vision, operates with integrity, and remains responsive to the needs of its constituents and the broader community.

Importance of Strategic Planning on Governance:

Strategic planning is of paramount importance for effective governance in Non-profit Organizations (NPOs). Below are key reasons why strategic planning plays a crucial role in enhancing governance within NPOs:

	Importance of Strategic Planning	Impact of Strategic Planning
Clarity of Purpose & Direction	Strategic planning provides a clear roadmap for the organization's future direction.	A well-defined strategic plan helps the board and leadership articulate the organization's purpose and direction, providing a common understanding among stakeholders.
Effective Resource Allocation	Strategic planning helps in the efficient allocation of financial and human resources.	By prioritizing goals and initiatives, NPOs can allocate resources to areas that align with the organization's strategic priorities, promoting responsible and effective governance.
Enhanced Decision Making	Strategic planning provides a foundation for informed decision-making.	With a clear strategic plan, the board and leadership can make decisions that are aligned with long-term goals, promoting consistency and coherence in governance decisions.

	Importance of Strategic Planning	Impact of Strategic Planning
Measurable Objectives and Accountability	Strategic plans include measurable objectives and action plans.	By defining measurable goals and assigning responsibilities, strategic planning establishes accountability structures, providing a basis for evaluating progress and promoting transparency in governance.
Adaptability to Change	A dynamic strategic plan allows for adaptability to changing circumstances.	NPOs operating in dynamic environments can adjust strategies in response to emerging opportunities or challenges, demonstrating agility in governance.
Enhanced Board Engagement and Effectiveness	Strategic planning engages the board in critical discussions about the organization's future.	Board members who actively participate in the strategic planning process are more likely to be informed and engaged, contributing to effective governance.
Increased Donor Confidence	Transparent strategic planning can enhance donor confidence.	Donors are more likely to support organizations that have a well-defined strategic plan, demonstrating a commitment to achieving impact and stewardship of resources.

2. Frequency of Strategic Planning in NPOs

The frequency of strategic planning in Non-profit Organizations (NPOs) can vary based on the organization's size, complexity, and the pace of change in its operating environment. While there is no one-size-fits-all answer, strategic planning is generally undertaken at intervals to ensure relevance, adaptability, and alignment with the organization's mission.

Here are some considerations for the frequency and situations where strategic planning should take place in NPOs:

Regular Review:

- **Every 3-5 Years:** Many NPOs engage in a comprehensive strategic planning process every 3-5 years. This allows for a thorough review of the organization's mission, goals, and strategies, considering changes in the external environment and the achievement of previous objectives.

Adaptive Planning:

- **More Frequent Updates:** In dynamic environments or rapidly changing sectors, organizations may engage in more frequent strategic updates, such as annual or biennial reviews. This adaptive planning approach allows NPOs to respond swiftly to emerging opportunities or challenges.

Major Organizational Transitions:

- **Leadership Changes:** A change in executive leadership or significant shifts in board composition may trigger the need for strategic planning. New leaders may bring fresh perspectives and priorities that warrant a reassessment of the organization's direction.

Crisis or Significant Events:

- **Crisis Response:** In response to crises or significant events affecting the organization or its operating environment, NPOs may engage in strategic planning to reassess priorities, address emerging needs, or adapt to new circumstances.

Achievement of Milestones:

- **Completion of Major Initiatives:** Upon the completion of major initiatives or the achievement of significant milestones, NPOs may conduct a strategic review to assess the impact, celebrate successes, and identify new areas of focus.

Changes in External Landscape:

- **Shifts in Funding Environment:** Changes in the funding landscape, donor priorities or regulatory environment may prompt a strategic reassessment to ensure the organization's financial sustainability and relevance.

Programmatic Evaluation:

- **Programmatic Reviews:** NPOs may conduct strategic planning focused on evaluating and refining specific programmatic areas. This targeted approach allows organizations to ensure program effectiveness and alignment with overall goals.

Community and Stakeholder Input:

- **Periodic Community Input:** Engaging stakeholders and the community in strategic planning can be an ongoing process. Periodic community input sessions or surveys can provide insights & perspectives that inform strategic decisions.

Technology and Innovation:

- **Technology Advancements:** Rapid advancements in technology or changes in communication channels may necessitate strategic planning to ensure the organization remains effective in reaching its target audience.

Capacity Building:

- **Organizational Growth:** During periods of significant organizational growth or expansion, strategic planning can help address any challenges or opportunities associated with scaling operations.

Learning and Reflection:

- **Periodic Learning and Reflection**: Organizations may engage in periodic learning and reflection sessions, even in the absence of major triggers, to foster a culture of continuous improvement and organizational learning.

It's important for NPOs to strike a balance between stability and adaptability, recognizing that strategic planning is not a one-time event rather it is a dynamic process that evolves with the organization's needs and external conditions. The key is to be responsive to changes while simultaneously maintaining a focus on the long-term vision and mission of the organization.

3. Strategic Planning: Stakeholders and Perspective

Involving a vast range of stakeholders in the strategic planning process and considering different perspectives is crucial for the success and relevance of Non-profit Organizations (NPOs). Engaging various stakeholders ensures that different perspectives, insights, and expertise are considered, leading to a more comprehensive and inclusive strategic plan.

Here are key stakeholders that should be involved in strategic planning for NPOs depending on the needs of the organization

Board of Directors:

- Board members play a central role in strategic planning. Their governance responsibilities make them key decision-makers, and their insights help align the strategic plan with the organization's mission and vision.

Executive Leadership:

- The executive leadership team, including the executive director or CEO, provides valuable insights into the organization's operations, strengths and challenges. Their involvement is essential for translating the strategic plan into actionable initiatives.

Staff Members:

- Frontline staff possesses a deep understanding of day-to-day operations and direct interactions with beneficiaries. Involving staff fosters a sense of ownership and ensures that the strategic plan is realistic and feasible.

Donors and Funders:

- Donors and funders have a vested interest in the success of the organization. Involving them in strategic planning can help align funding priorities with organizational goals, ensuring financial sustainability.

Beneficiaries and Service Recipients:

- Considering the voices of those directly served by the organization is critical. Reviewing success stories and challenges of beneficiaries provides

insights into their needs, preferences and the effectiveness of current programs, contributing to more client centered strategies.

Experts and Consultants:

- Subject matter experts or consultants can provide specialized knowledge and perspectives. Their expertise can contribute to a more informed and strategic decision making process.

Founding Members or Founders:

- In cases where the organization has founding members or founders, their insights into the organization's history, values, and original vision can provide valuable context.

Effective stakeholder engagement requires intentional communication, transparency and a commitment to inclusivity. By involving a diverse group of stakeholders, NPOs can benefit from a richer understanding of their environment and ensure that the strategic plan reflects a collective vision for the organization's future.

4. Strategic Planning process

The process of strategic planning in Non-profit Organizations (NPOs) involves a systematic and collaborative approach to defining the organization's direction, making decisions on allocating resources and setting priorities to achieve its mission and goals.

It considers various factors such as the organization's mission, vision, strengths, weaknesses, opportunities, threats, and key goals. This process typically consists of the following key stages:

Establishment of a Strategic Planning Committee:

- A cross-functional committee can be formed with representatives from the board, executive leadership, staff, and key stakeholders to guide the strategic planning process. The committee should be diverse, ensuring representation from various perspectives within the organization. Clear roles and responsibilities for committee members should be defined.

Conducting a Current State Assessment:

- This entail understanding the organization's current state, including strengths, weaknesses, opportunities, and threats (SWOT analysis). Data can be collected through input from stakeholders, surveys, interviews, and focus groups. Analysis of internal data like financial reports, performance metrics, etc. can be included. It is also a good practice to use this data for a SWOT analysis.

Defining, Refining Mission and Vision:

- The planning process should also clarify or refine the organization's mission and vision statements to ensure they reflect its core purpose and aspirational goals. Review and, if necessary, revise the existing mission and vision statements. Input can be sought from stakeholders to ensure alignment with organizational values.

Identifying Core Values:

- The strategic planning process also helps to define or reaffirm the core values that guide the organization's behavior and decision-making. This can be done by conducting workshops or discussions to articulate and document core values. The organization should ensure the core values are aligned with the organization's mission and vision.

Stakeholder Analysis and Engagement:

- Part of the planning process is identifying and engaging with key stakeholders to ensure diverse perspectives are considered. This is achieved first by developing a stakeholder engagement plan. The stakeholders are then engaged through interviews, surveys, or focus groups to gather input. Finally, the findings are shared with stakeholders for their feedback.

Setting Strategic Priorities and Goals:

- An effective strategic planning process establishes key priorities and goals that align with the mission and vision. Based on the SWOT analysis conducted through the gathered data, strategic focus areas are prioritized in order to develop Specific, Measurable, Achievable, Relevant, and Time-bound (SMART) goals.

Developing Action Plans:

- Detailed action plans should be created for each strategic goal, including responsible parties, timelines, and resource requirements. The following steps can help develop effective action plans:

  -Break down each goal into actionable steps.

  -Specify tasks milestones & deadlines for implementation.

  -Allocate resources effectively.

Budgeting and Resource Allocation:

- The next step in the process is to develop a budget aligned with the strategic plan to ensure financial resources are allocated appropriately. This begins with estimating the costs associated with each action plan, identifying potential funding sources and allocating resources accordingly.

Risk Assessment and Mitigation:

- Once the budgeting and resource allocation are complete for supporting the defined action plans to achieve the strategic goals and priorities identified by the organization, potential risks need to also be identified to successfully plan the implementation and develop mitigation strategies.

The following plan is recommended for carrying out a risk assessment and mitigation:

-Conducting a risk assessment to identify internal and external risks.

-Develop contingency plans for high-impact risks.

Creating Monitoring and Evaluation Mechanisms:

- Establishing Key Performance Indicators (KPIs) and evaluation criteria is important to track progress and measure success. This can be done by:

  -Defining KPIs for each strategic goal.

- Establishing a regular reporting and review process.

Communication Plan:

- A communication plan can be developed to keep stakeholder informed about the strategic plan. This is done by:

  -Determining the most effective communication channels.

  -Creating messaging for internal and external audiences.

Board Approval and Adoption

- The strategic needs to be finally presented to the board for review, feedback, and approval. A board meeting should be scheduled to discuss and approve the plan, with sufficient time for discussion and incorporation of board feedback into the final version.

Implementation:

- Once approved, the action initiatives outlined in the strategic plan need to be executed by assigning specific responsibilities to staff and volunteers.

Continuous Monitoring and Adaptation:

- Continuously monitor progress, evaluate outcomes, and make adjustments as needed. This can be done by:

  -Regularly reviewing KPIs & evaluating the effectiveness of strategies.

  -Adapting the plan based on feedback, changing circumstances or new opportunities.

Periodic Review and Renewal:

- Periodic reviews (e.g., every three to five years) to assess the relevance of the strategic plan and make updates as necessary should be conducted. Some ideas to conduct these reviews include scheduling strategic planning retreats or workshops to engage stakeholders in the review process.

Regular engagement with stakeholders, flexibility, and a commitment to learning and improvement are key elements of successful strategic planning for NPOs.

5. Principles, Frameworks and Best Practices for Effective Strategic Planning

Developing and executing a strategic plan is a complex process. By adopting some of these recommendations, ideas and best practices, the effectiveness of strategic planning in Non-profit Organizations (NPOs) can be enhanced.

We recommend keeping in mind the following broad principles through the planning process:

Long-Term Vision:

- Having a vision that extends beyond short-term goals, considers the long-term impact of strategic decisions on the organization's sustainability and mission fulfilment.

Flexible and Adaptive Approach:

- Fostering a culture of adaptability is critical. Strategic plans should be dynamic documents that can be adjusted in response to changing circumstances, emerging opportunities or unforeseen challenges.

Regular Monitoring and Evaluation:

- Establishing a systematic process for monitoring and evaluating process, regularly reviewing Key Performance Indicators (KPIs) can help assess the effectiveness of strategies.

Social Impact Measurement:

- Incorporating mechanisms to measure and communicate the social impact of the organization's work. Clearly articulate how the strategic plan contributes to the organization's mission and societal goals.

Additionally, there are several common strategies and frameworks that organizations can use during the strategic planning meeting itself. Here are some widely recognized approaches:

SWOT Analysis:

- Conducting SWOT analysis i.e. Strengths Weaknesses, Opportunities and Threats to assess internal and external factors influencing the organization. Use the insights to develop strategies that leverage strengths and opportunities while also addressing weaknesses and threats.

SMART Goals:

- Utilizing the SMART criteria (Specific, Measurable, Achievable, Relevant, Time-bound) to formulate clear and actionable goals. SMART goals are a widely accepted model for setting objectives that are specific, quantifiable and achievable.

OKR (Objectives and Key Results):

- Popularized by tech companies, OKRs involve setting clear objectives and defining key results to measure progress. It encourages transparency, focus and alignment of individual and team goals with organizational objectives.

Scenario Planning:

- Scenario planning involves developing multiple scenarios for the future considering various possible outcomes and their implications. This approach helps organizations anticipate and prepare for different future conditions.

The Five Whys:

- Rooted in problem-solving, the Five Whys involve asking "why" at every stage to identify the root cause of an issue. This method can be applied proactively during strategic planning to understand the underlying reasons for organizational challenges.

Gap Analysis:

- Performing a gap analysis to identify the difference between the current state and the desired future state. This helps organizations understand what steps are needed to bridge the gapand achieve strategic objectives.

PESTLE Analysis:

- Consider external factorsby conducting a PESTLE analysis (Political, Economic, Social, Technological, Legal, Environmental). This framework helps organizations understand the broader macro-environmental factors that may impact their operations.

Milestones and Roadmaps:

- Developing milestones and roadmaps to outline the sequential steps and timelines for achieving strategic

objectives provides a visual representation of the strategic journey and helps with tracking progress.

Appreciative Inquiry:

- Appreciative Inquiry focuses on identifying and building on an organization's strengths and successes. It involves a positive and collaborative approach to strategic planning, emphasizing what works well within the organization.

Theory of Change:

- The Theory of Change is a concept that outlines the steps required for an organization to achieve its long-term goals. It helps organizations articulate the causal links between their activities and intended outcomes.

Causal Layered Analysis (CLA):

- CLA is a sense-making framework that explores different layers of causality, including litany (events), social causes, systemic causes, and cultural worldviews. It helps organizations understand deeper, systemic issues.

Hoshin Kanri (Policy Deployment):

- Originating from Japanese management practices, Hoshin Kanri involves cascading strategic objectives through the organization, ensuring alignment at all levels. It emphasizes continuous improvement and goal deployment.

Adopting the most appropriate framework depends on the organization's context, goals, and the complexity of its operating environment. Often, a combination of these strategies and frameworks may be applied to create a comprehensive and tailored approach to strategic planning.

Conclusion

Strategic planning is most effective when it is approached as a structured and participatory process rather than a one-time exercise. By involving the right stakeholders, periodically reviewing organizational priorities, and adopting appropriate planning principles and frameworks, Non-profit Organizations can develop a strategic direction that is aligned with their mission and responsive to their operating environment. Such a planning process provides a strong foundation for informed decision-making and long term organizational sustainability.

The next issue of *INTERface* will explore the key considerations for effectively implementing a strategic plan and translating it into meaningful results.

03 IDENTIFICATION & EVALUATION OF RISK TREATMENT STRATEGIES

By: Sandeep Sharma
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Introduction

The process of identification and assessment of risk, discussed in previous issues of the *INTERface*, is instrumental in recognizing and determining the risk vulnerability of the organization. However, it is important to understand that merely identifying and assessing risks, without transforming these insights into actionable strategies, renders the process futile. Therefore, this article focuses on the possible measures for mitigation of those risks, i.e. Risk Treatment.

Organizations that devote time and effort for identification and assessment are likely to discover that mitigation of risk flows naturally as part of the process. It is nothing more than an action taken to help manage or mitigate a risk. The risk treatment is a critical phase to ensure that organizations proactively implement interventions to safeguard against potential threats.

The risk treatment process typically comprises of four key stages: 1) Identify Risk Treatment Strategies, 2) Evaluate Risk Treatment Strategies, 3) Develop Risk Treatment Plan, and 4) Implement Risk Treatment Plan. This article covers the first two stages, i.e. identifying and evaluating risk treatment strategies, aiming to provide a practical understanding of how organizations can select the most appropriate measures to address identified risks.

Participants in Risk Treatment Decisions

Determining the appropriate level of engagement in risk treatment decisions is essential for ensuring effective mitigation strategies. This level of engagement depends on the nature and severity of the risks involved. For instance, governance risks, which includes issues related to compliance, strategic direction, and reputation, often require oversight and decision-making from the board of directors or senior leadership. These individuals possess the authority and responsibility to make high-level decisions that safeguard the organization's overall integrity and long-term sustainability.

On the other hand, operational risks, which pertain to the day-to-day functioning of the organization, may necessitate involvement at the employee level. Since operational risks directly impact the execution of tasks, processes, and procedures within the organization, frontline employees and middle management may be best positioned to identify, assess, and address these risks in their respective areas of responsibility.

By appropriately involving stakeholders at the right levels of the organization, risk treatment decisions can be tailored to address specific challenges effectively. This ensures that the chosen mitigation strategies are not only practical and feasible, but also aligned with the organization's overall goals and objectives.

Moreover, involving relevant stakeholders creates a sense of ownership and accountability, enhancing the likelihood of successful implementation and sustained risk management efforts.

Process of Risk Treatment

The risk treatment process is a pivotal stage in the risk management journey of any organization, where identified risks are systematically addressed and managed to mitigate their potential impact. In order to make informed decisions, articulate specific treatment options, and ultimately mitigate potential risks, organizations can benefit from following the risk treatment process as outlined below.

1. Identify Risk Treatment Strategies

Traditionally, risk management strategies have primarily focused on mitigating the probability or impact of identified risks, aiming to minimize the severity of their negative consequences. However, it is important to recognize that risk is not always negative; in fact, some risks are also capable of presenting various opportunities to the organization. For example, adopting innovative technology solutions within an NPO may initially require significant investment and resources. However, this strategic decision presents the opportunity to streamline operations, improve program delivery, and enhance the organization's ability to achieve its mission effectively.

This broader perspective acknowledges that risk can present both threats as well as opportunities for organizations. Therefore, alongside strategies aimed at reducing the impact of negative risk (or threats), organizations should also consider approaches to maximize positive risk (or opportunities). This holistic approach to risk management ensures that organizations should not only aim to mitigate potential harm, but also capitalize on favorable circumstances to achieve their objectives and enhance overall performance.

However, considering the non-profit context, it is important to focus on the risk management strategies aimed at decreasing the probability or impact of an identified risk posing threat to the achievement of the organization's objectives. These strategies provide a structured framework for addressing risks effectively, thereby safeguarding the organization's mission and promoting sustainability.

There are four fundamental risk management strategies aimed at decreasing the probability or impact of an identified risk:

a) Treat

Treatment, the most prevalent risk management approach, refers to actions aimed at either reducing the possibility of occurrence of a risk or minimizing its potential consequences, or both. This pivotal strategy involves implementing customized strategies and actions to address the specific characteristics and potential consequences of each risk.

Treatment strategies can vary widely in terms of their cost and complexity. Some strategies may involve minimal expenses and effort, while others may require significant financial investment and resources. It's essential to carefully evaluate each treatment option based on its potential benefits and the organization's risk tolerance. By understanding the costs and implications associated with each strategy, non-profits can make informed decisions about how best to mitigate their risks.

Understanding “Treat” strategy through an example

“Consider a non-profit transitioning from a manual to a computerized accounting system, which introduces the risk of data loss during the transfer processor afterwards. In order to reduce the likelihood of this risk being materialized, the organization can take measures such as:

Comprehensive Data Backup Procedures

- Establish regular backup schedules to ensure all critical data is routinely backed up.
- Utilize automated backup solutions or cloud-based services for efficient and consistent backups.
- Store backup copies in secure, off-site locations to protect against physical damage or loss.

Data Migration Planning

- Develop a detailed plan for transferring data from manual to computerized systems, ensuring accuracy and completeness.
- Conduct thorough testing of data migration processes to identify and address any potential issues or errors.

Employee Training and Support

- Provide comprehensive training to staff members involved in the transition process to ensure they understand the new system and manage effectively.
- Offer ongoing support and resources to address any questions or challenges encountered during the transition.

Establish Security Measures

- Implement robust access controls to restrict unauthorized access to sensitive financial data.
- Utilize techniques to protect data both during transmission and storage.

Miscellaneous

- Maintain both manual and computerized bookkeeping systems simultaneously for a transitional period to ensure data integrity.
- Seek assistance from experts proficient in data migration to facilitate a smooth and efficient transition process.”

In terms of the example discussed, implementing data backup measures or establishing security measures, may lead to minimal expenses, for example purchasing external hard drives for taking backup, etc. However, maintaining dual book-keeping systems requires additional effort and financial investment from the non-profit. Similarly, hiring experts to oversee data transfer incurs significant costs but ensures a seamless transition with minimal disruption. Each approach carries its own set of advantages and considerations, requiring careful evaluation based on the organization's resources and risk tolerance.

b) Transfer

In conventional risk management literature, the term "transfer" is stated as one of the risk management strategies. It typically denotes the action of reallocating all or part of a risk to an external party. For instance, a non-profit may opt to outsource its IT services to a specialized company instead of managing them internally. By doing so, the non-profit offloads the responsibility of managing IT-related risks, such as cybersecurity threats or system failures, to the external service provider.

However, it's important to note that while the risk may be transferred, the ultimate accountability and consequences still rest with the non-profit. Therefore, clear terms and conditions must be outlined in the service agreement to ensure that both parties understand their respective responsibilities and liabilities. This underscores the importance of thorough oversight and ongoing risk management throughout the duration of the outsourcing arrangement.

Two primary methods for transferring risk are insurance and outsourcing. Insurance involves transferring the financial consequences of a potential risk to an insurance provider. For example, a non-profit organization might opt for liability insurance to transfer the financial burden associated with potential lawsuits or claims. On the other hand, outsourcing involves delegating certain activities or functions to external parties who are better equipped to manage the associated risks. For instance, an organization may choose to outsource its payroll services to a specialized firm to transfer the risk of payroll errors and compliance issues. Both insurance and outsourcing provide avenues for organizations to shift some of the burdens associated with risk management to external entities with the expertise and resources to handle them effectively.

c) Terminate

Termination is considered as an appropriate risk management strategy when a non-profit faces a risk that is both highly significant in frequency and magnitude, and alternative risk management approaches prove too costly or complex to implement. In such cases, some non-profits may deem elimination as the necessary response to mitigate an unacceptable risk.

For instance, consider an organization that is involved in planning programs or events in an area where potential political disturbances could endanger participant's safety or damage the organization's reputation. In response to this risk, the organization may choose to eliminate these programs or events altogether, thus avoiding the associated risks. However,

it is essential to recognize that a risk-averse non-profit's pursuit of elimination could inadvertently result in missed opportunities to fulfill its mission. For example, a non-profit utilizing internet banking for various payments, such as vendor payments and utility bills, may identify the risk of misappropriation of funds due to inadequate controls in online transactions.

As a risk treatment strategy, the organization may decide to eliminate the use of internet banking entirely, fearing the risk of fraud or theft. Yet, this decision may have its drawbacks, such as reduced efficiency and convenience in financial transactions. Similarly, some non-profits may exhibit excessive risk-taking behavior, relying on a history of incident-free operations as perceived protection against harm. For example – an organization may proceed with the transition from manual to computerized systems, even with the lack of required resources or insufficient capacity, viewing the risk as a challenge rather than a concern. However, such a decision could potentially disrupt its operations and also lead to financial risks, data integrity concerns, reputational damage, legal liabilities, and strategic setbacks.

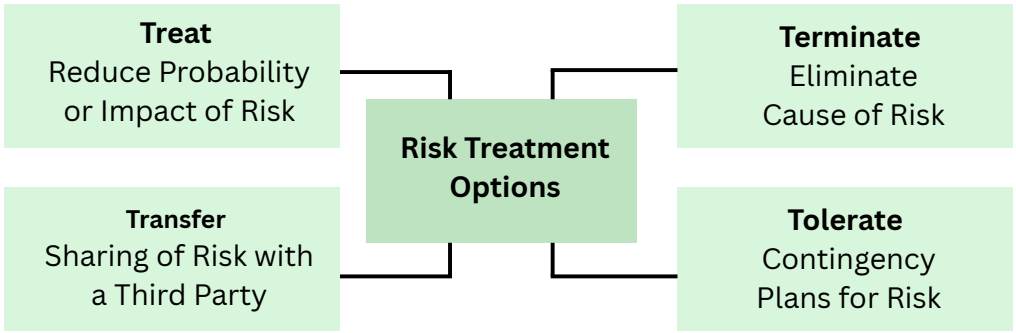
Therefore, in situations where complete termination is not possible, it remains crucial for non-profits to strike a balance between risk mitigation and mission fulfillment, carefully weighing the potential consequences of their risk mitigation decisions.

d) Tolerate

When a non-profit chooses to tolerate a risk, it opts not to take any action to reduce either the likelihood or the consequences of that risk, considering it acceptable. These tolerated risks may include those that are deemed either too remote to warrant resource allocation or whose potential consequences are deemed insignificant. However, it is crucial to note that the conscious acceptance of risk should be a deliberate decision made after thorough consideration, rather than a default position.

For example, a non-profit might opt to accept the risk of minor data entry errors in its database management system despite having stringent internal controls and skilled staff. This decision could stem from a thorough cost-benefit analysis, where the organization concludes that the expenses associated with additional error-checking measures exceed the potential impact of occasional errors. It's crucial to note that this tolerance for risk should not be mistaken for a strategic choice but rather a deliberate acceptance of certain risks based on careful consideration. For instance, a non-profit with weak internal controls may choose to tolerate the risk of errors in data entry, but in the long run, tolerating such risks might prove to be detrimental for the organization. Instead, the organization should address such risks by "treating" them (maybe by focusing on establishing strong internal controls), and not "tolerating" them.

Hence, when opting to accept a risk, non-profits should meticulously weigh the potential outcomes against the expenses of risk mitigation. It's imperative to thoroughly document this decision, guaranteeing that the chosen path aligns seamlessly with the organization's overarching mission and strategic goals.



2. Evaluate Risk Treatment Strategies

After the identification of risk treatment strategies, the next step is to evaluate the effectiveness of each of these strategies in the context of identified risks. In certain scenarios, the risks are sufficiently significant, necessitating a thorough cost-benefit analysis due to the diverse range of potential solutions and limited resources available within an organization. While every organization is mindful of operational costs and maximizing the use of its limited resources, funds allocated for risk treatment are essential for ensuring effective and efficient operations and supporting the organization's mission.

For instance, consider a non-profit contemplating on the installation of fire safety measures like extinguishers, alarms, and sprinkler systems to mitigate fire hazards. In evaluating these measures, the organization may compare the installation costs and staff training expenses against potential fire-related damages. This assessment weighs the safeguarding benefits against the incurred expenses, recognizing the invaluable protection these measures offer for employees, organizational resources, and operational continuity.

Risk treatment strategies must align with the non-profit's limited resources. Evaluating the adoption of risk treatment strategies involves considering the organization's resource constraints and determining the appropriate treatment level for each risk category. This includes assessing treatment needs for both moderate and high-risk scenarios while identifying opportunities for improvement. Internal management of risks may involve establishing a dedicated team or committee, while risks requiring external expertise necessitate the identification of external consultants or resources. This strategic approach ensures that the organization is equipped with the necessary resources and expertise to implement tailored risk treatment plans, effectively addressing the specific characteristics and levels of identified risks.

Therefore, establishing treatment goals provides the organization with a clear roadmap for addressing identified risks, ensuring a proactive approach to risk management and safeguarding the organization's stability and mission fulfillment.

Conclusion

Effective risk management extends beyond the identification and assessment of risks; it requires organizations to make informed decisions on how those risks should be addressed. Selecting an appropriate risk treatment strategy involves carefully considering the nature and significance of the risk, the organization's objectives, available resources, and the feasibility of different treatment options. Whether a risk is treated, transferred, terminated, or tolerated, the chosen approach should be based on a deliberate evaluation of its potential impact and the organization's capacity to manage it effectively.

Equally important is the evaluation of these treatment strategies to ensure that the selected measures provide the desired level of risk reduction while remaining practical and proportionate to the resources available. By adopting a structured approach to identifying and evaluating risk treatment strategies, organizations can strengthen their ability to safeguard their operations, resources, and mission. The next issue of the *INTERface* will cover the remaining stages of the risk treatment process, focusing on the development and implementation of a risk treatment plan.

04 Accounting Standard 4: Contingencies and Events Occurring After the Balance Sheet Date

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Introduction

Financial statements are prepared to present an organization's financial position and financial performance for a particular accounting year, which in India generally ends on 31 March. However, the information available at the end of the accounting year may not always provide the complete picture. Significant developments may occur between the balance sheet date and the date on which the financial statements are approved. Such developments may either provide further evidence about circumstances that existed at the balance sheet date or relate to circumstances that arose subsequently.

This distinction is particularly relevant for Non-Profit Organizations (NPOs), where financial affairs may involve grants and funding commitments, amounts receivable from donors or project partners, program related obligations, and other arrangements subject to specific conditions. Information received after the balance sheet date may therefore have implications for amounts already recognized in the financial statements or may represent significant developments that need to be considered while finalizing them.

Accounting Standard (AS) 4, Contingencies and Events Occurring After the Balance Sheet Date, issued by the Institute of Chartered Accountants of India (ICAI), provides guidance on the treatment of significant events occurring after the balance sheet date. A key consideration under the Standard is whether an event provides additional evidence regarding a condition existing at the balance sheet date or indicates a condition that arose after that date. This determines whether the financial statements require adjustment or whether the event needs to be appropriately disclosed.

As part of the ongoing series on Accounting Standards relevant to Not-for-Profit Organizations (NPOs), this article examines AS 4 from an NPO perspective, with a focus on events occurring after the balance sheet date, the distinction between adjusting and non-adjusting events, and their implications for the financial statements.

1. What is a Contingency?

A contingency refers to a possible future situation or event that may or may not occur. It represents an uncertainty that an organization needs to be prepared for because its eventual outcome may have financial or operational consequences. For instance, a former employee has filed a labour claim against the organization, and the outcome is awaited or a dispute with a donor over whether an amount already spent qualifies as eligible expenditure under the grant agreement, with a possible refund liability.

A contingency is a condition or situation, the ultimate outcome of which, gain or loss, will be known or determined only on the occurrence, or non-occurrence, of one or more uncertain future events.

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A contingency should not be confused with an estimate. An estimate is made when an amount or outcome is uncertain, but there is no uncertainty about whether the underlying transaction or event will occur or not. For example, an NPO may have incurred an electricity expense for March but receive the bill only in April. The expense relates to the accounting year ended 31 March, and the NPO may need to estimate the amount payable and recognize the expense in that year. The uncertainty is only about the amount, not about whether the expense was incurred. In contrast, where the existence or outcome of an obligation itself depends on an uncertain future event, it may constitute a contingency.

The treatment of contingencies under AS 4 needs to be considered along with the requirements of other applicable Accounting Standards. With the applicability of AS 29, Provisions, Contingent Liabilities and Contingent Assets, from 1 April 2004, the provisions of AS 4 relating to contingencies were withdrawn to the extent that they are covered by other Accounting Standards. AS 4 continues to apply to impairment of financial assets such as impairment of receivables (commonly known as provision for bad and doubtful debts) not covered by other Accounting Standards.

2. Contingencies – Losses and Gains

A contingency may result in either a potential loss or a potential gain for an organization. The accounting treatment, however, is different for the two. While a potential loss may require recognition or disclosure depending on the circumstances and the requirements of the applicable Accounting Standard, a potential gain is generally not recognized until its realization becomes sufficiently certain.

2.1. Contingent Losses to be Recognized by an NPO

A contingent loss may arise when an existing condition has the potential to result in a loss to an organization, but the ultimate outcome depends on the occurrence or non-occurrence of one or more uncertain future events. The organization needs to assess the likelihood of the loss and determine whether the matter needs to be recognized in the financial statements or disclosed as a contingency, as required under the applicable Accounting Standard.

For example, a former employee has filed a case against an organization claiming compensation for wrongful termination. The matter is still pending at the balance sheet date. The organization needs to assess the possible financial impact of the case based on the information available up to the date on which the financial statements are approved. If the available evidence is sufficient to estimate the possible loss, the estimated amount may be recognized in the financial statements. However, where the evidence is conflicting or insufficient to estimate the amount, the organization should disclose the nature of the contingency and state that the financial impact cannot be reliably estimated.

In making this assessment, the organization may consider developments occurring after the balance sheet date, its experience with similar matters and, where appropriate, the opinion or report of an independent expert.

The existence and amount of obligations undertaken by an organization are generally disclosed by way of notes to the financial statements, even where the possibility of a loss arising from such obligations is remote.

2.2. Contingent Gains to be Recognized by an NPO

A principle that organizations would do well to internalize is that contingent gains are not recognized in the financial statements, however encouraging the news may seem. A verbal assurance of a large donation, a grant that is "as good as approved," or a matching-fund commitment still awaiting the donor's internal sign-off, should not be recorded as income merely because the organization is confident it will materialize. Recognition is appropriate only when realization of the gain is virtually certain, at which point, strictly speaking, it ceases to be a "contingency" at all and is accounted for as income in the normal course.

This distinction protects the credibility of an organization's financial statements; overstating income based on expected, but unconfirmed funding can mislead trustees and donors alike about the organization's actual financial position.

3. Event Occurring After the Balance Sheet Date

The balance sheet date is 31st March, marking the close of the accounting year. But the accounts are not finalized on that date, as books are closed, the statutory audit is carried out over the following weeks, and the financial statements are then placed before the Board for formal approval, typically at the Annual General Meeting. It is this gap, between 31st March and the date the Board actually approves the accounts, that AS 4 refers to as the period during which "events occurring after the balance sheet date" must be reviewed.

> Events occurring after the balance sheet date are those significant events, both favourable and unfavourable, that occur between the balance sheet date and the date on which the financial statements are approved by the Board of Directors in the case of a company, and, by the corresponding approving authority in the case of any other entity.

In practice, this period is rarely a matter of days; it is shaped, to a large extent, by the organization's own statutory filing calendar. Under the Income-tax Act, an organization's return of income (Form ITR-7) follows the due dates prescribed under Section 263 of the Income Tax Act, 2025:

- 31st October of the relevant assessment year, where the organization's accounts are required to be audited.
- Where an audit is required, the audit report itself (in Form 112, corresponding to the erstwhile Form 10B/10BB) must be furnished at least one month before the due date of the return, i.e., ordinarily by 30th September.

Organizations registered as Section 8 companies carry an additional layer of timelines under the Companies Act, 2013, most notably, the requirement to hold the Annual General Meeting within the

prescribed period from the close of the financial year, at which the audited financial statements are placed for adoption.

AS 4 classifies such events into two categories:

- **Adjusting Events** – events that provide further evidence of conditions that already existed at the balance sheet date. These require the financial statements to be adjusted. For instance:
    - a theft or misappropriation of project cash or relief material by field staff, which took place during the year but is discovered only after the year end, while the accounts are still being finalized. The loss should be recognized in the year to which it relates.
    - a donor confirms, after the year end, that an expenditure incurred under the project is disallowed due to non-fulfilment of conditions. Since the expenditure was actually incurred before the balance sheet date, the condition giving rise to the disallowance already existed at year end. The donor's confirmation only provides evidence of it after the fact. The organization should therefore adjust the accounts for the year under audit.
- **Non-Adjusting Events –** events that are indicative of conditions arising only after the balance sheet date. These do not require the financial statements to be adjusted, though disclosure may be necessary. For instance:
    - a fire destroys an organization's field office or project asset after the balance sheet date. The loss did not exist as at the year end, so it is not adjusted in that year's accounts, though it may need disclosure, along with consideration of the going concern assumption if the impact is significant.
    - a major donor communicates, after the year end, a sudden withdrawal of previously committed future funding. This reflects a change in circumstances that arose only after the balance sheet date.

The distinction between adjusting and non-adjusting events can be understood through three questions:

Question 1. Did the underlying condition exist on 31st March?

If yes, subsequent information may provide further evidence about that condition.

Question 2. Did the condition arise only after 31st March?

If yes, it will generally be a non-adjusting event.

Question 3. Is the event significant for users of the financial statements?

Even where no adjustment is required, a significant subsequent event may need to be appropriately brought to the attention of users.

4. Events Affecting the Going Concern Assumption

Financial statements are prepared on the basis of certain fundamental accounting assumptions, one of which is the going concern assumption. This assumption means that an organization is expected to continue its operations for the foreseeable future and does not intend, or have a necessity, to substantially curtail its activities or cease operations. For an organization, the assessment of going concern may be closely linked to its ability to sustain its programs and meet its

financial and other obligations. This may depend on factors such as the availability of funding, continuation of key programs, regulatory status and access to the resources necessary to carry out its activities.

Certain events occurring after the balance sheet date may be significant enough to raise questions about the organization's ability to continue as a going concern. For example, an organization may be substantially dependent on foreign contributions for its programs and subsequently have its FCRA registration cancelled. If the organization has no alternative source of funding sufficient to continue its existing operations, the event may require the management and those responsible for governance to reassess whether the going concern assumption remains appropriate. Similarly, an organization's head suddenly leaves the organization after the balance sheet date, the event may have implications for the organization's ability to continue its activities. The significance of the event would depend on the organization's circumstances, including the availability of second line and resources to continue its operations.

The occurrence of such events after the balance sheet date does not, by itself, mean that the financial statements for the year ended 31 March should be adjusted for the event. However, where the event raises significant uncertainty about the organization's ability to continue as a going concern, its implications need to be considered while finalizing the financial statements and making the appropriate disclosures.

5. Understanding the Liquidation Basis

Where the going concern assumption is no longer appropriate, a liquidation basis of accounting may need to be considered.

Under a liquidation basis, assets and liabilities are considered based on the organization's expected process of winding up rather than on the assumption that assets will continue to be used and liabilities will be settled in the normal course of operations. For a commercial entity, moving to a liquidation basis is largely a valuation exercise. Assets are restated at their expected realisable value, and liabilities likely to crystallize on winding up are provided for in full. For an non-profit organization, the same shift carries an additional, distinctly regulatory dimension, because an NPO's assets and funds are rarely "free" to be realized and distributed the way a company's might be. Several overlapping legal frameworks determine where those assets can actually go, and this needs to inform how the Board and auditor think about liquidation-basis accounts, not merely how they value line items.

- **FCRA dimension** – where an NPO holds foreign contribution, cancellation or surrender of its FCRA registration has direct consequences for the assets created out of such contribution. On cancellation, the foreign contribution and the assets created from it do not remain freely at the organization's disposal. The custody and eventual utilization of all the assets are governed by the FCRA framework, generally passing under the control of a prescribed authority pending further direction. Any liquidation-basis assessment must therefore separately identify assets and funds traceable to foreign contribution, since these may not be realisable by the organization in

the way its domestically funded assets would be.

- **Income-tax dimension** – the consequences of winding up also need to be considered under the Income-tax Act, 2025. Section 352 provides for additional income-tax on accreted income in specified circumstances. In the case of dissolution, where an organization fails to transfer all its assets to another registered non-profit organization within twelve months from the end of the month in which the dissolution takes place, the provision may apply. The section also covers other specified situations, including cancellation or withdrawal of registration. Therefore, while preparing for winding up, an organization needs to consider not only the accounting treatment of its assets and liabilities but also the manner and time within which its assets are required to be transferred to avoid the specified tax consequences.

- **Constitutional documents** – the trust deed, memorandum, or byelaws carries a dissolution clause. Usually, the organization's assets will pass only to another entity with similar charitable objects and not be distributed to trustees, members, or shareholders.

- **Companies Act dimension –** where the organization is registered as a Section 8 company, the Companies Act, 2013 similarly restricts the destination of assets on winding up. Any surplus remaining after settlement of debts and liabilities is not available for distribution to members; it must be transferred to another Section 8 company with similar objects, or, failing that, credited to a specified statutory fund. Here too, the accounting effect of liquidation is shaped as much by this legal earmarking of assets as by their market realisability.

When the Board and auditor conclude that the going concern assumption is no longer appropriate, preparing accounts on a liquidation basis for an organization is therefore not simply a matter of writing assets down to scrap or resale value. It requires a parallel review of these regulatory constraints.

6. Disclosure of Events Occurring After the Balance Sheet Date

For material events occurring after the balance sheet date that are required to be mentioned in the report of the approving authority, the disclosure should include:

- the nature of the event; and

- an estimate of its financial effect, or a statement that such an estimate cannot be made.

Thus, the disclosure is not merely a statement that an event has occurred. It should provide sufficient information about what the event is and, where possible, its financial effect, so that users can understand its significance. It is also important to note that the disclosure requirements under AS 4 apply only to contingencies and events that affect the financial position to a material extent. Therefore, materiality remains an important consideration in determining whether disclosure is required.

Conclusion

AS 4 requires attention to the period between the balance sheet date and the date on which the financial statements are approved. Information becoming available during this period can have different accounting implications depending on the circumstances to which it relates.

Thus, the purpose of AS 4 is to ensure that the financial statements reflect the conditions relevant to the accounting year while also appropriately considering significant developments that occur until the financial statements are approved. For organizations entrusted with donor funds and public resources, this contributes to financial reporting that is both reliable and meaningful to those who rely on it.

05 IMPACT ASSESSMENT: MOVING FROM SPENDING COMPLIANCE TO OUTCOME ACCOUNTABILITY

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Introduction

The discourse on wealth has never been limited to its creation; its responsible use has been equally significant. Across centuries, societies have grappled with a fundamental question of how resources can be used to ensure fairness, dignity, and collective well-being. Different approaches have attempted to address this, ranging from state led redistribution to voluntary giving rooted in moral responsibility. However, neither approach in isolation proved sufficient, particularly in driving long term and systemic change. As societies evolved, so did expectations from corporations that draw extensively from societal resources and, in turn, hold significant economic power and influence. Corporations are no longer viewed solely as profit making entities; their legitimacy increasingly depends on how they engage with the communities and environments in which they operate.

In response to these evolving expectations, Corporate Social Responsibility (CSR) has emerged as a structured and policy driven approach. In India, CSR has been formalized under the Companies Act, 2013, positioning it as an integral part of corporate governance. It marks a shift from discretionary philanthropy to planned interventions under a defined compliance framework aligned with organizational objectives and societal needs.

While the statutory framework for CSR provides the foundation for responsible planning, implementation, and governance, its true effectiveness lies in ensuring that CSR initiatives achieve meaningful and measurable outcomes. In this context, Impact Assessment has emerged as an important mechanism for evaluating the effectiveness of such initiatives and strengthening accountability. This article examines the legal provisions governing Impact Assessment, such as, when such assessment becomes mandatory, the limits on related expenditure, reporting requirements, collaborative projects, and the roles of the CSR Committee and the Board, along with implications of non-compliance.

By examining these aspects, this article seeks to provide clarity on how Impact Assessment functions as a statutory feedback mechanism embedded within the CSR lifecycle, strengthening transparency, outcome-oriented CSR, and long-term strategic alignment of CSR initiatives.

1. What is Impact Assessment?

“Impact Assessment” is a combination of two words with distinct Latin origins: impact, derived from impactus, meaning “to strike against,” and assessment, derived from assidere, meaning “to sit beside” or evaluate. Together, the term conveys the idea of closely examining the effects of an action. While the individual words are much older, the combined expression gained prominence in the 1960s and 1970s as a formal approach to evaluating the consequences of projects and policies.

In simple terms, impact assessment refers to the process of evaluating the actual changes brought about by a project, program, or intervention after it has been implemented. It focuses on understanding the extent to which intended objectives have been achieved and examines outcomes, positive or negative, direct or indirect, and expected or unintended. This understanding becomes particularly important in contexts where significant resources are deployed with the expectation of creating social change, making it essential to assess whether such efforts are actually leading to the intended outcomes.

With the introduction of Section 135 under the Companies Act, 2013, (CSR) assumed a structured and formal framework, establishing it as a defined responsibility for eligible companies. Since then, CSR has moved beyond philanthropic intent to a more organized and strategic function involving multiple stakeholders, including companies, implementing agencies, communities, and regulators. This transition has also led to a significant increase in CSR expenditure.

However, as highlighted in a report by NITI Aayog on Social Impact Assessment of CSR in India (FY 2014 to FY 2020), this increase in spending has not been accompanied by a corresponding depth of evidence on outcomes. The report notes that while substantial resources have been deployed, often concentrated in specific sectors and geographies, there remains limited empirical understanding of the changes resulting from these interventions.

This disconnect between spending and demonstrated outcomes led to a greater emphasis on impact assessment, not merely as a conceptual exercise, but as a critical process to determine whether CSR initiatives are creating meaningful and measurable change. Recognizing this need, the concept of impact assessment in CSR was formally introduced through the Companies (Corporate Social Responsibility Policy) Amendment Rules, 2021 under the Companies Act, 2013.

2. Applicability of Impact Assessment

The requirement for impact assessment is provided under Rule 8(3)(a) of the Companies (Corporate Social Responsibility Policy) Amendment Rules, 2021 issued under the Companies Act, 2013. Impact assessment is not a mandatory requirement for every company that falls under the CSR ambit. The obligation is determined based on a company's CSR spending over a period of time, along with the size and completion status of specific CSR projects.

Companies having an average CSR obligation of ₹10 crore or more during the three immediately preceding financial years are required to carry out impact assessment of their CSR projects. Further, it applies only to those CSR projects that have an outlay of ₹1 crore or more and have been completed at least one year prior to the assessment.

Rule 8(3)(a) of The Companies (Corporate Social Responsibility Policy) Amendment Rules, 2021:

"Every company having average CSR obligation of ten crore rupees or more in pursuance of sub-section (5) of section 135 of the Act, in the three immediately preceding financial years, shall undertake impact assessment, through an independent agency, of their CSR projects having outlays of one crore rupees or more, and which have been completed not less than one year before undertaking the impact study."

For instance, ABC Private Limited has CSR obligations of ₹12 crore, ₹9 crore, and ₹11 crore during FY 2022–23, FY 2023–24, and FY 2024–25 respectively. The average CSR obligation in this case comes to ₹10.67 crore. Since this exceeds ₹10 crore, the company will be required to undertake impact assessment in FY 2025–26.

Now, suppose the company is implementing six CSR projects with outlays of ₹50 lakh, ₹90 lakh, ₹2 crore, ₹1.5 crore, ₹75 lakh, and ₹1.2 crore. In this case, impact assessment will be required only for those projects where the outlay is ₹1 crore or more, that is, the projects with outlays of ₹2 crore, ₹1.5 crore, and ₹1.2 crore, provided these projects have also been completed for at least one year.

Note: In cases where the above thresholds are not met, impact assessment may still be undertaken by the company on a voluntary basis.

3. Mode of Execution

The manner in which impact assessment is to be undertaken is prescribed under Rule 8(3)(a) of The Companies (Corporate Social Responsibility Policy) Amendment Rules, 2021, which mandates that, wherever applicable, such assessment shall be carried out through an independent agency.

Accordingly, when a company is required to conduct an impact assessment, it is required to engage an independent external agency for this purpose.

The law requires that the assessment be carried out independently; however, it does not prescribe specific eligibility criteria for the selection of such agencies. As clarified by the Ministry of Corporate Affairs through its Frequently Asked Questions on CSR, the Board has the prerogative to determine the eligibility criteria and select the independent agency for undertaking impact assessment.

4. Cost of Impact Assessment

The CSR framework recognises that impact assessment involves specialised evaluation and professional expertise. Accordingly, companies are permitted to book the cost pertaining to carrying out the impact assessment as CSR expenditure for the relevant financial year. However, this is subject to a prescribed limit. The amount that can be booked towards CSR on account of impact assessment shall not exceed two percent of the total CSR expenditure of the company for that financial year or fifty lakh rupees, whichever is higher. This position is based on the amendment introduced through the Companies (Corporate Social Responsibility

policy) Amendment Rules, 2022 under the Companies Act, 2013. Prior to this amendment, the limit was five percent of CSR expenditure or fifty lakh rupees, whichever was less. The amendment made two key changes by reducing the percentage from five percent to two percent and by revising the condition from whichever is less to whichever is higher.

Further, as clarified by the Ministry of Corporate Affairs through its FAQs on CSR, the expenditure incurred on impact assessment is over and above the limit prescribed for administrative overheads. Accordingly, such expenditure is not required to be included within the five percent cap applicable to administrative overheads.

Rule 8(3)(c) of The Companies (Corporate Social Responsibility Policy) Amendment Rules, 2022:

"A Company undertaking impact assessment may book the expenditure towards Corporate Social Responsibility for that financial year, which shall not exceed two percent of the total CSR expenditure for that financial year or fifty lakh rupees, whichever is higher."

5. Pooled CSR Projects

Two or more companies may collaborate for the implementation of a common CSR project by pooling their financial and operational resources. Such collaboration is recognised under the CSR framework, including Rule 4(4) of the Companies (Corporate Social Responsibility Policy) Amendment Rules, 2021, provided that each participating company is able to account for its contribution to the project.

In cases where a collaborative CSR project meets the criteria for mandatory impact assessment, a practical consideration arises regarding whether each participating company is required to undertake a separate assessment. This has been clarified by the Ministry of Corporate Affairs through General Circular No. 14/2021 dated 25 August 2021 (FAQs on CSR). It states that where two or more companies undertake a common CSR project, the impact assessment carried out by one company may be shared with the other participating companies. Accordingly, a single impact assessment may be relied upon by all collaborating companies, thereby avoiding duplication of effort and ensuring efficient utilisation of resources.

With respect to expenditure, the cost of conducting the impact assessment may be shared among the collaborating companies in a mutually agreed manner. However, each company is required to ensure that its share of such expenditure remains within the limits prescribed under the law.

6. Key Elements of Effective Impact Assessment

While the legal framework under the Companies Act, 2013 and the CSR Rules requires certain companies to undertake impact assessment, it does not prescribe a detailed methodology for conducting such assessments.

In practice, organizations and independent agencies adopt structured approaches to ensure that assessments are credible, focused, and useful for decision-making. Accordingly, the following elements are commonly considered by evaluators while undertaking impact assessments:

a) **Clear Objectives and Baseline** – A well-defined set of objectives is essential to determine what the project intends to achieve.

Wherever possible, baseline data should be captured to enable comparison and measurement of change over time.

b) Project Indicators – Indicators should be aligned with project objectives and limited to what is measurable and relevant.

- Output indicators track activities completed.
- Outcome indicators reflect short- to medium-term changes.
- Impact indicators capture long-term effects.

Clarity and relevance of indicators are more important than quantity.

c) Use of Mixed Methods – A combination of qualitative and quantitative methods is generally adopted:

- Qualitative methods include interviews, focus group discussions, and field observations.
- Quantitative methods include surveys and defined performance metrics.

Using both approaches provides a more balanced and reliable assessment.

d) Triangulation of Findings – Findings are typically validated by cross-verifying information from multiple sources and methods.

Note: Refer Annexure – 1 for the illustrative CSR impact assessment template.

7. Role of CSR Committee & Board

Impact assessment is embedded within the broader CSR governance framework. Although the assessment itself is carried out by an independent agency, the responsibility for initiating, reviewing, and acting upon its findings rests with the CSR Committee and the Board.

The CSR framework envisages that the CSR Committee places the annual action plan before the Board. The action plan should include details relating to need and impact assessment for the projects undertaken by the company, wherever applicable.

Rule 5(2) of The Companies (Corporate Social Responsibility Policy) Amendment Rules, 2021:

"The CSR Committee shall formulate and recommend to the Board, an annual action plan in pursuance of its CSR policy, which shall include the following, namely: -

a) the list of CSR projects or programmes that are approved to be undertaken in areas or subjects specified in Schedule VII of the Act;

b) the manner of execution of such projects or programmes as specified in sub-rule (1) of rule 4;

c) the modalities of utilisation of funds and implementation schedules for the projects or programmes;

d) monitoring and reporting mechanism for the projects or programmes; and

e) details of need and impact assessment, if any, for the projects undertaken by the company:

Provided that Board may alter such plan at any time during the financial year, as per the recommendation of its CSR Committee, based on the reasonable justification to that effect."

Accordingly, it may also recommend the appointment of an independent agency and review the assessment findings once received. Based on such findings, the Committee may suggest corrective measures or strategic modifications to improve the effectiveness of CSR initiatives.

The Board, being ultimately responsible for CSR governance, is required to take note of the impact assessment findings and ensure that the observations and recommendations are appropriately considered. These findings serve as an important input for refining future CSR strategies and annual action plans.

8. Disclosure and Reporting

In order to promote transparency and accountability in the implementation of CSR activities, the law prescribes specific disclosure requirements in relation to impact assessment. Rule 8(3)(b) of the Companies (Corporate Social Responsibility Policy) Amendment Rules, 2021 provides that the impact assessment report shall be placed before the Board and annexed to the Annual Report on CSR. This ensures that the Board formally considers the findings of the assessment and that stakeholders are informed about the outcomes of the company's CSR initiatives.

However, recognizing that impact assessment reports may be detailed and extensive, the Ministry of Corporate Affairs, through General Circular No. 14/2021 dated 25 August 2021 (FAQ on CSR), has clarified that providing a web-link to access the complete impact assessment report, along with an executive summary of the report in the Annual Report on CSR, would be treated as sufficient compliance with Rule 8(3)(b). This clarification reflects a balanced regulatory approach, maintaining substantive transparency while allowing flexibility in the mode of disclosure.

9. Non-Compliance Penal Provisions

There is no specific penalty prescribed exclusively for failure to conduct impact assessment. However, non-compliance would attract consequences under the broader enforcement framework of the Companies Act, 2013.

The Ministry of Corporate Affairs has clarified through General Circular No. 14/2021 dated 25 August 2021 (FAQs on CSR) that non-compliance with provisions of Section 135 or the CSR Rules would trigger applicable penal provisions. Accordingly, failure to make prescribed disclosures in the Board's Report may attract penalties under Section 134(8), while other contraventions may be covered under the general penalty provisions of Section 450 of the Act.

Under Section 454(3) of the Companies Act, 2013, the adjudicating officer may, by an order, impose penalties on the company and the officer in default, and may also direct rectification of the non-compliance. Further, as per Section 454(8), failure to comply with such an order within ninety days may result in additional penalties, including fines on the company and, in certain cases, imprisonment or fine for the officer in default.

Section 134(8) of the Companies Act, 2013:

"If a company is in default in complying with the provisions of this section, the company shall be liable to a penalty of three lakh rupees and every officer of the company who is in default shall be liable to a penalty of fifty thousand rupees."

Section 450 of the Companies Act, 2013:

"If a company or any officer of a company or any other person contravenes any of the provisions of this Act or the rules made thereunder, or any condition, limitation or restriction subject to which any approval, sanction, consent, confirmation, recognition, direction or exemption in relation to any matter has been accorded, given or granted, and for which no penalty or punishment is provided elsewhere in this Act, the company and every officer of the company who is in default or such other person shall be liable to a penalty of ten thousand rupees, and in case of continuing contravention, with a further penalty of one thousand rupees for each day after the first during which the contravention continues, subject to a maximum of two lakh rupees in case of a company and fifty thousand rupees in case of an officer who is in default or any other person."

Conclusion

Impact assessment represents the evolution of CSR in India from a compliance-driven activity to a genuine instrument of social change. The mandatory framework establishes standards, shifting the focus from "compliance through spending" to "accountability through outcomes". Companies that embrace impact assessment as a strategic tool, rather than a regulatory burden, will find that it transforms how they approach CSR. It provides a vital feedback loop that enables the Board of Directors to refine social interventions, optimize resource allocation, and maximize the effectiveness of every rupee spent. Over time, this shift leads to better-designed programmes, more meaningful beneficiary engagement, and greater resource efficiency. Further, as these findings move into the public domain through mandatory disclosures, they reinforce a culture of transparency. Therefore, integrating impact assessment into the CSR lifecycle ensures that corporate contributions create deeper and more lasting social impact.

Annexure-1

Illustrative format for CSR Impact Assessment report

Note: The law does not prescribe any specific format for preparing an impact assessment report. The structure presented below is only for reference and is intended to serve as a good practice guide. Companies may adopt, modify, or expand this format based on the nature, scale, and sector of their CSR projects.

Part 1 — Cover Information (Title Page)

Field	Details to Be Filled
Title of the Report	Impact Assessment Report of [Project Name]
Reporting Company	[Name of the company commissioning the IA]
CSR Project Name	[Full name of the CSR project assessed]
Implementing Agency	[Name of NGO / Government Body / Other]
Project Location	[State(s), District(s), Village(s)]
Project Duration	[Start date] to [End date]
Total CSR Outlay	Rs. [Amount] (as approved by the Board)
Actual Expenditure	Rs. [Amount] (as per audited statements)
Year of Impact Assessment	FY [Year]
Assessing Agency (IA Firm)	[Name, address, and brief credentials of the independent agency]
Date of Report	[DD/MM/YYYY]

Part 2 — Executive Summary

(1–2 pages maximum. This section should be a self-contained summary of the assessment, suitable for inclusion in the Annual Report on CSR. It should cover the project in brief, overall methodology, key findings, and top recommendations.)

Element	Content
Project Overview	One-paragraph description of the CSR project, its objectives, and beneficiaries.
Geographic Reach	States, districts, and communities covered.
Beneficiaries Reached	Total direct and indirect beneficiaries (disaggregated by gender, age, etc., where applicable).
Key Findings	Summary of impact across 3–5 most significant outcome areas.
Overall Assessment	High-level rating of project impact (e.g., using a 5-point scale or traffic-light system).
Top Recommendations	2–3 priority recommendations for the company and implementing agency.

Part 3 — Introduction

1. Background to the CSR Project

- Company overview and CSR mandate under Section 135 of the Companies Act, 2013.
- Description of the CSR project — why it was initiated, what need it was designed to address.
- Reference to the company's CSR Policy and Schedule VII alignment.

2. Objectives of the Impact Assessment

- State the purpose of this IA — what questions it seeks to answer.
- Confirm regulatory applicability (Rule 8(3) compliance or voluntary IA).

3. Scope and Limitations

- Geographic scope and time period covered.
- Any limitations in data availability, access to beneficiaries, or measurement constraints.

Part 4 — Research Methodology

This section should describe in detail how the assessment was conducted, including:

Methodology Element	Description
Assessment Framework	State the framework used — e.g., RUOEI (Relevance, Utility, Operation & Maintenance, Effectiveness, Impact), OECD-DAC (Organisation for Economic Co-operation and Development — Development Assistance Committee) criteria, or other.
Data Collection Tools	Structured questionnaires, interview guides, observation checklists, focus group protocols — attach as annexures.
Qualitative Methods	Interviews, focus groups, case studies, field visits, storytelling — specify with whom and how many.
Quantitative Methods	Surveys, Key Performance Indicators (KPIs), Social Return on Investment (SROI), Environmental Impact Assessment (EIA) — specify sample size, sampling technique, and statistical methods.
Sampling Strategy	State whether sampling was random, purposive, or stratified. Provide sample size with rationale.
Data Analysis Approach	How qualitative data was coded/thematised; how quantitative data was analysed.
Triangulation Approach	How multiple data sources were cross-verified to validate findings.

Part 5 — Project Profile and Stakeholder Details

1. Project Objectives (as approved)
2. Project Activities and Implementation Timeline
3. Financial Summary

Financial Head	Amount (Rs.)
Approved CSR Outlay	
Actual CSR Expenditure	
Balance Unspent (if any)	
IA Expenditure (booked as CSR)	

4. Direct and Indirect Beneficiaries

Beneficiary Category	Number	% Female	% SC/ST/OBC (if applicable)
Direct Beneficiaries			
Indirect Beneficiaries			
Total			

5. SDG Alignment – Specify the SDG Goal(s) and Target(s) that the project contributes to, with brief justification.

Part 6 — Impact Analysis (Project-wise)

For each CSR project assessed, provide a structured analysis under the following headings:

Assessment Dimension	Key Questions to Address
Relevance	Did the project address a genuine, priority need of the target community? Was it aligned with the company's CSR policy and national/state priorities?
Utility	To what extent are the facilities/services created being actively used? (Full / Partial / Not in use — with reasons.)
Operation & Maintenance	Are the assets created being properly maintained? Who is responsible? Is there a maintenance plan in place?
Effectiveness	Did the project achieve its stated outputs and outcomes? What evidence supports this? What were the gaps?
Impact	What tangible and intangible long-term benefits have been delivered? Have there been any unintended positive or negative effects?
Sustainability	Are the benefits likely to persist after project closure? What factors support or threaten long-term sustainability?

This section should include:

- Direct quotations and testimonials from beneficiaries (with proper attribution or anonymisation as appropriate).
- Data tables presenting survey results, satisfaction scores, and before/after comparisons.
- Case studies of individual beneficiaries or communities where the project had notable impact.
- Photographic evidence (where available and consented).

Part 7 — Consolidated Findings, Observations, and Recommendations

1. Overall Impact Rating – Summarise the overall project impact using a consistent rating scale.

Example:

Rating	Description	Score
Very High	Project significantly exceeded its objectives; deep, sustained community impact.	80%+
High	Project achieved its primary objectives; strong positive community outcomes.	70–79%
Moderate	Project partially met objectives; some positive outcomes with gaps.	60–69%
Low	Project fell short of objectives; limited impact observed.	50–59%
Very Low	Project did not achieve its objectives; impact negligible or negative.	Below 50%

2. **Key Observations –** Bullet-point summary of the most important findings (both positive and negative) across all projects assessed.
3. **Recommendations –** Action-oriented recommendations.

Part 8 — Annexures

- Annexure A: Data collection tools (questionnaires, interview guides, etc.)
- Annexure B: List of stakeholders consulted (name, role, location — suitably anonymised if required)
- Annexure C: Financial statements / CSR expenditure certificates
- Annexure D: Photographs and field documentation
- Annexure E: SDG mapping matrix
- Annexure F: Credentials of the assessing agency

06 STRUCTURAL CHANGES IN TAXATION OF NPOs

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Introduction

The Income-tax Act, 2025 introduced certain structural shifts in the charitable framework, which inadvertently created compliance risks and interpretational challenges for Non-Profit Organizations. The Finance Act, 2026, marks the first legislative effort to correct these unintended consequences. This article analyses the key amendments affecting mergers, cancellation risks, return filing, registration requirements and compliance timelines for NPOs, and explains how these changes restore parity with the settled position under the Income-tax Act, 1961.

The Income-tax Act, 2025 (ITA 2025), though enacted with the objective of simplification and structural clarity, introduced certain unintended consequences for the Non-Profit Organization (NPO) sector when compared with the settled framework under the Income-tax Act, 1961 (ITA 1961). Many provisions relating to registration, cancellation, merger, return filing, and exemption conditions were either drafted differently or positioned in a manner that created new compliance risks and litigation exposure for genuine NPOs.

The Finance Act, 2026, demonstrates the first legislative response to those concerns. A careful reading of the amendments shows that several provisions affecting NPOs have been revisited to restore parity with the legal position that existed under the ITA 1961 and to remove unintended hardship that would otherwise have arisen under the new regime.

1. Merger of Registered NPOs will Not Trigger the Accreted Tax

A new Section 354A inserted in ITA 2025, provides that tax on accreted income under section 352 shall not apply where a registered NPO merges with another registered NPO having the same or similar objects, subject to prescribed conditions. The amendment provides the statutory protection similar to Section 12ACf of the ITA 1961. This removes litigation risk in genuine NPO mergers.

Clarificatory amendment in Table to section 352: Along with the insertion of section 354A, a consequential clarification has also been carried out in Table Sl. No. 8 under section 352, applicable from tax year 2026-27. The earlier drafting of the table created ambiguity regarding the exact circumstances in which a merger would trigger tax on accreted income.

The amended table now clearly provides that accreted tax shall arise where a registered NPO merges with:

(a) an entity other than a registered NPO; or

(b) a registered NPO having similar objects but the merger does not fulfil the prescribed conditions; or

(c) a registered NPO not having the same or similar objects.

When read together with the newly inserted section 354A, the legislative scheme now makes it unambiguously clear when accreted tax shall apply and it shall not apply in case of NPO mergers.

2. No Cancellation Merely on Carrying on Commercial Activity in the GPU Category

Section 346 of the ITA 2025 prescribes specific restrictions on commercial activities undertaken by registered NPOs in the "advancement of any other object of general public utility" (GPU) category. Commercial activity is permitted only where all the following conditions are cumulatively satisfied:

(a) The activity is undertaken in the course of the actual carrying out of the GPU object,

(b) Aggregate receipts from such activity do not exceed 20% of the total receipts of the NPO for the relevant tax year, and

(c) Separate books of account are maintained in respect of such activity.

This provision substantially corresponds to the proviso to Section 2(15) of the ITA 1961.

Under the earlier provisions of the ITA, 2025, a breach of any of the conditions under Section 346, such as exceeding the 20% threshold, undertaking unrelated commercial activity, or failure to maintain separate books, attracts dual statutory consequences:

(a) Section 351(1)(b) expressly includes a violation of provisions referred to in section 346 within the scope of "specified violations". This empowers the tax authorities to cancel the NPO's registration and may also result in tax on accreted income under Section 352, subject to the prescribed conditions.

(b) Section 353 treats violation of Section 346 as an "other violation", triggering a special computation mechanism under which certain exemptions are restricted, and income may be subjected to tax based on such computation.

Thus, a breach of section 346 was uniquely placed in two separate consequence categories; it was treated both as a "specified violation" under Section 351 and as an "other violation" under Section 353.

However, the Finance Act 2026 has now removed commercial activity by NPOs under the "general public utility" category from the scope of "specified violation" under Section 351. Earlier, such a breach could have led to cancellation of registration and levy of the exit tax. The amendment restores the position under the ITA 1961, where such violations result only in a year-specific denial of exemption. It shall now be treated merely as an "other violation" under Section 353, triggering special computation for that tax year without affecting the registration of the NPO.

3. Registered NPOs can File a Belated Return

Section 349 of the ITA 2025 mandates that where the total income of a registered NPO, computed without giving effect to the provisions of Chapter XVII-B, exceeds the maximum amount not chargeable to tax for any tax year, such organization shall furnish its return of income in accordance with Section 263(1)(a)(iii) and (2), within the due date prescribed under Section 263(1)(c). This provision substantially corresponds to Section 12A(1)(ba) of the ITA 1961.

Under the 1961 Act, entities registered under section 12AB were required to file a return of income under section 139(4A) where their total income, before giving effect to Sections 11 and 12, exceeded the basic exemption limit. Importantly, the statutory framework under the 1961 Act permitted such returns to be filed either within the due date under section 139(1) or as a belated return under section 139(4). In contrast, the 2025 Act did not recognize the concept of a belated return for a registered NPO. Exemption under the special NPO regime was available only where the return is furnished within the original due date specified under Section 263(1)(c). There was no reference to Section 263(4), which otherwise permits belated filing of returns within the extended statutory timeline. The absence of reference to Section 263(4) had the legal effect that a delay in filing the return would trigger Section 353, resulting in special computation provisions for that year.

The Finance Act, 2026 has amended Section 349 to insert a reference to Section 263(4), allowing registered NPOs to file a belated return and still claim exemption. This amendment aligns the ITA 2025 with the ITA 1961 position.

Accordingly, where the return is furnished within the time limit permitted for filing an original or belated return, it shall not be treated as an "other violation" under Section 353.

4. The Time Limit for Filing a Revised Return is Extended to 12 Months

For NPOs, from assessment year 2026-27 and tax year 2026-27, the ability to correct omissions or errors in returns is crucial, as defects in return filing can directly jeopardize exemption claims under the charitable regime. The time limit for filing a revised return has now been extended.

Under the earlier provisions of Section 263(5) of the ITA 2025 (corresponding to Section139(5) of the ITA 1961), a revised return could be furnished within nine months from the end of the relevant tax year (i.e., up to 31 December of the assessment year) or before completion of assessment, whichever is earlier. Since the time limit for filing a belated return is also nine months, a taxpayer filing a belated return at the end of the permitted period is left with no opportunity to revise the return.

To address this issue, an amendment is effected to extend the time limit for filing a revised return from nine months to twelve months from the end of the relevant tax year or before completion of assessment, whichever is earlier. This effectively allows the revised return to be filed up to twelve months from the end of the relevant tax year (i.e., up to 31 March of the assessment year).

This extension will allow taxpayers to revise their returns even if a belated return was filed at the end of the permissible period. Further, the Finance Act, 2026 has levied a fee under Section 428(b) of the ITA 2025 [corresponding to Section 234F(1) of the ITA 1961] where a revised return is filed beyond nine months from the end of the relevant tax year. The fee shall be:

(a) Rs.1,000, where the total income does not exceed Rs.5 lakh; and

(b) Rs.5,000, in other cases.

Corresponding amendments were also done to Section 139(5) of the ITA 1961, introducing a new Section 234I to levy a similar fee for the delayed filing of revised returns. Accordingly, the extended timeline and fee provisions shall apply for the:

(a) Previous year 2025-26 (assessment year 2026-27) under the ITA 1961; and

(b) Tax year 2026-27 onwards under the ITA 2025.

It was further clarified that the corresponding amendments in the Income-tax Act, 1961 shall come into force from 1 March 2026 and shall apply for assessment year 2026-27 (previous year 2025-26).

Conclusion

Finance Act, 2026 represented the first substantive legislative refinement of the NPO framework under the ITA 2025, before the new law came into force. The amendments discussed above are not routine changes; they are structural corrections addressing unintended consequences arising from the redrafting of the charitable regime in the new Act.

Several provisions that, in their original form, exposed genuine NPOs to the risks of cancellation, exit tax, loss of exemption, and unnecessary compliance burdens have now been realigned with the settled legal position under the ITA 1961. The insertion of positive protections, removal of dual consequences, restoration of belated return benefits, rationalization of registration requirements, and extension of compliance timelines collectively indicate a legislative recognition of practical difficulties faced by the sector.

At the same time, these amendments also demonstrate that the transition from the 1961 Act to the 2025 Act is still an evolving process. While important corrections have been made, certain foundational and interpretational aspects of the NPO framework may still require further legislative clarification or administrative guidance.

07 OVERVIEW OF TRANSITION TO INCOME TAX ACT 2025

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Introduction

The Income-tax Act, 2025 brings with it a comprehensive restructuring of the framework governing the taxation of non-profit organizations. While the underlying philosophy of granting tax benefits to charitable and religious institutions continues, the manner in which the law is organized and applied has undergone significant change.

Under the erstwhile Income-tax Act, 1961, the provisions relating to charitable trusts and institutions were scattered across multiple sections and, to a large extent, shaped by judicial interpretation.

In contrast, the ITA, 2025 introduces a more structured and codified framework, largely contained in Chapter XVII-B, which sets out a consolidated scheme for the computation, classification, and taxation of the income of registered non-profit organizations.

As most readers are already familiar with the earlier law, this article provides a consolidated and simplified overview of the key changes introduced under the ITA, 2025. It also provides the fundamental shift and changes made in the new Act.

1. New Term "Registered Non-Profit Organisation"

Under the ITA, 1961, the law referred to various forms of entities such as trusts, institutions, funds, universities, and hospitals. The ITA, 2025 replaces this fragmented terminology with a single, unified expression, "Registered Non-Profit Organization."

An entity falls within this regime only upon meeting the prescribed eligibility conditions, obtaining registration under section 332, and operating within the framework laid down in sections 332 to 355.

2. Shift from Chapter III to Chapter XVII-B

Under the ITA, 1961, charitable and religious institutions were dealt with in Chapter III - *"Incomes which do not form part of total income"*. This positioned the income of such entities as being outside the normal charging framework of the Act, subject to the fulfilment of prescribed conditions. Sections 11 to 13 were consistently regarded by courts as a self-contained code, operating on commercial principles rather than the head-wise computation mechanism contained in section 14.

The ITA, 2025 retains the substance of these principles but alters their statutory placement. The provisions relating to non-profit organizations are no longer situated in a chapter dealing with exclusion of income. Instead, they are contained in Part B of Chapter XVII, as part of the special provisions applicable to certain persons.

3. Consolidation of Provisions

A key feature of the ITA, 2025 is the consolidation of provisions relating to registered non-profit organizations into a dedicated and self-contained framework. Under the ITA, 1961, the regime was largely fragmented, with relevant provisions dispersed across sections dealing with exemption, investment, accumulation, and violations.

In contrast the ITA 2025 adopts a more structured and codified approach. Chapter XVII-B brings together the entire life cycle of a registered NPO, covering registration, computation of income, application and accumulation, compliance requirements, and consequences of non-compliance, within a single, integrated framework.

4. Key Changes in Registration Provisions

The ITA 2025 introduces a restructured framework governing the registration and approval of non-profit organizations. The key changes emerging under the new law may briefly be noted as follows:

(a) Registration is now governed by section 332, replacing sections 12A/ 12AB of the ITA 1961, with a corresponding restructuring of approval provisions under section 354.

(b) Eligibility for registration is now restricted to specified categories of entities such as public trusts, societies, section 8 companies, universities, and other notified persons, as against fragmented terminology under the earlier law.

(c) The expression “legal obligation”, which expanded the scope of charitable institutions under the ITA 1961, has not been retained under the ITA 2025.

(d) A specific requirement has been introduced that the entity must be constituted, registered, or incorporated in India, thereby establishing a clear territorial nexus.

(e) The law now requires that the property must be held for charitable or religious purposes in India, as against the earlier framework which primarily focused on application of income in India.

(f) The timeline for filing provisional registration application, particularly in cases of entities where activities have not commenced, has been relaxed, allowing applications to be made at any time during the relevant tax year.

(g) The eligibility conditions for fresh registration now focus on whether the entity has been previously registered under any specified provision, as against the earlier emphasis on whether exemption had been claimed.

(h) The exception available under section 80G for institutions benefiting Scheduled Castes, backward classes, Scheduled Tribes, women, and children has not been carried forward in section 354.

(i) Rule 181 introduces a system of combined application forms (Form 104/105)for registration and approval, with separate orders being issued thereafter.

(j) New procedural features have been introduced in Rule 181, including the ability to surrender provisional registration or approval, withdrawal of application within a specified time, to submit a request for correction of section code or nature of activities, if these are wrongly mentioned and a limited right to re-apply in prescribed circumstances.

(k) While the specific rule relating to entities created otherwise than under a formal instrument has not been retained, the requirement to furnish supporting documents continues through the prescribed forms.

5. Shift from "Legal Obligation" to Entity Based Registration Framework

The ITA 2025 marks a significant shift in the manner in which eligibility for the registered NPO regime is determined. Under the ITA 1961, the expression "trust" was interpreted broadly and extended to situations involving "any other legal obligation", thereby enabling even informal or customary arrangements to claim exemption under sections 11 and 12

In contrast, the ITA 2025 adopts a more structured and entity-based approach. Section 332 limits eligibility to specified categories of recognized entities, such as public trusts, societies, section 8 companies, universities, government-financed institutions, and certain notified persons.
The omission of the expression "legal obligation" represents a departure from the earlier framework.

6. Shift from Exemption Based to Computation Based Framework

Under the ITA 1961, the regime was broadly understood as one of exemption, where income derived from property held under trust was excluded from total income subject to fulfilment of specified conditions.

The ITA 2025 marks a conceptual shift by introducing a computation-based framework. Income is first determined on commercial principles, and thereafter subjected to classification and taxation under the statutory scheme. The focus is thus on computation and characterization of income, rather than mere exclusion from the tax base.

7. Introduction of Classification of Income

One of the most significant innovations under the ITA 2025 is the explicit classification of income into:

(a) Regular Income;

(b) Specified Income;

(c) Residual Income.

This classification operates after the determination of income and forms the basis for taxation under section 334.

Regular Income constitutes the primary category eligible for application and accumulation. Specified Income arises upon the occurrence of defined statutory violations and is subject to tax at a special rate. Residual Income represents the balance income not falling within the other categories and is taxed under general provisions.

8. Changes in Taxation Mechanism

Section 334 introduces a structured rate mechanism for different categories of income:

(a) Taxable Regular Income and Residual Income is taxed at the rate applicable to the entity.

(b) Specified Income is taxed at a flat rate of 30%.

The presence of a *non-obstante* clause in section 334 ensures that this framework prevails over other provisions of the Act, reinforcing its character as a special code.

9. Relocation of Proviso from Definition of Charitable Purpose

The ITA 2025 retains the traditional definition of "charitable purpose" but introduces an important structural change in its formulation. Under the ITA 1961, the definition was contained in section2(15), which included a proviso restricting commercial activities in cases of advancement of any other object of general public utility (GPU).

Under the ITA 2025, while section 2(23) continues to define "charitable purpose" in substantially similar terms, the restrictive proviso has been removed from the definition itself. Instead, the conditions governing commercial activities of NPOs engaged in GPU have been relocated to a separate provision under section 346.

10. Time Limit for Filing Form no.108 (Deemed Application)

The concept of deemed application is governed by section 341(5) to (7), which permit an NPO to treat any shortfall in application (below 85%) as application of income, subject to prescribed conditions.

Under section 341(7) read with Rule 184, this option is required to be exercised by furnishing Form No. 108 electronically on or before the due date specified under section 263(1).

A significant change from the earlier regime is the rationalization of the timeline for exercising this option. Under the ITA 1961, the corresponding provision (Explanation 2 to section 11(1)) required filing of Form No. 9A at least two months prior to the due date for furnishing the return of income (subsequently relaxed by administrative circulars).

The ITA 2025 removes this requirement of advance filing and allows the option to be exercised up to the due date of filing the return of income, thereby aligning the compliance timeline with the return filing process.

11. Time Limit and Conditions for Accumulation (Form no. 109)

The ITA 2025 retains the framework permitting accumulation or set apart of income for a specified purpose for a period not exceeding five years under section 342. The option is to be exercised by furnishing a statement in Form No. 109, specifying the purpose and period of accumulation.

A notable change relates to the timeline for exercising this option. Under section 342 read with the relevant rules, the statement is now required to be furnished on or before the due date for filing the return of income under section 263(1).

Under the ITA 1961, while accumulation under section 11(2) was also permitted for a similar period, Form No. 10 was required to be filed at least two months prior to the due date under section 139(1), though this requirement was subsequently relaxed by CBDT Circular No. 6/2023. The ITA 2025 removes this advance filing requirement altogether and aligns the timeline with the return filing due date.

Further, under the ITA 1961, section 13(9) linked the availability of accumulation benefits to the condition that the return of income must be filed within the due date. No such explicit condition has been prescribed under the ITA 2025 in relation to section 342.

12. Specified Forms for Change in Purpose of Accumulation

Section 342(5) and 342(6) permit a registered NPO to seek approval from the Assessing Officer for a change in the purpose of accumulation.

A notable change under the ITA 2025 is the introduction of a structured procedural framework for such applications. Under the ITA 1961, there was no prescribed form for seeking approval for change of purpose, nor any prescribed format for the order of the Assessing Officer.

In contrast, Rule 186 of the Income-tax Rules, 2026 now prescribes Form No. 110 for making the application and Form No. 111 for the order of the Assessing Officer approving or rejecting such request.

13. Use of the Term "Deemed Accumulated Income"

Under the ITA 2025, a registered NPO is required to apply at least 85% of its regular income for charitable or religious purposes in each tax year.

Section 343 expressly permits retention of up to 15% of such income, which is now described as "deemed accumulated income."

While this concept existed under section 11(1)(a) of the ITA 1961, the statute did not expressly use the term "deemed accumulation" for this 15% retention. The ITA 2025 formalizes this position by introducing a defined expression, thereby bringing greater clarity and precision to the treatment of such income.

14. Taxation of Entire Investment in Case of Violation

Under the ITA 2025, any investment or deposit made in contravention of section 350 is treated as specified income under section 337. This represents a significant departure from the earlier regime, as the entire amount of such investment is now brought to tax, irrespective of the source of funds, rather than taxing only the income arising therefrom.

15. Application for Non-Charitable Purposes Expressly Taxed

The ITA 2025 expressly includes within specified income under section 337 any amount applied for purposes other than the objects for which the NPO is registered. This marks a departure from the earlier framework, where such application did not constitute a separately classified category of taxable income.

16. Income Earlier Taxable Under Section 164(2) now Included Within "Specified Income"

The ITA 2025 expands the scope of "Specified Income" under section 337 by expressly including certain categories of income which were earlier governed by section164(2) of the ITA 1961.

One such category relates to deemed corpus donations. Under the ITA 2025, any deemed corpus donation in respect of which the conditions specified in section 340 are violated, such as failure to maintain separate identification or failure to invest in permissible modes, is treated as specified income and subjected to tax at 30%.

Similarly, any additional income determined by the Assessing Officer under section 344 in excess of the income disclosed in the books of account of a business undertaking held by the NPO is also specifically included within the scope of specified income.

Under the ITA 1961, both these categories were generally governed by section 164(2) and were taxable at the rates applicable to an Association of Persons (AOP).

17. Consequences for Non-Compliance Under Section 353

The ITA 2025 introduces a structured mechanism under section 353 for denial of exemption in cases of specified non-compliances, such as failure to maintain books of account, failure to get accounts audited, failure to furnish return of income, or undertaking impermissible commercial activities. In such cases, the income of the NPO is computed under a special mechanism and becomes taxable accordingly.

A notable change under the ITA 2025 is the clear distinction between substantive and procedural non-compliances. The provision restricts its application to core compliance failures listed in 353(1). It does not extend to ancillary or procedural lapses, such as failure to maintain additional documents or delay in furnishing the audit report.

18. Computation of Gains From Commercial Activites

The ITA 2025 introduces a structured mechanism for computation of gains from permissible commercial activities carried on by registered NPOs under sections 344, 345 and 346. Rule 182 of the Income-tax Rules, 2026 provides that such activities are to be treated as if carried on by a separate entity, with a requirement to maintain separate books of account, and the gains are to be computed in accordance with the provisions relating to profits and gains of business or profession.

This represents a departure from the earlier regime under the ITA 1961, where the manner of computation of such income was largely governed by general principles and judicial interpretation. The ITA 2025 formalizes this position by prescribing a clear computation framework through delegated legislation.

However, this approach gives rise to an interpretational issue when read with section 334(2), which provides that the special provisions governing NPO taxation operate not with standing other provisions of the Act. The prescription of computation under the general business income provisions may therefore create confusion between the special regime and the general computation framework.

While the rule appears to operate only for the limited purpose of computation, its interaction with the overriding provisions of the Act may require careful interpretation.

19. Segregation of GPU From Incidental Commercial Activity Framework

Under the ITA 2025, section 345 governs the permissibility of commercial activities only in respect of registered NPOs other than those engaged in the advancement of any other object of general public utility (GPU). NPOs falling under the GPU category are specifically carved out and are instead governed by a separate provision under section 346.

This represents a structural change from the position under the ITA 1961. Section 11(4A) applied uniformly to all charitable institutions, including those engaged in GPU, and permitted business activities subject to the conditions of being incidental to the objects and maintenance of separate books of account.

The ITA 2025, by contrast, segregates the treatment of commercial activities based on the nature of charitable purpose,

by placing GPU entities under a distinct framework with separate conditions and thresholds. As a result, section 345 is now confined to "per se" charitable categories, while GPU-related commercial activities are governed independently under Sec 346.

20. From Two Audit Forms to a Single Unified Audit Report

Under the ITA 1961, audit reporting requirements were prescribed through Forms 10B and 10BB, with applicability determined by thresholds relating to income, foreign contributions, and the application of income outside India.

The ITA 2025 replaces this form-based distinction with a single unified audit reportin Form No. 112.

The distinction between different categories of NPOs is now embedded within the reporting framework itself, rather than being reflected through separate audit forms.

21. Introduction of "Small" and "Large" Registered NPO Classification

The ITA 2025 introduces a formal classification of registered NPOs into "Small Registered NPOs" and "Large Registered NPOs", determined through a structured questionnaire embedded in the audit report (Form No. 112).

Under the new regime, an NPO is classified as a Large Registered NPO if any one of the following conditions is satisfied:

(a) Regular income under section 335 exceeds Rs.5 crore; or

(b) Foreign contribution received during the tax year exceeds Rs.10 lakh; or

(c) Application of income outside India exceeds Rs.10 lakh.

An NPO is classified as a Small Registered NPO only where all of the above conditions are not triggered.

This classification now serves as the basis for determining the extent of disclosure and reporting obligations under the audit framework.

22. Revised Threshold for Audit Report Form

In addition to the structural change in audit reporting, the ITA 2025 also revises the threshold criteria governing such classification.

Under the ITA 1961, Form 10B was required where the total income exceeded Rs.5 crore, or where the trust had received any foreign contribution or applied any part of its income outside India, with no minimum threshold for the latter two conditions.

The ITA 2025 replaces this form-based distinction with a single unified audit report in Form No. 112. In place of separate forms, the law now classifies NPOs as Small or Large Registered NPOs based on specified criteria.

While the Rs.5 crore income threshold has been retained, a notable change is the introduction of quantitative thresholds of Rs.10 lakh for foreign contributions and for applications of income outside India. Accordingly, an NPO is classified as a Large Registered NPO only when such amounts exceed Rs.10 lakh, as opposed to the earlier position, where any amount, however small, triggered the requirement to file Form 10B.

It is further to be noted that Section 348, dealing with audit requirements, is triggered where the total income of a

registered NPO, computed “without giving effect to the provisions of this Part,” exceeds the maximum amount not chargeable to income-tax in a given tax year, whereas the criteria for classification as a Large/Small NPO is that the Regular Income under section 335 exceeds Rs.5 crores in the relevant tax year.

23. Shift from AOP Based Taxation to Entity Based Taxation

Under the ITA 1961, section 164(2) provided that income of charitable or religious trusts which was not exempt under section 11 or 12 would be taxed “as if” such income were the income of an Association of Persons (AOP). Consequently, even where the underlying arrangement arose from a trust or other legal obligation, the taxable income was generally subjected to tax in the status of an AOP.

The ITA 2025 does not contain a corresponding provision similar to section 164(2). Instead, the new regime adopts an entity-based approach to taxation. A “Registered Non Profit Organization” is not treated as a separate category of person under the Act, but merely represents a regulatory status granted to an existing legal entity satisfying the conditions of section 332.

Accordingly, the assessment status of an NPO under the ITA 2025 depends upon its underlying legal form, such as a trust, society, section 8 company, university, or other eligible entity, rather than a deemed status of Association of Persons. This marks a structural departure from the earlier framework.

08 OVERVIEW OF REGISTRATION FRAMEWORK FOR NPOs UNDER INCOME TAX ACT, 2025

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Introduction

Section 332 of the Income-tax Act, 2025 introduces a unified and comprehensive framework governing registration of non-profit organizations, replacing the fragmented regimes that existed under the Income-tax Act, 1961.

Under the earlier law, exemptions were available through two parallel regimes: approval based exemptions under section 10(23C) and registration-based exemptions under sections 11, 12 and 12AB, which have now been consolidated under section 332 of the ITA 2025.

Approval-based exemption categories under section 10(23C) have been subsumed into the registration framework under section 332, while automatic exemption categories have been relocated to Schedule-based exemption read with section 11 of ITA 2025.

Section 332 serves as the central procedural gateway for availing an exemption under the special tax regime applicable to registered non-profit organizations set out in Part B of Chapter XVII.

The provision lays down a comprehensive code covering eligible applicants, substantive eligibility conditions, timelines and categories of registration, condonation of delay, extended validity for small NPOs, and the procedure for inquiry and grant or rejection of registration.

Under section 332(3) the timelines for processing registration applications vary by applicant status. For instance, for provisional registration where the activities of the applicant have not commenced, the timeline for granting registration is 1 month from the end of the month in which the application is made. And for regular registration and all other registration the timeline for granting registration is 6 months from the end of the quarter in which the application is made. A detailed table is provided in ***Annexure 1.***

Section332(9) provides for the regularization of expired registrations granted before 1st April 2021 under the ITA 1961, where the delay in making the application is condoned for reasonable cause. Such regularization is valid for 5 years from FY2021-22, i.e., up to FY 2025-26.

The procedural framework is supplemented by Rule 181 of the Income-tax Rules, 2026, which prescribes Forms 104 and 105 for applications and Forms 106 and 107 for orders for registration.

1. Table Comparing Old Provisions

Section 332 of the Income-tax Act, 2025 contains the comprehensive code governing registration of non-profit organizations and serves as the foundational gateway for availing exemption under the special tax regime.

The registration related sections which were scattered over section 11, 12A, 12AB, and 115TD have been consolidated provided under section 332 of ITA 2025.

The provisions dealing with registration under section 332 of the ITA 2025 vis-à-vis provisions under ITA 1961 are as follows:

ITA 2025	ITA 1961
Section 332(1)	No corresponding provision
Section 332 (2)	Section 11(1)(a) & (b)
Section 332(3)	Sections 12A(1) & 12AB
Section 332(4)	Proviso to Section 12A(1)(*a*)
Section 332(5)	Proviso to Section 12AB(1)
Section 332(6)	Section 115TD(3)(*iii*)
Section 332(7)	Section 12AB(1)
Section 332(8)	Section 12AB(1)
Section 332(9)	Section 12A(1)

2. Overview of Old Provisions Under the ITA 1961

Under the ITA 1961, charitable and religious institutions could claim ex-emption primarily under two distinct regimes:

(a) Section 10(23C): This provision provided exemptions for specified funds, universities, educational institutions, hospitals, and certain other notified entities, with sub-clauses covering approval-based and automatic exemption categories.

(b) Section 11 read with Sections 12, 12A, 12AA/12AB and 13: A registration-based regime applicable to "property held under trust wholly for charitable or religious purposes," with exemptions allowed on application or accumulation of income for such purposes.

The ITA 2025 consolidates and reorganizes these regimes by placing non-approval-based exempt categories in Schedules II to VII (read with Section 11), and by migrating approval based exemption categories into a unified registration framework under section 332.

Approval-based exemption under section 10(23C): Section 10(23C) of the ITA 1961 provided tax exemption for income received by any person on behalf of specified funds, universities, educational institutions, hospitals, and certain other notified bodies. Certain categories enjoyed automatic exemption (no approval required), such as wholly or substantially government-financed universities and hospitals, while others required approval from the Principal Commissioner or Commissioner to secure exemption.

The Finance (No. 2) Act, 2024, effective from 01-10-2024, amended the exemption process under section 10(23C) to shift from approval-based to registration-based exemption under section 12A. After 1st October 2024, no new or provisional approvals under section 10(23C) can be applied for. However, entities already holding valid approvals under Section 10(23C) continue to be governed by the existing approval regime until the expiry of the validity period of such approval.

Under the ITA 2025, these approval-based categories are subsumed within the unified registration framework under section 332, thereby replacing the earlier dual-track system.

Non-approval exemption under Section 10(23C): Apart from approval-based categories, Section 10(23C) also contained certain automatic exemption categories that did not require prior approval. These included, inter alia, universities and hospitals wholly or substantially financed by the Government, and certain educational or medical institutions that satisfied prescribed receipt thresholds.

Under the ITA 2025, these automatic exemption categories have been re-located to Schedule VII (read with Section 11), particularly Items 17, 18 and 19. The substantive conditions, such as educational or philanthropic purpose and monetary threshold limits, remain largely consistent with the earlier framework.

Thus, while the statutory placement has changed, the non-approval-based exemption regime continues under the ITA 2025 in the form of a Schedule-based exemption rather than as a standalone substantive provision.

Registration -based exemption under sections 11 and 12: Section 11 of the ITA 1961 exempted income derived from property held under trust wholly for charitable or religious purposes,

to the extent applied or accumulated for such purposes in India.

3. Registration Framework Under the ITA 2026

Under the ITA 2025, the framework is restructured. The exemption principle is preserved, but operational provisions are merged into Part B of Chapter XVII ("Special Provisions for Registered Non-Profit Organization"), with registration governed exclusively by Section 332. It absorbs and replaces multiple provisions of the ITA 1961 (Sections 12A, 12AB, approval provisions of Section 10(23C)), creating a unified procedural code for registration.

Section 332 is the central procedural gateway for any NPO seeking exemption under the ITA 2025(except for certain automatic exemption categories under the Schedules).

Section 355(f) defines registration as follows:

"(f) "registration" includes provisional registration, provisional approval or approval, as referred to in the second proviso to section 10(23C) or 12AB (1) of the Income-tax Act, 1961 and under section 332, but shall not include approval under the second proviso to section 80G(5) of the said Act or section 354;"

Furthermore, Section 355(g) defines a registered NPO as follows:

"(g) "registered non-profit organization" means any person having a valid registration under any specified provision and such registration has not been cancelled;"

A common question arises as to whether charitable or religious institutions already registered under section 12AB of the ITA 1961 are required to obtain a fresh registration under section 332 of the ITA 2025. On a plain reading of the provision, the answer is in the negative. On a conjoint reading of clauses (f) and (g) of Section 355, these definitions indicate that existing registrations under Section 12AB or Section 10(23C) of the ITA 1961 shall be deemed valid for purposes of the ITA 2025 until the expiry of their registration period under the ITA 1961. Accordingly, there is no requirement for institutions already registered under Section 12AB to re-register under Section 332 during their current validity period. Thus, the ITA 2025 preserves the continuity of status for existing NPOs, avoiding unnecessary duplication of registration processes.

Section 332 of the ITA 2025 provides the following provisions for the registration of an NPO:

(a) Eligible applicants

(b) Eligibility criteria

(c) Time limits and categories of registration

(d) Acceptance of belated applications

(e) Extended validity for Small NPOs

(f) Procedure and Inquiry before granting registration

(g) Re-registration of Pre-2021 Entities

4. Eligible Applicants Under Section 332(1)

The following persons may apply for registration as a registered non-profit organization in the prescribed form and manner to the Principal Commissioner or Commissioner:

(a) Public trusts;

(b) Societies registered under the Societies Registration Act, 1860 or any State law;

(c) Companies registered under Section 8 of the Companies Act, 2013 (or Section 25 of the 1956 Act) and deemed to have been registered in pursuance of Section 465(2) (g) of the Companies Act, 2013;

(d) Universities established by law or educational institutions recognized by the Government;

(e) Government or local authority-financed institutions;

(f) Persons specified in relevant Schedules; or

(g) Any other person notified by the Board.

5. Eligibility Criteria Under Section 332(2)

An entity qualifies for registration under the ITA 2025 if:

(a) It is constituted/ registered/ incorporated in India for charitable purposes or public religious purposes;

(b) its properties are held under an irrevocable trust for the benefit of the general public, wholly for charitable or religious purposes in India; and

(c) its properties are held under an irrevocable trust for the benefit of the general public, partly for charitable or religious purposes in India (only if established before the commencement of the ITA 1961).

6. Time Limits Categories of Registration Under Section 332(3)

The timelines for registration applications vary by applicant status. For instance, for provisional registration where the activities of the applicant have not commenced, the timeline for granting registration is 1 month from the end of the month in which the application is made. And for regular registration and all other registration the timeline for granting registration is 6 months from the end of the quarter in which the application is made. A detailed table is provided in ***Annexure 1.***

7. Condonation of Delay Under Section 332(4) and 332(6)

Section 332(4) of the Income-tax Act, 2025 empowers the Principal Commissioner or Commissioner to condone a delay in filing an application for registration where the applicant demonstrates reasonable cause for such delay.

Further, Section 332(6) provides that where an application for registration is not made within the time specified in Annexure 1 in respect of the following categories, and the delay in filing such application is not condoned, such a person shall be liable to pay tax on accreted income under section 352.

(a) Conversion of Provisional to Regular Registration (post commencement of activity)

(b) Conversion of Provisional to Regular Registration (provisional registration period is due to expire)

(c) Renewal of Regular Registration

(d) Modification of Objects.

8. Extended Validity of Small NPOs Under Section 332(5)

If an applicant (other than a first-time applicant) has total income (before exemptions) not exceeding Rs.5 crore in each of the two preceding tax years, the

registration shall be valid for 10 years (as opposed to 5 years). Accordingly, the benefit of extended validity will be available to the following categories of applicants:

(a) Entities with provisional registration that have commenced activities.

(b) Entities whose provisional registration is expiring but have not commenced activities.

(c) Entities whose registration is due to expire.

(d) Entities whose registration has become in operative due to a regime switch.

(e) Entities that have adopted or undertaken modifications to their objects that do not conform to the conditions of registration.

The benefit of extended validity will not be available to the following categories of applicants:

(a) Entities that have not yet commenced activities and were never registered under any specified provision.

(b) Entities that have commenced activities but were never registered under any specified provision.

9. Procedure and Inquiry Under Section 332(7) and 332(8)

For applications other than provisional registration, the Principal Commissioner or Commissioner may:

(a) Call for documents, conduct inquiries, and assess compliance with such requirements of any other law as are material for the purpose of achieving its objectives.

(b) If satisfied with the objects, the genuineness of the activities and compliance with the requirements of any other law in force, grant registration by passing a written order.

(c) If not satisfied, issue a written rejection order after providing the applicant an opportunity to be heard.

(d) If rejecting a subsequent application, i.e. conversion of provisional registration, regular registration renewal, or registration on modification of objects, cancel the registration as well.

A copy of the order shall be in the prescribed form, manner and communicated to the applicant and the Assessing Officer. However, if an application is made for provisional registration, the Principal Commissioner or Commissioner shall grant the registration without inquiry solely based on the application.

10. Re-registration of Pre-2021 Entities Under Section 332(9)

Section 332(9) provides for the regularization of expired registrations granted before 1st April 2021 under the ITA 1961, where the delay in making the application is condoned for reasonable cause. Such regularization is deemed valid for 5 years from FY 2021-22, i.e., up to FY 2025-26.

However, this provision raises concerns about its practical utility, as the validity period extends only to AY 2026-27, where as the ITA 2025 comes into effect from 1st April 2026, corresponding to Assessment Year 2027–28. As a result, the effective benefit of the five-year regularization period expires before the new Act becomes operative, compelling affected entities to

seek fresh registration almost immediately upon transition to the new regime.

11. Forms for Registration Applications

Rule 181 of the Income-tax Rules, 2026 prescribes that an application for provisional registration shall be furnished in Form No. 104, while applications relating to other categories of registration are required to be made in Form No. 105.

The rules and forms governing NPO registration provisions under the Income-tax Rules, 2026 vis-à-vis the corresponding provisions under the Income-tax Rules, 1962 are summarized below:

Compliance/Subject	IT Rules/ Forms 1962	IT Rules/ Forms 2026
Registration	Rule 17A	Rule 181
Fresh/Provisional Registration	Form 10A	Form 104
Regular Registration/Renewal	Form 10AB	Form 105
Order for Provisional Registration	Form 10AC	Form 106
Order for Regular Registration	Form 10AD	Form 107

Annexure 1

The timelines for registration applications vary by applicant status. The following table outlines the applicable deadlines, processing timelines, and validity periods:

Category	***Description***	***Time Limit to Apply***	***Time Limit to Pass Order***	***Validity of Registration***
Provisional Registration	For entities that have not yet commenced activities and were never registered under any specified provision.	Any time during the tax year from which registration is sought.	Within 1 month from the end of the month in which the application is made.	3 tax years from the tax year in which the application is made.
Regular Registration	For entities that have commenced activities but were never registered under any specified provision.	Any time during the tax year from which registration is sought.	Within 6 months from the end of the quarter in which the application is made.	5 tax years from the tax year in which the application is made.
Conversion of Provisional to Regular Registration (post commencement of activity)	For entities with provisional registration that have commenced activities.	Within 6 months of the commencement of activities.	Within 6 months from the end of the quarter in which the application is made.	5 tax years from the tax year in which the application is made.
Conversion of Provisional to Regular Registration (provisional registration period is due to expire)	For entities whose provisional registration is expiring but have not commenced activities.	At least 6 months prior to the expiry of provisional registration.	Within 6 months from the end of the quarter in which the application is made.	5 tax years following the tax year in which the application is made.

Category	*Description*	*Time Limit to Apply*	*Time Limit to Pass Order*	*Validity of Registration*
Renewal of Regular Registration	For entities whose registration is due to expire.	At least 6 months prior to the expiry of registration.	Within 6 months from the end of the quarter in which the application is made.	5 tax years following the tax year in which the application is made.
Reactivation of Registration (after switching exemption regime)	For entities whose registration became inoperative due to a regime switch.	Any time during the tax year from which reactivation is sought.	Within 6 months from the end of the quarter in which the application is made.	5 tax years from the tax year in which the application is made.
Modification of Objects	For entities that have adopted or undertaken modification of their objects which do not conform to the conditions of registration.	Within 30 days of the date of such adoption or modification.	Within 6 months from the end of the quarter in which the application is made.	5 tax years from the tax year in which the application is made.

9 BOOKS AND RECORDS UNDER INCOME TAX ACT, 1961

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NOTE

The Income Tax Act, 2025 has been enacted and has come into effect from 01 April 2026. However, this article is based on the provisions of the Income-tax Act, 1961, which continue to govern the maintenance of books of account and related reporting requirements as for the Financial Year 2025–26.
Readers are advised to refer to the applicable law for the relevant financial year while interpreting compliance requirements.

Introduction

It may be noted that up to the Finance Act, 2022, there was no specific requirement to maintain books of accountby trusts and institutions. Although, certain provisions made it an inherent requirement to maintain the books of accountby the charitable institutions.

The Finance Act, 2022 has introduced additional requirements to maintain books of account by the trusts and institutions under section 12A(1)(b)(i) with effect from the assessment year 2023-24.

The CBDT has notified Rule 17AA *vide* Notification No. 94/2022 dated 10-08-2022, which prescribes the books and other documents to be kept and maintained by entities approved under Section 10(23C) or registered under Section 12AB.

After the enactment of section 12A(1)(b)(i) and Rule 17AA, charitable organizations have been subjected to extensive requirements for maintenance of books of account and allied records.

Prior to the insertion of explicit provision by the Finance Act 2022, there was no specific requirement to maintain books of accoun tby trusts and institutions. However, there were several provisions which made it an inherent requirement to maintain the books of account for charitable trusts and institutions.

1. Requirement of Audit Implied Books of Account

One of the conditions for availing exemptions under section 11 and section 12 is auditing the organization's accounts under section 12A(1) (b)(ii). As per the prevailing provisions, the audit report must be obtained and furnished at least one month before submitting the income tax return.

The monetary limit for compulsory audit under section12A(1)(b)(ii) is currently Rs.4,00,000. The accounts of the trust should be audited if the total income of the trust or institution as computed under the

Income-tax Act, without giving effect to the provisions of section 11 and section 12 exceeds the maximum amount that is not chargeable to income tax in any previous year. Since charitable institutions that have receipts above Rs.4,00,000 are mandatorily required to get accounts audited, in a way, it is an essential requirement for them to maintain books of account that need to be audited by a chartered accountant.

In the audit report in Form 10B/10BB, the auditor has to certify that he has examined the balance sheet and the Profit and loss account of the trust or institution, which are in agreement with the books of account maintained by the said trust or institution.

2. Books of Account for Incidental Business Activity

Income from a business carried on by a trust shall be treated as income from 'property held under trust.' Such business income shall be eligible for exemption under Section 11 if it is incidental to the attainment of objectives of the trust and separate books of account are maintained by the trust in respect of such business.

The Hon'ble High Court of Madras, in the case of *DIT v. Willington Charitable Trust* [2010] 195 Taxman 232 held that maintenance of separate books of account is mandatory and a condition precedent for the assessee to seek exemption under section 11. The court observed that in so far as the compliance of the maintenance of separate books of account required under section 11(4A) is concerned, a reading of the above-said provisions would make it clear that it is mandatory and a condition precedent for the assessee to maintain the same while seeking exemption.

3. Submission of Accounts at the Time of Registration

Application for registration/approval under the new scheme of registration/ approval effective from 01-04-2021 for charitable and religious entities seeking registration/approval under section 12AB/10(23C)/80G/35 is to be filed in Form 10A/Form 10AB.

The rules provide the list of documents to be furnished while making the application in Form 10A or 10AB. One of the prescribed attachments is that where the applicant has been in existence during any year or years prior to the financial year in which the application for registration is made, self-certified copies of the annual accounts of the applicant relating to such prior year or years (not being more than three years immediately preceding the year in which the said application is made) for which such accounts have been made up.

4. Requirement of Books of Account Under Section 80G

Deduction under section 80G is allowed when a person donates to a fund or institution specified in the provision itself or is notified by the tax authorities for deduction under the said section. The income-tax authority notifies a fund or institution only when it fulfils the conditions as specified under section 80G(5). One of the prescribed conditions is that such a fund or institution should maintain regular books of account.

5. Insertion of Explicit Provision by the Finance Act 2022

The Finance Act, 2022 amended Section 12A(1)(b), imposing an explicit requirement to maintain books of account by charitable institutions. A similar requirement of maintenance of books of accounts is

introduced for the institutions approved under Section 10(23C) pursuant to the tenth proviso to Section 10(23C).

Section 12A(1)(b) of Income Tax Act, 1961:

"(b) where the total income of the trust or institution as computed under this Act without giving effect to the provisions of sections 11 and 12 exceeds the maximum amountwhich is not chargeable to income-tax in any previous year,—

(i) the books of account and other documents have been kept and maintained in such form and manner and at such place, as may be prescribed; and"

Tenth proviso to Section 10(23C) of Income Tax Act, 1961:

"Provided also that where the total income of the fund or institution or trust or any university or other educational institution or any hospital or other medical institution referred to in sub-clause (iv) or sub-clause (v) or sub-clause (vi) or sub-clause (via), without giving effect to the provisions of the said sub-clauses, exceeds the maximum amount which is not chargeable to tax in any previous year, such fund or institution or trust or any university or other educational institution or any hospital or other medical institution shall, —

(a) keep and maintain books of account and other documents in such form and manner and at such place, as may be prescribed; and"

Condition of the requirement to maintain books of account: The Finance Act, 2022 amended Section 12A(1)(b) to provide that where the total income of the trust or institution without giving effect to an exemption under sections 11 and 12, exceeds the maximum amount which is not chargeable to tax, such trust or institution shall keep and maintain books of accountand other documentsin such form and manner and at such place, as may be prescribed. This amendment is effective from the assessment year 2023-24.

Applicable if total income exceeds Rs.4,00,000: This provision regarding maintenance of prescribed books of account and other documents is applicable only if the total income of the charitable institution as computed under the Act without giving effect to the provisions of sections 11 and 12 exceeds the maximum amount, which is not chargeable to income tax in the previous year.

It is thus, not applicable to institutions whose total income (ignoring sections11 and 12) is less than or equal to Rs.4,00,000.

6. Meaning of Books of Account

The term 'books of account' has been defined in section 2(12A) as under:

"books or books of account" includes ledgers, day-books, cash books, account-books and other books, whether kept in the written form or in electronic form or in digital form or as print-outs of data stored in such electronic form or in digital form or in a floppy, disc, tape or any other form of electromagnetic data storage device;

Thus, as per the definition under section 2(12A), the books of account include the following:

(a) Ledgers

(b) Day-books

(c) Cash books

(d) Account books

(e) Other books

7. List of Books & Documents Under Rule 17AA

The CBDT has notified Rule 17AA *vide* Notification No. 94/2022 dated 10-08-2022, which prescribes the books and other documents to be kept and maintained by entities approved under Section 10(23C) or registered under Section12AB. Here is a list of the books and documents to be maintained by the trust or institution:

(a) Books of account;

(b) Record of contributions received;

(c) Records of application of income;

(d) Records of donations made;

(e) Records of money invested or deposited;

(f) Records of income accumulated;

(g) Records of loans and borrowings;

(h) Records of properties;

(i) Records of specified persons;

(j) Records of income and projects; and

(k) Any other documents containing any other relevant information.

Books of accounts to be maintained by a trust or institution: A trust or institution shall maintain the following books of account:

(a) Cash book;

(b) Ledger;

(c) Journal;

(d) Copies of bills issued by the trust or institution (machine numbered or otherwise serially numbered);

(e) Copies or counterfoils of receipts issued by the trust or institution (machine numbered or otherwise serially numbered);

(f) Original bills issued to the trust or institution and receipts in respect of payments made; and

(g) Any other book that may be required to give a true and fair view of the state of the affairs of the trust or institution and explain the transactions effected.

These books of account shall also be maintained for business undertaking under Section 11(4) and other business carried on by the trust or institution.

8. Records of Contributions and Donations

Type of contributions: A trust or institution registered under Section 12AB or approved under Section 10(23C) shall maintain the records of the following contributions:

(a) Voluntary contributions;

(b) Voluntary contributions made with a specific direction that they shall form part of the corpus;

(c) Contribution received (in the current year or past years) for renovation or repair of the temple, mosque, gurdwara, church, or other place notified under Section 80G(2)(b), that is being treated as corpus during the current year.

Which records of contributions shall be maintained? : A trust or institution shall maintain the following records separately of each contribution as referred to above:

(a) Name of the donor;

(b) Address;

(c) Permanent account number (if available); and

(d) Aadhaar number (if available).

9. Records of Application or Utilisation

Types of application of income: A trust or institution registered under Section 12AB or approved under Section 10(23C) shall maintain the records of the following application of income:

(a) Application of income in India;

(b) Application of income outside India;

(c) Deemed application of income due to non-receipt of income or for any other reason;

(d) Application out of the accumulated income

(e) Application out of income deemed to be applied in preceding years;

(f) Application out of corpus contribution;

(g) Application out of contribution received (in the current year or past years) for renovation or repair of the temple, mosque, gurdwara, church, or other notified places, which is being treated as corpus during the current year;

Which records of application of income shall be maintained? : A trust or institution shall maintain the following records separately of each application of income as referredto above:

(a) Details of the amount of application;

(b) Name and address of the person to whom any credit or payment is made;

(c) Object for which such application is made.

Additional records to be maintained: In the following cases, the additional records shall also be maintained:

(i) Application out of accumulated funds

In the case of the application out of the accumulated funds, the following records shall also be maintained:

(a) Year of accumulation;

(b) Application out of income accumulated during the previous year;

(c) Application out of income accumulated during any preceding previous year.

(ii) Deemed application

In the case of the deemed application, the following records shall also be maintained:

(a) Reasons for deemed application;

(b) Year of deemed application;

10. Records of Donations Given to Other Institutions

Types of donations: A trust or institution shall maintain the records of the amount paid or credited to another trust or institution registered under Section 12AB or approved under Section 10(23C) from the following:

(a) Out of the voluntary contribution;

(b) Out of the corpus contribution received during the previous year (if credited or paid towards the corpus);

(c) Out of the corpus contribution received during any of the preceding previous year (if credited or paid towards the corpus);

(d) Out of the corpus contribution received during the previous year for renovation or repair of the temple, mosque, gurdwara, church, or other notified places (if credited or paid towards the corpus);

(e) Out of the corpus contribution received during any of the preceding previous year for renovation or repair of the temple, mosque, gurdwara, church, or other notified places (if credited or paid towards the corpus).

Which records of donation shall be maintained? : A trust or institution shall maintain the following records separately of each amount paid or credited as referred to above:

(a) Name;

(b) Address;

(c) Permanent account number; and

(d) Object for which such credit or payment is made.

11. Records of Investment

Which income should be invested in the specified mode? : Section 11(5) specifies the permissible mode in which the income of a trust or institution registered under Section 12AB or approved under Section 10(23C) can be invested or deposited. A trust or institution is required to maintain the records of investments or deposits made out of the following incomes or contributions:

(a) Current year income;

(b) Accumulated income;

(d) Corpus contribution received for renovation or repair of the temple, mosque, gurdwara, church, or other notified places.

Which records of donation shall be maintained ? *:* A trust or institution shall maintain the following records separately of each income as referred to above invested or deposited in permissible modes specified in Section11(5):

(a) Money received during the previous year and invested or deposited in permissible modes;

(b) Money received during the previous year and invested or deposited in other than the permissible modes;

(c) Money received during any previous year preceding the previous year and invested or deposited in permissible modes;

(d) Money received during any previous year preceding the previous year and invested or deposited in other than the permissible modes;

(e) Money invested or deposited back into corpus donation, which was applied during any preceding previous year and not claimed as application.

12. Records of Income Accumulated by a Trust or Institution

Where a trustor institution registered under Section 12AB or approved under Section 10(23C) is not able to apply 85% of its income in a particular year, it can accumulate the shortfall to be used for religious or charitable purposes within the next 5 years. This accumulation is allowed

if the assessing officer is informed about the purpose of the accumulation and the period for which the income is being accumulated.

The trust or institution shall maintain the records containing details of the purpose for which such income has been accumulated.

13. Records of Loans and Borrowings Taken by a Trust or Institution

Where a trustor institution registered under Section 12AB or approved under Section 10(23C) takes loans or borrowings, it shall maintain the following records:

Details of loan and borrowings: The records to be maintained for loans and borrowings shall contain the following:

(a) Amount of loan or borrowing;

(b) Date of loan or borrowing;

(c) Amount of repayment;

(d) Date of repayment;

(e) Name of the lender;

(f) Address of lender;

(g) Permanent Account Number of the lender; and

(h) Aadhaar number (if available) of the lender.

Records shall also be maintained for the repayment of loan or borrowing during the previous year, whichwas applied during any preceding previous year but not claimed as an application.

Application out of loans and borrowings: The records to be maintained for application out of the loan or borrowing shall contain the following:

(a) Amount of application;

(b) Name of the person to whom any credit or payment is made;

(c) Address of the person to whom any credit or payment is made; and

(d) Object for which such application is made.

Application out of loans of preceding years: The records to be maintained for application out of the loan or borrowing received during any previous year preceding the previous year shall contain the following:

(a) Amount of application;

(b) Name of the person to whom any credit or payment is made; and

(c) Address of the person to whom any credit or payment is made.

14. Records of Properties of a Trust or Institution

A trust or institution registered under Section 12AB or approved under Section 10(23C) shall maintain the following records of properties held by it:

Records of immovable properties: The trust or institution shall maintain the records of immovable properties containing the following details:

(a) Nature of the properties;

(b) Address;

(c) Cost of acquisition;

(d) Registration documents;

(e) Transfer of such properties;

(f) Net consideration utilized in acquiring the new capital asset.

Records of movable properties: The trust or institution shall maintain the records of movable properties, including details of the nature and cost of acquisition of the asset.

15. Records of Specified Persons of a Trust or Institution

Section 13 prescribes certain circumstances in which the exemption under Section 11/12 or Section 10(23C) is withdrawn. One of such circumstance is the application of income for the benefit of the interested person prescribe dunder Section 13(3). A trust or institution shall maintain the following records of such specified persons:

Details of specified person: The trust or institution shall maintain the records of specified persons containing the following details:

(a) Name;

(b) Address;

(c) Permanent Account Number; and

(d) Aadhaar number (if available).

Details of transaction with specified person: The trust or institution shall maintain the records of transactions with specified persons containing the following details:

(a) Date of the transaction;

(b) Amount of transaction;

(c) Nature of the transaction; and

(d) Documents to the effect that such transaction is, directly or indirectly, not for the benefit of such specified person.

16. Records of Income and Projects

A trust or institution registered under Section 12AB or approved under Section 10(23C) shall maintain the following records of income earned by it during the previous year:

Record of income: The trust or institution shall maintain the records of income containing the following details:

(a) Income from property held under trust along with a list of such properties;

(b) Income of trust or institution other than the voluntary contribution.

Records of projects and institutions: A trust or institution shall maintain the records of all the projects and institutions run by it containing the following details:

(a) Name;

(b) Address; and

(c) Objectives.

17. Manner of Keeping Books of Account

The books of account and other documents may be kept in the following forms:

(a) Written;

(b) Electronic form;

(c) Digital form;

(d) Print-outs of data stored in electronic or digital form; or

(e) Any other form of electromagnetic data storage device

18. Place of Keeping Books of Account

The books of account and other documents shall be kept and maintained by the trust or institution at its registered office.

Such books of account and other documents may be kept at such other place in India as the management may decide if the following conditions are satisfied:

(a) A resolution is passed for such purposes;

(b) An intimation is given to the jurisdictional Assessing Officer in writing within 7 days;

(c) In such intimation, the full address of that other place is mentioned; and

(d) The intimation is duly signed and verified by the person who is authorized to verify the return of income under Section 140.

19.Period for which Books are to be Maintained

The books of account and other documents shall be kept and maintained for a period of 10 years from the end of the relevant assessment year.

However, where the assessment of any assessment year has been reopened under Section 147 within the period specified in Section 149, such books of account and other documents (kept and maintained at the time of reopening of the assessment) shall continue to be so kept and maintained till the assessment has become final.

10 ACCOUNT AND AUDIT PENAL PROVISIONS

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NOTE

The Income Tax Act, 2025 has been enacted and has come into effect from 01 April 2026. However, this article is based on the provisions of the Income-tax Act, 1961, which continue to govern the maintenance of books of account and related reporting requirements as for the Financial Year 2025–26.
Readers are advised to refer to the applicable law for the relevant financial year while interpreting compliance requirements.

Introduction

The Finance Act, 2022 inserted sections 13(10) and 13(11) with effect from the assessment year 2023-24 to provide that if the accounts of the trust or institution have not been audited or books of accounts have not been maintained, the income chargeable to tax shall be computed after allowing a deduction for only those expenditure specified in these sections.

CBDT has issued circular for condonation of delay in filing Form 10B and Form 10BB, which may be referred to if there is a delay in the submission of the audit report.

Following the amendments made by the Finance Act of 2020, the audit report requirements have been specifically linked with section 44AB. Therefore, the audit report must now be obtained and filed at least one month prior to the due date for submitting the Return. Previously, the provision required that the audit report be filed along with the return.

The amended provision stipulates that the audit report should be furnished before the specified date referred to in section44AB. As a result, it appears that from the assessment year 2020-21 onwards, the filing of the audit report has become a mandatory requirement.

1. Submission of the Audit Report: Directory or Mandatory?

The Finance Act 2020 has explicitly mandated that the audit report be obtained and furnished one month prior to the due date under section 139(1). There were numerous judicial precedents where it has been determined that although submitting Form 10B along with the return is one of the conditions for claiming benefits under sections 11 and 12, it is a directory requirement rather than a mandatory one. In other words, it is a curable defect, and the Assessing Officer should accept the belated filing of the Audit Report in Form 10B. However, following the amendments made by the Finance Act 2020, the audit report must now be obtained and filed at least one month prior to the due date for submitting the Return. Previously, the provision required that the audit report be filed along with the return of income. The amended provision stipulates that the audit report should be furnished before the specified date referred to in section 44AB.

As a result, it appears that from the assessment year 2020-21 onwards, the filing of the audit report has become a mandatory requirement.

Hence, in light of the amendments, the filing of audit reports seems to be a mandatory requirement, which used to be a directory in nature, i.e., prior to the assessment year 2020-21.

2. Delay in Obtaining/Submission of Audit Report w.e.f. AY 2023-24

If there is a delay in obtaining and furnishing the audit report at least one month prior to the due date, it will result in non-compliance with one of the conditions specified under section12A. However, from AY 2023-24 this violation of condition will not result in withdrawal of benefit under sections11 and 12, but incomeshall be computed under newly inserted provisions of Section 13(10) and Section 13(11).

3. Computation of Income as per Section 13(10) & 13(11)

The Finance Act 2022 inserted sections 13(10) and 13(11), with effect from the assessment year 2023-24. Similarly, the twenty-second proviso was inserted into section 10(23C). In the following cases, the benefit of exemption under Section 11/12 or Section10(23C) shall not be available, if:

(a) Trust or institution has not obtained the audit report

(b) Books of accountand other documents have not been kept in the prescribed form/manner/place

(c) Trust or institution has not furnished the return of income within the time allowed under section 139(4A)

(d) If proviso to section 2(15) is applicable to trust or institution

Consequently, if a trust or institution has no to btained an audit report or has not maintained its books of account, the benefit of exemption will be denied to them in that assessment year.

In case of violation, the income for that specific year will be calculated according to the specific provisions outlined in the twenty-second proviso to Section 10(23C) and Section 13(10)/13(11). These provisions provide that in case specified conditions are violated, the income chargeable to tax shall be computed after allowing a deduction for expenditure incurred for the objects of the institution as specified in this section.

It provides that the income chargeable to tax shall be computed after allowing the deduction for the expenditure (other than capital expenditure) incurred in India for the objects of the trust or institution, subject to fulfilment of the following conditions, namely:

(a) Such expenditure is not from the corpus standing to the credit of such trust or institution as on the last day of the financial year immediately preceding the previous year relevant to the assessment year for which the income is being computed;

(b) Such expenditure is not from any loan or borrowing;

(c) Claim of depreciation is not in respect of an asset, acquisition of which has been claimed as an application of income in the same or any other previous year; and

(d) Such expenditure is not in the form of any contribution or donation to any person.

The provisions of Section 40(a)(ia), Section 40A(3) and Section 40A(3A) shall, *mutatis mutandis,* apply as they apply in computing the income chargeable under the head "Profits and gains of business or profession". Therefore, the disallowances shall be made for the cash payment of expenditure and non-deduction or non-payment of TDS on the sum payable to a resident.

Further, no deduction of any expenditure or allowance or set-off of any loss shall be allowed to the assessee under any other provision of the Act.

4. Condonation of Delay in Filing Audit Report in Form 10B/10BB

CBDT has issued circular for condonation of delay in filing Form 10B and Form 10BB which may be referred to if there isa delay in the submission of the audit report.

Delay in filing Form 10B/10BB: The CBDT has authorized the Principal Commissioner/Commissioner to admit belated applications under Section 119(2)(b) for condonation of delay in filing of Form 10B/10BB. Such a belated application shall be admitted as per the provisions explained below.

(a) Up to 365 days delay in filing of Form 10B/10BB for assessment year 2018-19 & onwards [Circular No. 16/2024, dated 18-11-2024]

In cases of delay of up to 365 days in filing of Form 10B/10BB, Pr. CsIT/ CsIT can admit applications for condonation and decide on merit. While entertaining such applications, Pr. CsIT/CsIT shall satisfy themself that the assessee was prevented by reasonable cause from filing such application within the stipulated time.

(b) More than 365 days delay in filing of Form 10B/10BB for assessment year 2018-19 & onwards [Circular No. 16/2024, dated 18-11-2024]

In cases of delay of more than 365 days and up to three years in the filing of Form 10B/10BB for AY 2018-19 or for any subsequent Assessment Years, the Pr. CCsIT/CCsIT/DGsIT are authorized to admit such applications of condonation of delay and decide on merits.

The Pr. CCsIT/CCsIT/CsIT/DGsIT, while entertaining such applications for condonation of delay in filing of Form 10B/10BB, shall satisfy themself that the applicant was prevented by reasonable cause from filing such form within the stipulated time. Such application for condonation shall preferably be disposed of within six months from the end of the month of receipt of the application.

11 CONDONATION OF DELAY IN 80G RENEWAL

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CA Suresh Kejriwal,
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Introduction

CBDT has issued Circular No. 06/2026 dated July 2, 2026 (F. No. 300176/ 3/2026-ITA-I) which condones the delay inelectronic filing of Form No. 10AB for regular approval under section 80G(5) of the Income Tax Act, 1961. The Circular is provided in ***Annexure 1.***

This circular condones the delay in filing of the application of the NPOs that filed their Form 10AB application for 80G approval electronically between October 1, 2025, and March 31, 2026, after missing the original due date of September 30, 2025.

It may be noted that applications previously rejected solely due to late submission within this window will now be treated as condoned and must be reconsidered on their merits.

The jurisdictional Principal Commissioner or Commissioner of Income-tax must dispose of these applications on or before December 31, 2026.

1. Background

Section 80G of the Income-tax Act, 1961 provides for deduction in respect of donations made to certain funds and institutions.

Under clause (ii) of the first proviso to section 80G(5), a fund or institution already approved under section 80G(5), whose approval is due to expire, is required to file an application for renewal in Form No. 10AB electronically, at least six months prior to expiry of the said approval period.

For approvals expiring on 31.03.2026, the statutory due date for filing Form No. 10AB was 30.09.2025. A number of funds and institutions were unable to meet this deadline on account of bona fide reasons and representations to this effect were made to the Central Board of Direct Taxes ("CBDT" or "the Board") for consideration of application filed after the due date 30.09.2025. In response CBDT has issued Circular No. 06/2026 dated July 2, 2026 (F. No. 300176/3/2026-ITA-I) condoning the delay, however, circular raises certain issues and confusions which have not been effectively addressed and are discussed in this article.

2. Relief Granted by the Circular

The CBDT has in exercise of its powers under section119(2)(b) of the Income-tax Act, 1961 read with section 536(2) of the Income Tax Act, 2025, granted the following relief in case of application being submitted under section 80G(5)(ii) :

Condonation of delay: Where Form No. 10AB has been furnished electronically between 01.10.2025 and 31.03.2026, the delay in filing (beyond the original due date of 30.09.2025) stands condoned.

Deemed condonation in rejected cases: Where an application in Form No. 10AB filed within the same window (01.10.2025 to 31.03.2026) has already been rejected solely on the ground of delay, the delay is deemed to have been condoned as on the date of issue of the Circular.

Disposal authority and timeline: The jurisdictional Principal Commissioner of Income-tax ("Pr. CIT") or Commissioner of Income-tax ("CIT")is authorized to dispose of such applications on merits, with the order to be passed on or before 31.12.2026.

The Circular clarifies that it does not confer any automatic entitlement to approval under section 80G(5), or under the corresponding provision (section 133(1)(b)) of the Income Tax Act, 2025. Each application will still be examined and decided on merits.

3. Applicability of the Circular and Suggested Action to be Taken

The table below summarizes the scenarios covered by the Circular and the corresponding action to be taken.

Scenario	Description	Action Required	Timeline
A	Form No. 10AB filed electronically between 01.10.2025 and 31.03.2026 (i.e., after the original due date of 30.09.2025), and the application is still pending disposal.	Delay stands condoned by this Circular. No fresh application or condonation request is needed. Await disposal by the jurisdictional Pr. CIT/CIT on merits.	Order expected on or before 31.12.2026
B	Form No. 10AB filed within the same window (01.10.2025 to 31.03.2026) but already rejected solely on the ground of being filed beyond 30.09.2025.	Delay is deemed condoned automatically. Recommended: write to the jurisdictional Pr. CIT/CIT (with a copy of the rejection order and this Circular) requesting revival/ disposal of the application on merits.	Order expected on or before 31.12.2026
C	Form No. 10AB not filed at all, or filed after 31.03.2026, or rejected for reasons other than delay alone.	Not covered by this Circular. No automatic relief;	Not applicable

4. No Real Relief to Renewal Category Applications

The circular has condoned the delay of applications filed between 01.10.2025 to 31.03.2026, but under the prevailing Income Tax Law, an organization can continue the same benefit, even if it makes a fresh application after 01.04.2026 under section 354 of the Income Tax Act 2025 (the new section against section80G) and get the approval with effect from the Tax Year 2026-27.

Therefore, as the earlier approval was having its validity up to asst. year 2026-27 and a fresh approval shall be having validity with effect from tax Year 2026 -27 both with a validity period of five years.

Therefore, an NPO whose80G(5) approval expired on 31.03.2026 is independently eligible to move a fresh application under section 354 (Table Sl. No. 2) of the 2025 Act for a fresh approval. It is important to note here that such an approval, when granted, is expressed to be effective from the tax year in which the application is made.

5. Provisional to Regular Registration not Covered

The next important issue to note is that the circular does not provide any relief to the organization having provisional registration and have made delay in filing of application for regular registration. The condonation of delay applies strictly to delayed filings under clause (ii) of the first proviso to section 80G(5) — i.e., renewal of an existing registration under section 80G which is set to expire. The circular does not extend similar condonation to delayed filings by NPOs falling under other clauses of the first proviso to section 80G(5) such clause(iii), covering conversion of provisional approval to regular approval.

It may not be legally sustainable to deprive the organizations which fall under clause (iii) of section 80G(5). In this context, one may rely on the Madras High Court's decision in Sri Narsimha Priya Charitable Trust v. Central Board of Direct Taxes, 2024 SCC OnLine Mad 729 (decided 02.04.2024). In this case the Madras High Court adjudicated the legality of CBDT Circular No. 6 of 2023 in which also the delay of the organization falling in category (iii) was not condoned. The Madras High Court observed that once the Board itself recognized genuine hardship as the basis for granting an extension, excluding one similarly-placed category without any stated rationale amounted to an artificial classification bearing no nexus to the object of the circular, and was therefore arbitrary and violative of Article 14 of the Constitution. The Court directed the CBDT to consider such excluded category also for condonation. In the light of the Madras High Court decision, it seems that similar benefit of condonation should be available to organization falling under clause (iii) of section 80G(5) also.

Annexure 1

CIRCULAR NO. 06 /2026

F. NO. 300176/3/2026-ITA-I
Government of India / भारत सरकार
Ministry of Finance /वित्त मंत्रालय
Department of Revenue / राजस्व विभाग
Central Board of Direct Taxes केंद्रीय प्रत्यक्ष कर बोर्ड

Sub: Condonation of delay in filing Form No. 10AB electronically for approval under clause (ii) of the first proviso to section 80G(5) of the Income-tax Act, 1961 – reg.

Section 80G of the Income-tax Act, 1961 ("the Act") provides for deduction in respect of donations made to certain funds and institutions. For availing approval under clause (ii) of the first proviso to section 80G(5) of the Act, a fund or institution approved under section 80G(5) and whose approval is due to expire, is required to furnish an application in Form No. 10AB electronically, at least six months prior to expiry of the said period.

2. Representations have been received in the Board from certain funds and institutions whose approval was expiring on 31.03.2026 and who could not furnish Form No. 10AB for seeking approval under clause (ii) of the first proviso to section 80G(5) of the Act within the due date of 30.09.2025.

It has been represented that the delay in furnishing the prescribed application was attributable to bona fide reasons and other circumstances resulting in genuine hardship to the funds or institutions in terms of receipt of donations.

3. The matter has been examined by the Board. In order to mitigate genuine hardship to such funds and institutions, the Central Board of Direct Taxes, in exercise of the powers conferred under section 119(2)(b) of the Income Tax Act, 1961 read with section 536(2) of Income Tax Act, 2025, hereby condones the delay in filling Form No. 10AB, where the prescribed application in Form No.10AB has been furnished electronically between 01.10.2025 to 31.03.2026. The jurisdictional Principal Commissioner of Income-tax or Commissioner of Income-tax are authorized to dispose of such applications on merits and pass an order on or before 31.12.2026.

4. Further, where an application in Form No. 10AB filed electronically between 01.10.2025 to 31.03.2026 has been rejected as on date of issue of this circular solely on the ground that it was furnished beyond the prescribed time limit of 30.09.2025, the delay shall be deemed to have been condoned in such cases. The jurisdictional Principal Commissioner of Income-tax or Commissioner of Income-tax are authorized to dispose of such applications on merits and pass an order on or before 31.12.2026.

5. Nothing contained in this Circular shall be construed as conferring any automatic entitlement to approval under section 80G(5) of the Act or section 133(1)(b) of I.T. Act, 2025, as the case may be.

6. Hindi version shall follow.

(Hardev Singh)
Under Secretary (ITA-I), CBDT

Copy to:

1. PS to FM/OSD to FM/PS to MoS(R)/OSD to MoS(R)
2. PPS to Revenue Secretary
3. Chairman, CBDT & All Members, CBDT
4. All Pr. Chief Commissioners of Income-tax/Pr. Directors General of Income-tax
5. Pr. Chief Controller of Accounts, New Delhi
6. All Joint Secretaries/Commissioners, CBDT
7. Web Manager, O/o Pr. DGIT(Systems) with request to upload on https://incometaxindia.gov.in
8. Commissioner of Income-tax (Media & TP) and Official Spokesperson of CBDT, New Delhi
9. Secretary General, IRS Association/Secretary General, ITGOA/All-India Income-tax SC & ST Employees' Welfare Association/Income-tax Employees Federation (ITEF)
10. JCIT, Data-Base Cell for uploading on www.irsofficersonline.gov.in
11. Guard File.

Under Secretary (ITA-I), CBDT

12 CONSOLIDATION OF ACCOUNTS OF A SECTION 8 COMPANY

By: Adv. (Dr.) Manoj Fogla,
Founder, SAGA LAW LLP
CA Suresh Kejriwal,
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Introduction

Section 8 companies are formed with charitable objects, and the profits of a subsidiary cannot be distributed back to the members, including a holding company. Section 8 companies are formed without profit motive, however if there is any profit then such profit shall be applied in promoting its objects. At the time of winding up or dissolution, surplus assets, if any, shall be transferred to another company registered under Section 8 having similar objects.

In case of conversion of a Section 8 company into any other kind of company the Board of directors are required to give a declaration to the effect that no portion of the income or property of the company has been or shall be paid or transferred directly or indirectly by way of dividend or bonus or otherwise to persons who are or have been members of the company or to any one or more of them or to any persons claiming through any one or more of them [Rule 22(4) of Companies (Incorporation) Rules, 2014].

Section 129 of the Companies Act, 2013 mandates preparation of consolidated financial statements in accordance with applicable accounting standards, therefore, the applicable accounting standards needs to be considered in this regard.

The scope of AS 21, as defined by the Institute of Chartered Accountants of India, clearly excludes the control over those entities from where economic benefit are not permissible. Further, under para 11 of the AS 21, it is again clarified that the consolidation shall not be necessary if there are permanent restrictions on the subsidiary regarding transfer of profits to the holding company. It has been clarified that the company in such circumstances may disclose the reasons for not consolidating a subsidiary should be disclosed in the consolidated financial statements.

In contrast to AS 21, Ind AS 110 is based on variable return and not economic benefit. Variable return is much wider concept than economic benefit. While economic benefit only considers profit or loss, variable return is broad and extends well beyond purely financial gains.

Now, the question arises whether the accounts of a section 8 company are required to be consolidated with the CSR company if such section 8 company is a subsidiary.

The Expert Advisory Committee (EAC) of the ICAI has examined the matter relating to the consolidation of a Section 8 company with the sponsor company and opined that since the Company exercises control over the Section 8 Company and no specific exemption is provided under Ind AS 110 or the Companies Act, 2013, from the requirement to consolidate a Section 8 Company, the Company is required to

consolidate the financial statements of its sponsored Section 8 Company.

It has to be understood that the holding company of a section 8 company cannot directly or indirectly benefit out of the section 8 company. If the accounts of the section 8 company are consolidated into the holding CSR company then such consolidation may result in increase in the networth, book value, and EPS of the holding company, which will consequently result in indirect benefit to the shareholders of the holding company. Otherwise also a section 8 company is a legal obligation held on behalf of public at large and any assets held in fiduciary capacity can never be consolidated with the assets of the trustees held in personal capacity.

When we consolidate the holding company with a Section 8 company, it will however depict a wrong picture of the wealth of the holding company, as the holding company can never claim any right over the profits of a Section 8 Company. Therefore, the question of consolidation does not arise.

1. Consolidation Under Section 129 of The Companies Act, 2013

Section 129 mandates preparation of consolidated financial statements in accordance with applicable accounting standards as is evident from the sub section (3) of section 129, as reproduced below:

"(3) Where a company has one or more subsidiaries or associate companies, it shall, in addition to financial statements provided under sub-section (2), prepare a consolidated financial statement of the company and of all the subsidiaries and associate companies in the same form and manner as that of its own and in accordance with applicable accounting standards, which shall also be laid before the annual general meeting of the company along with the laying of its financial statement under sub-section (2):

Provided that the company shall also attach along with its financial statement, a separate statement containing the salient features of the financial statement of its subsidiary or subsidiaries and associate company or companies in such form as maybe prescribed:

Provided further that the Central Government may provide for the consolidation of accounts of companies in such manner as may be prescribed."

Therefore, the provisions of applicable Accounting Standards must be read with section 129 of the Companies Act 2013 for the purpose of consolidation of Accounts of Section 8 company with it's holding company.

2. Accounting Standards in India

In India there exists two sets of Accounting Standards viz.:

(1) Accounting Standards (AS), and,

(2) Indian Accounting Standards (Ind AS).

Ind AS are applicable to Listed companies or companies in process of listing in recognized stock exchange or companies having net worth of Rs. 250 crores or more and their subsidiaries, joint ventures or associate companies. And AS are applicable to companies which are not covered by Ind AS.

Applicability of Accounting Standard 21:

Accounting Standards issued by Companies (Accounting Standards) Rules, 2006 under the erstwhile Companies Act, 1956 are applicable to companies not covered IND AS.

AS 21 clearly states, “This Standard should be applied in the preparation and presentation of consolidated financial statements for a group of enterprises under the control of a parent.”

The requirement of consolidation is dependent on the control of the holding company as per the criteria provided in the standard. In the scope of the AS 21 it has been clarified when control does not yield any economic benefit then AS 21 is not intended to apply to such entities. The relevant extract from AS 21 is as under:

“Control exists when the parent owns, directly or indirectly through subsidiary(ies), more than one-half of the voting power of an enterprise. Control also exists when an enterprise controls the composition of the board of directors (in the case of a company) or of the corresponding governing body (in case of an enterprise not being a company) so as to obtain economic benefits from its activities. An enterprise may control the composition of the governing bodies of entities such as gratuity trust, provident fund trust etc. Since the objective of control over such entities is not to obtain economic benefits from their activities, these are not considered for the purpose of preparation of consolidated financial statements.”

This scope of AS 21 as defined by the Institute of Chartered Accountants of India clearly excludes the control over those entities from where economic benefit are not permissible.

Further under para 11 of the AS 21 it is again clarified that the consolidation shall not be necessary if there are permanent restrictions on the subsidiary regarding transfer of profits to the holding company. It has been clarified that the company in such circumstances may disclose the reasons for not consolidating a subsidiary in it's consolidated financial statements.

In the light of the above it is clear that consolidation of accounts shall not be necessary in case of section 8 company. Therefore, there is no requirement of consolidation of accounts of Section 8 companies with Holding company for companies falling under the ambit of Accounting Standards.

Applicability of Ind AS 110:

In contrast to AS 21, Ind AS 110 is based on variable return and not economic benefit. Variable return is much wider concept than economic benefit. While economic benefit only considers profit or loss, Variable return is broad and extends well beyond purely financial gains. It also includes non-financial returns, such as:

- Exposure to losses or expenses arising from providing funds, donations, credit, or liquidity support;
- Intangible benefits like enhanced reputation and image gained through strong governance practices; and
- Synergistic returns available only to specific interest holders — for example, combining operating functions to generate economies of scale or positively influencing market capitalization.

This wide definition captures both risk/exposure elements and unique strategic or reputational advantages that may not be accessible to other parties.

Furthermore, in Query 9, the Expert Advisory Committee (EAC) of the ICAI has examined the matter relating to the consolidation of a Section 8 company with the sponsor company and opined that since the Company exercises control over the Section 8 Company and no specific exemption is provided under Ind AS 110 or the Companies Act, 2013, from the requirement to consolidate a Section 8

Company, the Company is required to consolidate the financial statements of its sponsored Section 8 Company.

The Extract from EAC Opinion is Reproduced as Under:

"With regard to exposure or rights to variable returns from the Section 8 Company, the Committee believes that the Company is exposed to variable returns arising from activities of Section 8 Company for the following key reasons:

(i) In accordance with the requirements of Ind AS 110, returns include not only positive returns, but negative returns also. Under Ind AS 110, variable return is a wide notion that also encompasses non-financial returns, such as, exposure to loss or expenses from providing funds, donation, credit or liquidity support and intangible benefits of reputation and image from good governance practices, synergistic returns that are not available to other interest holders, such as, combining operating functions to achieve economies of scale, impact on market capitalization, etc.

(ii) The Company contributes funds for the CSR purposes to the Section 8 Company and the objective of the Section 8 Company is to implement the CSR activities of the Donor Company (primarily, Sponsor Company). Thus, the Section 8 Company is apparently dependent on and carries out or manages CSR activities on behalf of the Company.

(iii) The Company has an exposure to variable returns in the form of exposure to statutory penalties for non-compliance with the Company's CSR obligations, loss from funding or providing liquidity support for running the CSR entity (Section 8 Company). In addition, there will be intangible/ non-financial returns by way of enhancement or damage to reputation and image including, being a listed company its market capitalization. Therefore, it can be construed that such Section 8 Company engaged in CRS activity of the Company has the ability to affect the Company's returns.

(iv) The Company does the charity with administrative support, and associates itself with the Section 8 Company which also indicates that it has an exposure to variable returns from that company. This is also supported by paragraph B57(c) of Ind AS 110 which states that an investor might use its assets, with the investee's assets, to enhance the value of its other assets. From the Company's perspective, this could include the intangible benefit of being associated with the Section 8 Company and providing it with a support function."

Thus, the EAC opinion recommends that under Ind AS 110, even the accounts of a section 8 company has to be consolidated if it happens to be the subsidiary.

3. Opinion of EAC of ICAI may not be Legally Sustainable

It has to be understood that the holding company of a section 8 company cannot directly or indirectly benefit out of the section 8 company. If the accounts of the section 8 company are consolidated into the holding CSR company then such consolidation may result in increase in the networth, book value, and EPS of the holding company, which will consequently result in indirect benefit to the

shareholders of the holding company. Otherwise also a section 8 company is a legal obligation held on behalf of public at large and any assets held in fiduciary capacity can never be consolidated with the assets of the trustees held in personal capacity.

A holding company of a Section 8 company is not entitled to any share in profits or income of its subsidiary. One of the primary purpose of consolidation is to reflect the correct picture of the value of investment in the subsidiary company. If the value of shares in subsidiary company is reflected through consolidation of the assets and liabilities then it will show an incorrect picture of the net worth of the holding company as it cannot claim anything from the subsidiary.

Further the investment in a section 8 company should be shown as application of income and technically should not remain as investment in the balance sheet. When we consolidate the holding company with a Section 8 company, it will however depict a wrong picture of the wealth of the holding company, as the holding company can never claim any right over the profits of a Section 8 Company. Therefore, the question of consolidation does not arise.

Notes

Notes

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