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# *The International Journal of Not-for-Profit Law*

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*Letter from the Editor* ..... 5

## **RESTRICTIONS ON FOREIGN FUNDING OF CIVIL SOCIETY**

### *Introduction*

International Center for Not-for-Profit Law ..... 6

### *Egypt*

Mohamed ElAgati ..... 9

### *Ethiopia*

Debebe Hailegebriel ..... 18

### *Russia*

Aleksej Bogoroditskii ..... 28

### *Sri Lanka*

Rohan Edrisinha ..... 35

### *Venezuela*

Marcos Carrillo ..... 41

## **ARTICLES**

### *Maintaining Firm Control:*

#### *Recent Developments in Nonprofit Law and Regulation in Vietnam*

Mark Sidel ..... 52

### *The NGO Law:*

#### *Azerbaijan Loses Another Case in the European Court*

Mahammad Guluzade and Natalia Bourjaily ..... 68

### *The Origin of the Species:*

#### *Why Charity Regulations in Canada and England Continue to Reflect Their Origins*

Peter R. Elson ..... 75

*Legal Forms of Civil Society Organizations*

*as a Governance Problem:*

*The Case of Switzerland*

Georg von Schnurbein and Daniela Schönenberg ..... 90

## ***Letter from the Editor***

In this issue, the *International Journal of Not-for-Profit Law* revisits an enduring topic of concern: **restrictions on foreign funding of civil society**. Last fall, we published an overview of the subject.<sup>1</sup> Now, we feature expert reports from the field: Egypt, by **Mohamed ElAgati**; Ethiopia, by **Debebe Hailegebriel**; Russia, by **Aleksej Bogoroditskii**; Sri Lanka, by **Rohan Edrisinha**; and Venezuela, by **Marcos Carrillo**.

This issue also includes a summary of current nonprofit law in Vietnam, by **Mark Sidel**. In another article, **Mahammad Guluzade** and **Natalia Bourjaily** dissect a European Court of Human Rights case challenging Azerbaijan's dissolution of a registered public union. **Peter Elson** argues that one cannot fully understand charity regulations in Canada and England without considering their history. And **Georg von Schnurbein** and **Daniela Schöenberg** examine changes in the governance of civil society organizations in Switzerland.

We thank USAID for its generous support of the articles on restrictions on foreign funding of civil society. We also thank our authors for their incisive and timely articles.

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<sup>1</sup> Rebecca B. Vernon, "Closing the Door on Aid," *International Journal of Not-for-Profit Law* 11(4), August 2009, [http://www.icnl.org/knowledge/ijnl/vol11iss4/special\\_1.htm](http://www.icnl.org/knowledge/ijnl/vol11iss4/special_1.htm).

***Restrictions on Foreign Funding of Civil Society***

## **Introduction**

**International Center for Not-for-Profit Law<sup>1</sup>**

### **Introduction**

The ability to seek and secure financial resources is fundamental to many, if not most, not-for-profit, non-governmental organizations (NGOs). The legal and regulatory framework may facilitate or impede efforts to secure resources. Indeed, the law may place NGOs in a precarious position by imposing barriers to specific resource categories – such as funding from foreign sources. The issue has immediate relevance in many countries. In the past six months alone:

- The President of **Azerbaijan** issued a decree prohibiting NGOs from concluding any transactions with grant funds unless the grant is registered with the Ministry of Justice (December 2009).
- In **China**, in 2010, the State Administration of Foreign Exchange introduced new rules governing the administration of foreign funds donated to or by domestic institutions. Most notably, domestic “enterprises” receiving funds donated from abroad by foreign nonprofits must file documentation with permitted banks to include an application; a copy of the domestic institution’s business license; a notarized donation agreement with the purpose of the donation described; a registration certificate for the overseas organization; and other raw materials that may be required. Much about the new rules and their potential impact remain unclear, with uncertainty surrounding whether or not the new rules apply to non-enterprise social organizations and other NGOs.
- In the first quarter of 2010, the *Bill for the Duty of Disclosure for Someone Supported by a Foreign Political Entity* passed its preliminary first reading in the **Israeli** Knesset. Under the terms of the draft Bill, Israeli NGOs that accept foreign governmental funding and attempt to influence Israeli government policy would be required to disclose all funding from “foreign political entities.” These same Israeli NGOs would lose their tax-exempt status. And board members and staff of non-compliant NGOs would be subject to criminal liability, including imprisonment.
- The **Egyptian** newspaper *Al Dustour* published what is reported to be the leaked text of a Draft Law to replace the existing Law on Associations and Foundations (Law 84 of 2002); the Draft Law requires civil society organizations (CSOs) to obtain permission from the Ministry of Social Solidarity prior to receiving foreign funds or affiliating or

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<sup>1</sup> This paper is made possible with the generous support of the American people through the United States Agency for International Development (USAID). The contents are the responsibility of the authors and do not necessarily reflect the views of USAID or the United States Government.



partnering with foreign organizations, and gives the Ministry apparently unlimited discretion to approve or deny such requests.

- The Ministry of Labor and Social Affairs in **Yemen** has released draft amendments to the Law on Associations and Foundations that would represent a significant degradation in the status of NGOs in that country. Among other things, the proposed law would require NGOs to seek prior approval before receiving funds from abroad, conducting public fundraising at home, or publishing any public media statements.

This new wave of restrictions – including laws either enacted or proposed – adds further momentum to a regulatory backlash against civil society that has been frequently noted by the International Center for Not-for-Profit Law (ICNL), commentators, academics, and practitioners. Countries rely on a panoply of legal tools to prohibit or limit access to certain resources. Examples include restrictions on the ability to engage in economic activities; limits on the opportunity to compete for government grants or contracts; burdensome tax obligations; and restrictions on investment alternatives. But perhaps the most common – and arguably, the most controversial – of resource barriers are restrictions on funding from foreign sources, including foreign governments, multilateral institutions, private foundations, and individuals.

The barriers to foreign funding assume many forms: outright prohibitions (as in Eritrea, where the law restricts the UN and bilateral aid agencies from funding NGOs); the requirement of advance approval (as in Jordan, where foreign funding to associations is subject to the approval of the Council of Ministers); and the mandatory routing of government funding through government banks (as in Uzbekistan, where foreign funding for NGOs must be channeled through government banks, which has reportedly led to the obstruction of at least 80 percent of foreign grants to NGOs). These regulatory approaches are outlined in the *Defending Civil Society* report, published in February 2008.<sup>2</sup>

In the two years since publication of *Defending Civil Society*, we have witnessed ongoing efforts – and sometimes innovative approaches – to constrict access to funding resources, and foreign funding in particular. In **Egypt**, as stated above, a new draft Law would replace the existing Law on Associations and Foundations (Law 84 of 2002), require organizations to obtain permission from the Ministry of Social Solidarity prior to receiving foreign funds or affiliating or partnering with foreign organizations, and give the Ministry apparently unlimited discretion to approve or deny such requests. In **Venezuela**, the draft Law on International Cooperation, which remains pending, would create an international cooperation fund and require compliance with government priorities. In **Sri Lanka**, a draft Bill on NGOs has been prepared, but not released to the public; it may be reasonable to presume, however, that the Bill is likely to empower the state to investigate the financial management and accountability of NGOs that receive foreign funding, as this has been the practice of the Select Committee of Parliament, active since 2006.

In **Russia**, a government list of foreign donors has been substantially reduced, thereby limiting the number of organizations legally able to provide tax-exempt grants to Russian recipients. Perhaps most notorious of all recent regulatory acts is the Proclamation to Provide for the Registration and Regulation of Charities and Societies (CSP), enacted in **Ethiopia** in February 2009. The law is one of the most controversial NGO laws in Africa, and indeed in the world. The Proclamation, among other things, restricts NGOs that receive more than 10 percent

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<sup>2</sup> See ICNL and the World Movement for Democracy Secretariat at the National Endowment for Democracy, *Defending Civil Society*, February 2008, <http://www.icnl.org/knowledge/news/2008/3-21.htm>.

of their financing from foreign sources from working on the advancement of human rights, promoting the rights of children and the disabled, equality of gender, nations and nationalities, promoting good governance and conflict resolution as well as the efficiency of the justice system.

These five countries – Egypt, Ethiopia, Russia, Sri Lanka, and Venezuela – are in the spotlight of this issue of the *International Journal for Not-for-Profit Law*. In countries like Egypt and Ethiopia, organizations which are dependent on foreign funds – especially human rights and opposition groups – may find themselves starved of funds and effectively unable to continue operations. In Sri Lanka and Venezuela, where draft laws currently threaten the sector, concern runs high over the content of the draft law (Sri Lanka) and over whether the law will actually be enacted (Venezuela). In Russia, more encouragingly, there have been recent improvements to the regulatory environment for civil society, but these improvements have not necessarily touched upon foreign funding restrictions.

While each country report describes the legal constraints at issue, the focus of the reports is more squarely on the political context within which the legal constraints have arisen. Prior to the drafting and enactment of laws or regulations imposing such barriers, there are often warning signs, in the form of ominous statements by government officials or politicians or the enactment of restrictive law in other areas, such as the media. The proffered government justifications for the barriers are as diverse as the constraints themselves and can include calls for increased accountability and transparency of CSOs; preventing foreign interference with domestic political processes; protecting national security; combating terrorism and extremism; and the coordination and harmonization of foreign aid and CSOs implementing foreign aid programs. And the civil society responses, unsurprisingly, vary with each country context. These are the questions that this issue of the *International Journal for Not-for-Profit Law* explores.

ICNL is grateful for the ongoing support of USAID and Pact, who made these reports possible under the auspices of the NGO Legal Enabling Environment Program (LEEP). ICNL also expresses its appreciation to the local partners in each country and is pleased to present the results of their efforts. We hope that the country reports will raise awareness and provoke consideration of what has become an ongoing threat to civil society in many countries.



## ***Restrictions on Foreign Funding of Civil Society***

# **Egypt**

**Mohamed ElAgati<sup>1</sup>**

Since the beginning of the 1990s, the issue of foreign funding of civil society organizations (CSOs) has been controversial in the Arab region. Some are supportive; others are critical. Hypocrisy is not uncommon in the debate; for example, some of those who seek to discredit rights-based groups because of their use of foreign funding are the same people who welcome foreign financing in other areas, including sensitive areas such as political parties and the media.

Governments in the Arab world generally do not welcome the existence of rights-based organizations or advocacy-based pressure groups, especially where these CSOs seek to criticize government policies and actions and to raise awareness among the public and international community of government shortcomings or violations of international agreements. Moreover, many of the human rights principles promoted by rights-based CSOs – such as gender equality and freedom of speech and belief – face strong opposition from some active political forces in Arab countries.

The regulatory principles relating to foreign funding are not well established in the Arab world. In examining the issue of foreign funding, questions abound: What is the purpose of the funding? Why do other people (or organizations or governments) finance projects aimed to improve the situation of the Arab citizen? Why do they spend their own funds to support our basic rights?

In considering the issue, it is important to keep in mind the following facts. First, CSOs must be creative in using foreign funds, avoid wasting funds, and work toward greater financial independence in the long run. Second, although Arab governments depend heavily on foreign aid, it is impossible to challenge the hypocrisy of these governments for receiving foreign aid while simultaneously criticizing or burdening the receipt of foreign aid by CSOs. Third, the development and stability of society in the Southern Mediterranean region and the Arab world is directly connected with stability in Europe. Improving the political and economic environment will lower the rate of illegal immigration to the United States and Europe, will assist in countering the danger of extremism, and will open new markets.<sup>2</sup>

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<sup>1</sup> Mohamed ElAgati is Executive Director, Arab Forum for Alternatives, [www.Afaegypt.org](http://www.Afaegypt.org).

This paper is made possible with the generous support of the American people through the United States Agency for International Development (USAID). The contents are the responsibility of the authors and do not necessarily reflect the views of USAID or the United States Government.



<sup>2</sup> Negad Elboraie, *A Manual for Funding*, United Group, Cairo, w.d., p.3.

## **A. Types of Restrictions on Foreign Funding**

### **1) Law No. 84 on NGOs (2002)**

The current governing law, Law No. 84 (on Non-Governmental Organizations or NGOs) (2002), allows NGOs to receive foreign funds, superseding Law No. 32 (on Civil and Voluntary Associations) (1964), which forbade organizations from receiving any foreign funding and prohibited participation in the activities of any foreign organization.<sup>3</sup> Nonetheless, Law No. 84 contains several obstacles and restrictions to foreign funding, at both the legal and practical level. Law No. 84 on NGOs (2002) is predicated on control.<sup>4</sup> It is based on the desire of the Government to keep the issue of foreign funding under its complete control.

Article 17 grants NGOs the right to receive funding from legal entities or individuals, but conditions this right on obtaining the approval of the Ministry of Social Solidarity. The Law grants the Ministry wide discretion in reviewing requests for approval. Moreover, there are no application procedures defined in the Law, and no criteria upon which to guide Ministerial decision-making. The Law does require the Ministry to respond to requests for approval within 60 days, but there is no clear recourse where the Ministry fails to act in a timely fashion, as is often the case.<sup>5</sup> The implementing regulations to Law No. 84 do not clarify these questions.

Significantly, Law No. 84 distinguishes between (1) funds sent from abroad (including from Egyptians living abroad) and identified as “foreign funding,” which requires advance approval, and (2) funds sent from within Egypt (including from foreign organizations registered in Egypt) and identified in the law as “local funding.” The latter category – “local funding” – is not subject to advance approval; instead, NGOs must simply notify the Government of the funding received. In practice, however, the Ministry of Social Solidarity also requires that NGOs apply for approval to receive this category of “local funding” – that is, funding from foreign organizations registered in Egypt.<sup>6</sup> This practice contravenes Article 65 of the Law, which guarantees the right of NGOs to receive funds from foreign agencies that have obtained permission to operate in Egypt.

In addition, the Law also states that an NGO’s budget, if it exceeds 1000 EGP (\$180), must be approved by the Ministry of Social Solidarity, further complicating the procedure for obtaining foreign funding. Because the threshold is so low, virtually all NGOs are subject to this requirement, which was highly criticized by the United Nations Committee on Economic, Social and Cultural Rights in 2002.<sup>7</sup> The rule is even more disturbing when considered alongside the penalty for non-compliance, which includes imprisonment of up to six months and/or a fine of 2000 EGP (Article 76).

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<sup>3</sup> Abdel Mawla Ismail, *Tyranny of the Law, and the Retraction of the Egyptian Civil Society*, Land Center for Human Rights, Cairo, 2002, p.6.

<sup>4</sup> Press release issued by the Cairo Center for Human Rights Studies, 1 May 2009.

<sup>5</sup> Mohamed ELAGATI, *Undermining Standards of Good Governance: Egypt’s NGO Law and Its Impact on the Transparency and Accountability of CSOs*, ICNL, 2006.

<sup>6</sup> Press release, *ibid*

<sup>7</sup> <http://www.awan.com/pages/oped/100612>

## **2) Proposed Amendments to Law No. 84**

After nearly two years of work on three draft laws, the Ministry of Social Solidarity announced that no new law will be produced, but that instead a committee will work on modifying the existing law. The members of the committee were appointed by the Ministry, and include two experts, two Ministry officials, two from the General Union of Associations, and an NGO representative (reportedly a representative of a service delivery NGO formed by the Government, and therefore more truly a GONGO representative).<sup>8</sup> The General Union of Associations is an entity that organizations are free to join and is run by a board of members appointed wholly by the Minister. It is well known that the Union does not include independent organizations.

The Government's declared efforts to revise Law No. 84 come at a time when the Government is suppressing civic organizations and stifling the freedoms of association and speech as well as other forms of social and political activity.<sup>9</sup> Efforts to amend the Law go hand in hand with attempts to abolish all forms of social and political activity. The clear power imbalance between the State and citizens facilitates the Government's attempts to suppress the movements seeking to promote freedom and democracy. A contributing factor is the decline in external pressure exerted on the Arab and Muslim world due to the fight against terrorism. Most tellingly, for the first time since the establishment of human rights organizations in Egypt, the Government closed down two major organizations, the Center of Trade Unions and Workers Services (established in 1992), and the Association of Human Rights Legal Support (established in 1994), based on an amendment made to Article 97 of the Law's implementing regulations issued by the Ministry of Social Solidarity in 2005. According to this amendment, instructions carried out by the Ministry to dissolve any association could take effect immediately.<sup>10</sup>

To date, the Government has refrained from officially announcing the proposed changes to the current Law. Egyptian NGOs and a "freedom of association coalition" have demanded several times that the Ministry of Social Solidarity publish the proposed amendments to the NGO law, but to no avail – a clear violation of the principle of transparency and accountability. Some members of the committee, especially Mr. Abdul-Aziz Hegazi, former Prime Minister and current Chair of the General Union of Associations, have attended seminars and workshops, where suggested modifications to the Law were discussed. Moreover, there have been leaks about the planned restrictions that the Government plans to impose on ability of Egyptian NGOs to raise funds.

In addition, several modifications to the rules governing the General Union of Associations,<sup>11</sup> which are contained in the Law No. 84, have been proposed, which would:

- make membership mandatory for NGOs and automatic upon registration as a legal entity;
- transform the fully appointed board of directors to a board with both appointed and elected members; and

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<sup>8</sup> Interview with NGO activist.

<sup>9</sup> Press release, *ibid*

<sup>10</sup> Essam Eldin Sharaf, *Towards a democratic law to the liberalization of civil work in Egypt*, by the Cairo Center for Human Rights Studies, *Ibid*, p.23.

<sup>11</sup> The Union rules are contained in part 3, chapter 2 of the Law No. 84 on NGOs (2002).

- empower the Union to receive projects from funding agencies and nominate organizations that can receive the funding and implement the projects.

It is not clear if the nomination would be considered obligatory or merely a suggestion that the donor agency could ignore. Practical experience indicates, however, that even if the nomination were not obligatory, it would be difficult to ignore. This policy approach would place the needs of funding organizations over and above those of general society since all projects would in this case originate from the donors themselves. This also runs counter to the accepted wisdom that organizations should apply for projects based on their own principles and agendas. Moreover, this approach would further jeopardize the independence of civil society. Although these amendments have not been formally announced, they reveal the Government's intentions to restrict the limited freedoms now available to CSOs.

### **3) Implementation Practices**

Barriers to foreign funding arise not only from legal requirements, but also from regressive implementation practices.

A significant extra-legal implementation practice relates to the involvement of security services in the foreign funding determinations. The Law clearly does not require the approval of the security services. NGO representatives, however, report that the Ministry of Social Solidarity does not approve foreign funding applications without their approval. Some also added that the process often involves coordination between the chiefs of security departments in different governorates. Many believe that the approval of security departments is a green light for the Ministry to officially approve the funding. Reportedly, reservations made by security departments in some ministries make obtaining the approval of the security department in the Ministry of Social Solidarity impossible.<sup>12</sup> One NGO representative commented as follows:

The administrative authority sends it [the request for approval of foreign funding] to the Directorate of Social Solidarity, Financing Section to investigate the foundation requesting the funding. It also writes a report for the Ministry. The Ministry sends the report in turn to the Security Department in the Ministry to obtain its approval (National Security Department - State Security) and after 60 days – that's the law – a decision is made, although usually months pass before securing approval. Of course these practices are not based on the law.<sup>13</sup>

A second key area of manipulation is the time period for reviewing and deciding on foreign funding approval requests. As previously mentioned, there is no recourse for NGOs whose requests have not been answered within the 60-day time period. In practice, the Ministry may delay issuing a response for up to one year. Such delays not only impact on the implementation of a specific project, but may also threaten the NGO's existence, where it undermines the NGO's ability to pay wages and fulfill its obligations.

NGO representatives have also noted that the delays in securing approval for funding can render project implementation untimely and inappropriate, and even lead to the termination of a project. For example, an NGO was scheduled to launch a project in January 2009, but only secured approval at the end of July, seven months after the beginning of the implementation

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<sup>12</sup> Essam Eldin Sharaf, *ibid*, p.23.

<sup>13</sup> Quotation from interviews with CSOs.

period. Other project contracts signed in May 2009 were approved only at the end of January 2010, more than seven months after the beginning of the implementation period.<sup>14</sup>

A third implementation barrier relates to inspections. The Law vests the Ministry with full authority over financial auditing. Based on this authority, the Ministry has increased the number of inspection committees; these committees spend long periods of time reviewing the records of the NGO, especially in the governorates. For example, in Al Menia governorate, an NGO was subject to a very detailed inspection for six months, through various overlapping committees. In addition, the Law on Local Governance gives authority to governors to conduct inspections of NGOs, which increases the burden on NGOs, and hinders NGOs in conducting their work efficiently and implementing their programs effectively. As one NGO noted:

For example, we launched the campaign of "freedom of association." We used to conduct seminars and organize protests in front of the Ministry of Social Solidarity; then afterwards, or even during the protests, we received a phone call, informing us of an inspection by the Ministry and the Central Auditing Organization (CAO), though the CAO is not authorized to do so. Furthermore, there was security interference and threats of suspending the activities of the campaign.<sup>15</sup>

Similarly, frequent government requests for documents, data, and reports may also amount to a constraint against NGOs. The practice can overwhelm the NGO and drain its resources every time it undergoes the process of applying for foreign funds. The requested documentation includes items that are not supported by the law. According to one NGO:

We face many problems as a result of the multiple bodies overseeing foreign funding. As an organization, our activities are known and specific. I should not need to introduce the organization every time I apply for funding to the Ministry of Social Solidarity. Moreover, there are multiple steps to the process; every time I am compelled to secure new approval from the security department, which takes so much time. A few years ago, during our participation in the Coalition of NGOs organized to change the previous NGO Law, I began to face many problems from the Ministry of Social Solidarity, which rejected a number of applications submitted to get approval for funding.<sup>16</sup>

#### **4) The Impact of Foreign Funding Restrictions**

In recent years, with the increase in the number of CSOs and the range of their activities, the issue of funding has emerged as one of the most controversial issues within civil society. The limited possibilities for local funding, whether from governmental or private sources, have forced human rights organizations in Egypt to seek foreign funding. The receipt of foreign funding, however, has subjected CSOs to accusations from the Government and from independent media agencies that the funding was granted in order to implement hidden foreign agendas. As a result, Egyptian CSOs are facing serious challenges relating to financial sustainability and the continuity of their activities.<sup>17</sup>

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<sup>14</sup> Quotation from interviews with donor organizations.

<sup>15</sup> Quotation from interviews with CSOs.

<sup>16</sup> Quotation from interviews with CSOs.

<sup>17</sup> Abdallah Kahalil & Vivian Mourad, *Human Rights Organizations and Society Development*, paper presented to the National Council for Human Rights, Cairo, 2007, p.1.

To provide illustrative examples of how foreign funding restrictions and financial auditing can be used to strike at the very existence of human rights CSOs in Egypt, here are three brief case studies:

- Egyptian Human Rights Organization

The head of the organization, Mr. Hafez Abu Saada, a human rights defender, was detained in December 1998 when the organization published a report on human rights violations against a minority group in “Al kosheh” village, where a Coptic Christian majority exists. He was released on bail after six days, following efforts by human rights organizations to raise awareness of the arrest both inside and outside Egypt. The charges against him were initially related to receiving unauthorized funds and the publication of false information. On February 13, 2000, the Attorney General’s Office announced that the case will be transferred to the Supreme Court, according to the Military Decree No. 4 (1992).<sup>18</sup> The case was later dropped due to lack of evidence. It seems that the purpose was not prosecution, but rather to undermine the reputation of the organization and civil rights associations in general.

- Ibn Khaldoun Center

Mr. Saad Al Deen Ibrahim is the President of the Center and a human rights activist. He was arrested and accused of receiving funds without government approval, the publication of false information, and obtaining money by fraud. He was sentenced to seven years in prison. Dr. Ibrahim was taken from his home in Cairo on June 30, 2000, and placed under detention in the Torrah Farm Detention Facility, until he was released on August 10, 2002. The charges that Dr. Ibrahim faced related to projects funded by the European Union in Egypt; his arrest and detention therefore contradict the agreement signed by the Egyptian Government in February 1998 as a part of the European-Mediterranean partnership. According to Article 7 of the MEDA<sup>19</sup> agreement, signed by the Egyptian Government, the European Commission, and the European Investment Bank: “The beneficiaries of programs financed by the European Commission and the European Investment Bank could be: private associations, organizations, corporations, agencies, charity agencies and non-governmental organizations.” An Egyptian court held that since the contracts between Ibn Khaldoun Center and the European Union are civil contracts and not grants, they do not require official approval. Moreover, the semi-annual financial reports related to the project did not give any reason for suspicion.<sup>20</sup>

- Egyptian Center for Legal Aid

The Legal Aid Center submitted a request to receive foreign funds but did not receive a reply from the Ministry within the time limit required by law. The board of the Center considered the absence of a reply to constitute acceptance and began implementing the project. On September 24, 2007, the Cairo Governor issued a decision terminating the Center, as explained in the “Al Khbar” newspaper (owned by the Government) through an article entitled “Closing down the office of legal human rights association for receiving foreign funds.” The

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<sup>18</sup> <http://www.amnesty.org.ru/library/Index/ARAMDE120162001?open&of=ARA-EGY>

<sup>19</sup> The MEDA program is the principal financial instrument of the European Union for the implementation of the Euro-Mediterranean Partnership.

<sup>20</sup> <http://www.amnesty.org.ru/library/Index/ARAMDE120162001?open&of=ARA-EGY>

news story explained that termination resulted from not obtaining permission from the Minister of Social Solidarity to receive foreign funds, and for other logistical discrepancies. The Center issued a press release refuting these accusations. After a hearing, the administrative court declared on October 26, 2008, that the decision taken by the authorities was unjustified, and that there was no evidence for the finding of any violations, and that the decision to terminate the organization was taken without any legal or factual basis.<sup>21</sup>

## **B. Justifications**

### **1) Declared Justifications**

The Egyptian Government promotes false information regarding the funding received by civil society. According to the Government, civil society groups exist to harm national security, with the financing of millions of dollars from European and American institutions.<sup>22</sup> This accusation greatly influenced the votes of Members of Parliament in favor of new legislation imposing more restrictions on NGOs, especially relating to the acceptance of foreign funding or joining networks and international institutions.<sup>23</sup> Indeed, Parliamentary discussion of the draft legislation was based on the principle that foreign funding has negative effects on national security.

The Egyptian Security Department views the NGO sector as a threat to be dealt with rather than as a partner to be supported. From the Security Department perspective, NGOs working in the rights field are a threat to national security, NGOs active in the economic and social fields are a threat to social stability and cohesion, and those operating in the cultural field represent a threat to public morality; confronting these dangers is therefore critical to preserve and promote national security.

Most recently, and perhaps most disturbingly, Mr. Abdel-Aziz El-Hegazi, former Prime Minister and current Chair of the General Union of Associations, accused CSOs – and particularly those working in the field of human rights – of threatening national security and fostering increased corruption. He stated that he does not believe that human rights activities have any value, and demanded that security services tighten their grip over the NGO sector. NGOs signed a statement expressing strong disapproval of these statements, especially as they came from the lips of the Chairman of the General Union of Associations, a body which is currently leading efforts to draft expected amendments to the Law on NGOs. Moreover, the statements come alongside new leaks about the planned restrictions that the Government plans to impose on the work and ability to raise funds of Egyptian NGOs.

### **2) Underlying Motivations**

The NGO sector, through its involvement in all manner of social, economic, and cultural rights issues, upsets the powers that benefit from the status quo. The oppression of civil society, especially private organizations and institutions, is an integral part of the state system, which includes the oppression of political parties, unions, and social movements. Just as the system

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<sup>21</sup> <http://www.ahrla.org>

<sup>22</sup> Despite the propaganda surrounding foreign funding, the Minister of Social Solidarity urged the U.S. Ambassador and the Head of the European Commission delegation in Egypt to increase their funding!

<sup>23</sup> Negad Elboraei, *After 25 years did the foreign funding help in the democratic change*, United Group, 2004, p.2.

restricts pluralism in the political party domain, it has restricted NGOs. Restrictions that include advance governmental approval for activities and financing tend to reveal the bureaucracy and security concerns dominating the mentality of legislators.<sup>24</sup>

In the view of some, the Egyptian Government is seeking to reduce the role of NGOs in Egypt and to paralyze the human rights movements. Some NGOs have a well-developed structure inside and outside Cairo and the different governorates, and are able to engage the people in addressing their problems. Such activity is suspect in the eyes of the Government and a reason to curb the role and work of these organizations.<sup>25</sup>

### **C. Responses and Lessons Learned**

*Navigating the existing legal framework.* NGOs and private organizations seek to overcome the legal obstacles and constraints by various means. One option is to avoid registering as an NGO under Law No. 84 (2002) with the Ministry of Social Solidarity and instead to register as a branch of a foreign institution, as did the Cairo Center for Human Rights Studies, or as a law firm or company, as did the Hisham Mubarak Law Center. A second option is to conclude contracts for projects in the form of civil service contracts, under the supervision of the Ministry of Investment and Taxation Agency, as is the practice for the Ibn Khaldoun Center. Third, where organizations are registered as NGOs, they often scrutinize the names of projects and expense items in their records to mask anything that may indicate involvement in pressure campaigns or anything else that may give rise to governmental concern. Most NGOs also seek to maintain positive links with governmental contacts and involve them personally in some of the NGO's activities.

In addition, NGOs have also sought foreign assistance to overcome the conflicts with administrative bodies. Funding agencies sometimes become involved in the matter whether they want to or not, especially in cases involving the seizure of funds they have released or when they are forced to defend their reputation.<sup>26</sup>

*Improving the legal framework.* A key strategic response must be to develop and improve the legal framework, so that it enables political participation, the devolution of power, and the creation of a secure environment for the promotion of democracy, freedom of association, freedom of expression, etc. In the absence of such a legal framework, it will be difficult to achieve positive changes to the NGO Law in particular or for civil society more broadly.

In part, the goal of legislative reform must be to motivate the private sector to support and fund independent civil society directly. The need to request approval for foreign funding must be replaced with a requirement simply to provide reports on funding. Mandatory public disclosure of funding information (making budgetary information available on websites or in official newspapers) could also strengthen public trust.<sup>27</sup>

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<sup>24</sup> Editor: Medhat ELZAHED, *Future of Civil Society in Egypt*, Development Support Center and Elfostat Center, Cairo, 2003, p.58

<sup>25</sup> Quotation from Interviews with CSOs.

<sup>26</sup> Mohamed ELAGATI, *ibid.*

<sup>27</sup> Mohamed ELAGATI, *ibid.*



*NGO Transparency.* NGOs should seek to comply with high standards of transparency and accountability. It is their duty to declare resources and exchanged items and make the information available to all.

*The Role of Funding Institutions.* The role of funding institutions must be to support local CSOs in their struggle and to deal realistically with the Government, while refraining from imposing further obstacles against CSOs, such as requiring complex accounting systems or registration under repressive laws.

Funding institutions should not bow to pressure from the State. Interference from all parties should be resisted. In other words, funding institutions should remain independent and certainly not collude with “governmental nongovernmental organizations” established as competitors to independent civil society.

Donors should recognize the importance of an enabling legal framework, which should not only guarantee fundamental freedoms, but also build the basis for greater trust between the sectors and meaningful NGO/government cooperation in addressing development needs. In addition, donors should be cognizant of the capacity weaknesses within governmental departments and ministries, and prioritize programs that seek to increase the capacity of governmental staff to deal effectively with NGOs.<sup>28</sup>

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<sup>28</sup> Quotation from interviews with donor organizations.

## ***Restrictions on Foreign Funding of Civil Society***

# **Ethiopia**

**Debebe Hailegebriel<sup>1</sup>**

### **A. Types of Restrictions on Foreign Funding**

The newly enacted Charities and Societies Proclamation (CSP) has a unique legislative history as a subject of fierce debate and contention between the Ethiopian Government, on the one hand, and Ethiopian civil society and other interested parties, on the other hand. The controversies surrounding the legislation are multi-dimensional and relate to various aspects of the Proclamation. The focal point, however, of much of the controversy has been the restrictions on foreign funding for civil society organizations (CSOs) in Ethiopia.

#### **1. The Nature of the Legal Restriction**

The Proclamation contains restrictions on foreign funding that are fundamental to the definition, identity, and operational mandate of CSOs. Based on this standard, the Proclamation recognizes three forms or types of CSOs, which may be established as either charities or societies. These are “Ethiopian Charities or Societies,” “Ethiopian Resident Charities or Societies,” and “Foreign Charities or Societies.” The legal definitions of these categories are provided under Article 2 of the CSP as follows:<sup>2</sup>

1. Article 2(2): “Ethiopian Charities” or “Ethiopian Societies” shall mean those charities or societies that are formed under the laws of Ethiopia; all of whose members are Ethiopians; generate income from Ethiopia; and are wholly controlled by Ethiopians. Here it should be noted that the law includes an exception to the general rule concerning the generation of income from within Ethiopia. Accordingly, organizations can still be considered “Ethiopian Charities or Ethiopian Societies” “if they **use** not more than ten percent of their **funds** which is received from foreign sources”<sup>3</sup> (emphasis added). The 10% restriction relates to the use of foreign funds and not to the amount of foreign income the organization is receiving.
2. Article 2(3): “Ethiopian Resident Charities” or “Ethiopian Resident Societies” shall mean those charities or societies that are formed under the laws of Ethiopia, and that consist of

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<sup>1</sup> This paper is made possible with the generous support of the American people through the United States Agency for International Development (USAID). The contents are the responsibility of the authors and do not necessarily reflect the views of USAID or the United States Government.



<sup>2</sup> See Article 14 (2),(3) and (4) of the Charities and Societies Proclamation (CSP) No. 621/2009.

<sup>3</sup> "Income from Foreign source" means “a donation or delivery or transfer made from foreign source of any article, currency or security. Foreign sources include the government agency or company of any foreign country; international agency or any person in a foreign country”. See Article 2(15) of the CSP.

members who reside in Ethiopia, and that **receive more than 10% of their funding from foreign sources.**

3. Article 2(4): “Foreign Charities” shall mean those charities that are formed under the laws of foreign countries or which consist of members who are foreign nationals or are controlled by foreign nationals or **receive funds from foreign country sources.**<sup>4</sup> As one can observe, the criteria in this provision are outlined in the alternative, using the word “or” to indicate that if one of the distinguishing elements applies, then the organization is considered a “Foreign Charity.” Accordingly, an organization receiving funds from a foreign source could be classified as foreign charity even if none of the other criteria apply. This raises the question of the precise contours between “Ethiopian Resident Charities” and “Foreign Charities.” It is worth noting that the classification of “Ethiopian Resident Charities” and “Ethiopian Resident Societies” was introduced in the draft CSP as a compromise to labeling Ethiopians as “Foreign.”

The foregoing provisions indicate the significance and centrality of funding to the classification of charities and societies. These provisions make clear that the corporate citizenship of CSOs is not determined only by the law under which they are incorporated or the national composition or citizenship of their members. Rather, the decisive factor for entitlement to, or deprivation of, Ethiopian corporate citizenship is also the actual or anticipated source of funding. In other words, for a CSO to acquire Ethiopian corporate citizenship, it is not sufficient to be incorporated under Ethiopian law; in addition, the amount of funding received by the CSO from foreign sources must not be more than 10% of its overall funding. If it acquires more than 10% of its funds from foreign sources, then it is denied Ethiopian corporate citizenship.

The definitional distinction between Ethiopian Charities or Societies and Ethiopian Resident Charities or Societies acquires heightened significance, since it serves as the basis for eligibility for involvement in human rights and governance issues. As stated above, the CSP determines the nationality of a given CSO based on its source of income, and at the same time makes Ethiopian nationality (or corporate citizenship) a requirement for engaging in governance and advocacy activities.<sup>5</sup> Organizations that receive more than 10% of their income from foreign sources are effectively excluded from working on the advancement of human rights, promoting the rights of children and the disabled, gender equality, nations and nationalities, good governance and conflict resolution, as well as the efficiency of the justice system.

## **2. Early warning signals for the legal restriction**

The enactment of legislation incorporating foreign funding restrictions as well as other restrictive provisions has been under consideration since 2003. Especially after the conflict between the prominent human rights CSOs and the Government on matters related to the May 2005 National Election, such a legislative initiative from the Government seemed imminent. However, the Ministry of Justice (MOJ), in its official explanatory document of the Draft

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<sup>4</sup> Please note that the law does not provide for the establishment of “Foreign Societies.”

<sup>5</sup> See Article 14 (5) of the CSP which reads, “Those who can take part in activities that fall under Sub-Article 2(j) the advancement of human and democratic rights, (k) the promotion of equality of nations, nationalities and peoples and that of gender and religion, (l) the promotion of the rights of the disabled and children’s rights, (m) the promotion of conflict resolution and reconciliation and (n) the promotion of the efficiency of the justice and law enforcement services shall be only Ethiopian Charities and Societies.”

Proclamation, provided a depoliticized explanation about the need for the new legislation. According to the MOJ, the initiative for drafting the new Proclamation sprang from the Business Process Reengineering (BPR) study, which was geared toward overhauling the operational structure and procedures of the Ministry.

Immediately after the 2005 National Election, the tone of the Government toward CSOs changed. The Government began denying not only the role and contribution of CSOs in the economic and democratic process but also the foundational principles of the sector. The Prime Minister and other government officials repeatedly asserted that only “mass-based organizations” such as women, youth, trade unions, etc. can play roles both in the democratization and economic development of the country. On the contrary, government officials blamed NGOs for being “rent seekers” and for contributing to the economic crisis of Africa. The ruling party, the Ethiopian People Revolutionary Democratic Front (EPRDF), has clearly indicated its hostile position towards NGOs since the 2005 National Election. In its policy document, the EPRDF questions the role of NGOs in the development process, and describes NGOs as patronage networks distributing “policy rents,” receiving big salaries and benefits without bringing concrete results, spending 60% of their budgets on administrative matters, strengthening a rent-seeking political economy, and thereby negatively affecting the development of the country.<sup>6</sup>

According to EPRDF policy document, which can also be considered a government policy document:

NGOs are not organizations established by citizens to protect their rights. These organizations are rather established by individuals mainly for personal benefit, accountable to, and advancing the interests of foreign agencies. Their leaders are not accountable to the staff of the organizations and the beneficiaries. As result, they cannot have a democratic nature and role.... Therefore, the government has to confront the “rent seeking” nature of NGOs, for example, by considering those organizations receiving 15% of their income from foreign sources as foreign organizations and denying them recognition as a means of expression of freedom of association as well as democratic forums.

### **3. Impact of the Legal Restrictions**

The restriction on foreign funding is already having an effect on both the operation and existence of CSOs, and particularly advocacy-based CSOs. Donors have become hesitant to engage in long-term project agreements because of the uncertainty and restrictions of the CSP. Consequently, some CSOs have already been obliged to reduce the number of their staff and/or close branch offices.<sup>7</sup>

The restrictions on access to foreign funding and operational areas will likely have an unprecedented effect not only on the development of CSOs but also on the democratization process. As things now stand, foreign funding is the only source of funding for almost all CSOs

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<sup>6</sup> Revolutionary Democracy and Struggle for the Development of Democratic Rule, EPRDF, 2006.

<sup>7</sup> It has been reported that Ethiopian Human Rights Council (EHRCO), Ethiopian Women Lawyers Association (EWLA), and Action Aid and Christian Relief Development Association (CRDA) are some of the organizations engaged in lay offs and closing branch offices. EHRCO has decided to close nine branch offices and to confine its activities at the head office and three branches. See also “Addis Neger,” weekly Amharic newspaper, October 24, 2<sup>nd</sup> year, No. 105.

in Ethiopia. Due to the poverty of the nation, there is no substantial indigenous funding that can compensate for the loss of resources engendered by the restrictions. Consequently, the restrictions will likely create a severe financial crisis for CSOs, which might result in their being crippled. Alternatively, human rights CSOs may opt to abandon their activity in such areas and turn to relief provision and related non-sensitive areas of work.

Moreover, the role of CSOs as watchdogs promoting human rights and good governance will be affected by this legislation. As stated repeatedly, generating over 90% of their budget from local sources will be a challenge for local CSOs and, hence, their survival will be at risk. The law heavily curtails the involvement of CSOs in activities that are key to empowerment and sustainable development. In other words, the CSP discourages the rights-based approach to development, which is essential to holding government accountable for its actions.

This legislation will also affect the contribution of development partners who seek to support the country's development by working with both Government and CSOs. Consequently, the CSP may reduce (temporarily or permanently) foreign aid, particularly foreign aid channeled through NGOs. The CSP also contradicts international instruments such as the Paris Declaration, which calls for a rights-based approach to development and the participation of CSOs in the formulation and assessment of national development strategies.<sup>8</sup>

Recently, 42 community-based organizations (CBOs) operating in the Southern Nations, Nationalities and Peoples' Region (SNNPR) were shut down and banks instructed to freeze their assets. The official reasons given for such actions by the Government include the engagement of the organizations in promoting harmful traditional practices, mobilizing communities against the use of fertilizers, setting up a parallel government, and non-transparent accounting practices. Although all of these organizations were registered with the Regional Government of SNNPR and not with the Federal Government, there is an argument that these organizations fall under the jurisdiction of the new CSP because of their reliance on foreign sources of income.<sup>9</sup> According to Article 3(1)(b) of the CSP, organizations established as Ethiopian Resident Charities or Societies, and therefore receiving more than 10% of their income from foreign sources, are subject to the CSP.

## **B. Justifications**

### **1. Declared Justifications**

The underlying ideological justification for the restriction on foreign funding of CSOs emanates from the Ruling Party's position on promoting Revolutionary/Developmental Democracy in all aspects of public life. The Party (EPRDF) considers the free flow of foreign funding to CSOs as a means for perpetuating parasitism and rent-seeking, which the Party considers as the most prevalent evil in Ethiopian public life. The Party further expounds that the fact that a CSO is wholly established and managed by Ethiopians is not enough to make it an Ethiopian CSO unless it also generates its funding from local sources. A CSO receiving a

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<sup>8</sup> See Paragraph 14 and 47 of the Paris Declaration on Aid Effectiveness, Ownership, Harmonization, Alignment, Results and Mutual Accountability, High Level Forum, February 28 to March 2, 2005.

<sup>9</sup> Please recall that organizations that are receiving more than 10% of their income from outside are considered as Ethiopian Residents' Charities or Societies. All of them were funded by the Christenson Fund and under the management of the Fund's Program Officer for the African Rift Valley Region.

substantial portion of funding from foreign sources could be an instrument for the illicit advancement of the interests of foreign powers. This means that the sources of funding of a CSO should determine its identity and legal standing in the Ethiopian legal system. Therefore, the EPRDF considers it appropriate to impose restrictions on the level of foreign funding (i.e., a maximum of 10%) on those CSOs that engage in such sensitive areas as human rights, good governance, gender equality, children's rights, the rights of the disabled, conflict resolution, and the efficiency of the justice sector.

The official justification is also related to a unique understating of the very nature of the constitutional right to freedom of association. The official position is that the right to freedom of association is a democratic/political right and not a human right. Consequently, it is officially propounded that since this right is not a human right, it does not belong to all human beings. Rather it is said to belong to citizens alone; as such, the enjoyment of this right is said to be limited only to citizens. The logical result of this position is that since freedom of association is a right that exclusively pertains to citizens, foreigners cannot exercise it either directly by establishing a CSO, or indirectly by funding local CSOs. The overall tone of the justification is that these restrictions are necessary to ensure that those CSOs involved in the designated sensitive areas truly represent national interests and are not vulnerable to manipulation by foreign elements through foreign funding.

The Government has expressed the rationale for the enactment of the CSP in the law itself and other relevant documents. Accordingly, we may highlight the following stated objectives:<sup>10</sup>

- to ensure the realization of **citizens' right** to association enshrined in the Constitution of the Federal Democratic Republic of Ethiopia;
- to aid and facilitate the role of charities and societies in the overall development of Ethiopian people;
- to provide varieties of measures to be taken against CSOs in case of fault;
- to ensure the accountability, transparency, and consistency of CSOs to the public;
- to provide the legal basis for the relationship between CSOs and sector administrators; and
- to determine the amount of money CSOs spend for administrative purposes and project activities (core objectives).

## **2. Underlying Motivations**

The most revealing indicator underlying the enactment of the CSP is the generally skeptical attitude adopted by the State regarding the role and participation of CSOs in the national political space. The Government displays a hostile attitude towards “rights watchdogs” and human rights organizations, which it brands as funnels for civil and political discontent and mouthpieces of the Opposition. In the context of political party debates and rights-based CSO activities during the May 2005 election, the Government grew more inimical toward CSOs.

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<sup>10</sup> For objectives mentioned under a and b, please see the Preamble of the PCS whereas the rest are taken from the Minutes of the Legal and Administrative Affairs of the House of Peoples' Representatives of Ethiopia, December 24, 2008.

Some CSOs have also been active in monitoring and exposing human rights violations. Moreover, the Government has shown a tendency to consider the advocacy-based NGOs as petty fault-finders who capitalize on the weaknesses and mistakes of the Government to promote their own interests. In line with this perception, the Government holds that the main cause for such “belligerence” on the part of the CSOs is the financial support received from abroad.

In addition, the Government accuses some of the human rights CSOs and their leaders of abandoning their impartiality and aligning themselves with the Opposition. Consequently the Government resorts to vindictive measures toward the CSO leaders, whom it has labeled as “angry elites” in league with Opposition leaders. The restrictive legislation also seems to be a manifestation of these vindictive measures.

### **3. Evaluation of the Justification**

The central point underpinning the official arguments of the Government appears to be an attitude of aversion towards CSOs as alternative forms of social organization and political participation. In claiming a share of the nation’s political space, the existence of such structures may be perceived as threatening to the Government’s hold over the political space. The Government seems to consider itself as the sole genuine actor in public life. The argument is flawed in that it is based on the wrong perception of CSOs and their role in society; the Government should consider them as partners and should support their development.

The second aspect of the Government’s arguments appears to be xenophobic hostility toward the involvement of foreigners in matters related to human rights and governance. The Government emphatically asserts that foreigners cannot exercise the right to freedom of association in Ethiopia. The fact that the right to freedom of association is found in the section of the Ethiopian Constitution dealing with democratic rights cannot by itself deprive this right of its status as a human right. Such fundamental human rights as child rights, women’s rights, and the right to property are also found in this section. It would be outrageous to argue that these rights are not human rights because they are found in a certain section of the Constitution. Moreover, the restriction on the involvement of the international community in human rights and related matters in Ethiopia by providing funds for local human rights CSOs contradicts Ethiopia’s obligations vis-à-vis the global concern for human rights.

### **4. Legal Grounds to Challenge the Justifications**

As stated above, government justifications for restricting the rights of CSOs are more political than legal. The argument that freedom of association is a “democratic right” and not a human right to be respected to everyone<sup>11</sup> runs counter to Article 31 of the Ethiopian Constitution, which guarantees freedom of association for **everyone** regardless of their nationality or source of income.<sup>12</sup> Further, the same provision entitles everyone to associate for **any cause or purpose**. Thus, the CSP restricts the rights of individuals to engage in advocacy activities based on their source of income, in violation of this constitutional guarantee. The Constitution is the supreme law of the land and, therefore any law, customary practice, or

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<sup>11</sup> The Explanatory Note of the Draft Charities and Societies Proclamation, Ministry of Justice, 2008, p. 11.

<sup>12</sup> Article 31 of the FDRE Constitution reads, “Every person has the right to freedom of association for any cause or purpose. Organizations formed, in violation of appropriate laws, or to illegally subvert the constitutional order, or which promote such activities are prohibited.”

decision of an organ of state or a public official that contravenes the Constitution shall be of no effect.<sup>13</sup>

Unlike most countries, the power of interpreting the Constitution is given to a political body called the House of Federation.<sup>14</sup> This House is professionally supported by the Council of Constitutional Inquiry, which is empowered to receive applications “where any Federal State law is contested as being unconstitutional and such a dispute is submitted to it by any court or interested party. In such cases, the Council shall consider the matter and submit it to the House of the Federation for a final decision.”<sup>15</sup> Therefore, one option is challenging the constitutionality of the CSP in these *fora* at the domestic level.

It should also be noted that Ethiopia is party to various international and regional human rights instruments, such as the International Covenant on Civil and Political Rights and the African Charter on Human and Peoples Rights. Taking the matter to these international and regional *fora* is another option.

### **C. Responses and Lessons Learned**

#### **(1) Responses**

##### **(a) Participation in the Drafting Process**

The draft Proclamation was presented for discussion with civil society organizations as well as other interested bodies. A number of consultative meetings were held with representatives of CSOs and concerned government officials. This included two roundtable discussions between the Prime Minister and CSO representatives, and several other meetings with the Ministry of Justice (MOJ). Although some provisions in the draft Proclamation were changed as a result of this dialogue, it is difficult to say that civil society input had any meaningful impact on the final shape of the Proclamation. Most of the revisions were more technical and cosmetic than substantive. Government officials remained stubborn and resistant to genuine and constructive dialogue.

##### **(b) Collective Responses of CSOs**

The CSOs responded to this legislation in a coordinated manner by establishing a special Taskforce that pursued continuous dialogue with the Government. Members of the Taskforce are drawn from various segments of civil society: development, advocacy, religious, and networks. The Taskforce prepared commentaries on the different draft versions of the law and submitted

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<sup>13</sup> See Article 9 of the FDRE Constitution.

<sup>14</sup> The Federal Government has two houses: the House of Peoples' Representatives and the House of the Federation. The House of Peoples' Representatives is the highest authority of the Federal Government which is made accountable to the people. Members of the House of Peoples' Representatives are elected by the people for a term of five years. On the other hand, the House of the Federation is composed of representatives of Nations, Nationalities, and Peoples. Each Nation, Nationality, and People is represented in the House of the Federation by at least one member who is elected by the State Councils (Regional Governments). This House is given the power, among others, to interpret the Constitution, decides on the rights self-determination of including secession, provide solutions for conflicts among the different regions, and determine division of revenue between the Federal Government and Regional States and subsidies that the Federal Government may provide to the States. Looking at the composition of its members and the procedure by which they are elected, many people consider this House as a political body and question its independence in interpreting constitutional issues.

<sup>15</sup> Council of Constitutional Inquiry Proclamation No 250/2000, Article 6(2).



these to the Government. It organized forums wherein government officials and experts as well as CSO representatives came together and discussed the draft legislation. It also served as means of communication between the international community and CSOs. After the adoption of the Proclamation, the Taskforce has continued its activities with a revised mandate.

### **(c) The Response of the International Community**

The international community played a significant role in exerting influence on the Ethiopian Government. High delegations from countries including the United States and the United Kingdom made frequent visits to Ethiopia to express their concern over the legislation, and held high-level meetings with various officials, including the Prime Minister and Ministry of Justice. The CSO legislation offered one of the rare instances in Ethiopia when the international community came together with a unified voice and expressed its concern.

Many doubt, however, whether these efforts made any impact on the final outcome of the Proclamation. Moreover, it appeared that some members of the international community preferred an approach of “wait and see” to pressuring the Government during the drafting process. The concern of the international community was countered by appeals to “non-interference” in domestic affairs by the Ethiopian Government: “We need your money but if you try meddling in our internal affairs, you can take your money away.” In addition, the Government challenged members of the international community by claiming that some CSP provisions were taken from other laws, such as the UK Charities Act.

Certain international organizations, such as the International Center for Not-for-Profit Law, Human Rights Watch, and CIVICUS, played crucial roles in providing comments and position statements on the draft CSP. These organizations played a significant role in providing technical support and attracting the attention of other actors towards the challenges posed by the draft law.

After the adoption of the CSP, the donors group<sup>16</sup> designed a strategy called “POST PACKAGE STRATEGY”<sup>17</sup> which has two major components: Law Enforcement Monitoring System and CSO Adaptation Facility. Under the first component, the plan is to monitor the application of the law, challenges CSOs may encounter, and the impact of the law on donor assistance and citizens’ rights. To this end, a monitoring tool will be developed, and the findings of the monitoring exercise will be used to support the advocacy and policy dialogue with the Government.<sup>18</sup> DFID has taken the lead role in implementing the Monitoring Component. Although the implementation of this activity was planned to begin in October, and preparatory work has been completed, it has proved challenging to secure the permission of the Government. Reportedly, the Government has now accepted the project in principle, but the Ministry of Finance and Economic Development (MoFED) is still expected to write a formal letter to the Charity and Society Agency (CSA) and the donor community.

The second component includes four strategies:

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<sup>16</sup> Among the donors group the following are actively participating in the process of supporting the CSOs and expressing their concern on the legislation; USAID, DFID, CIDA (ECCO), Irish Aid, SIDA, etc.

<sup>17</sup> The Strategy called as Post Package Strategy just to indicate the continuation of the support of the international community even after the adoption of the CSP.

<sup>18</sup> Interview with Mr. Shimelis Assefa; Governance Officer, CIDA and member of the Civil Society Support Group of Donor Assistance Group. June 27, 2009, Addis Ababa.

1. CSO Adaptation Facility
  - Help CSOs to adapt to the legal environment
  - Raise awareness of CSOs on the content and nature of the law
2. Provide technical assistance to CSOs
  - Engage in capacity building activities in areas such as fundraising, income generation, cost share, etc.
  - Provide funding for capacity building and adaptation strategies
3. Link the issue of CSOs with other initiatives such as Protection of Basic Service (PBS), EC Civil Society Fund, etc.
  - Roles and contribution of CSOs
  - Media outreach
  - Documenting and distributing best practices of CSOs
4. Policy dialogue towards better legal environment
  - Lobbying
  - Networking

Various donors have expressed their interest in supporting the Civil Society Task Force, and some donors, such as Irish Aid and CIDA, have already begun releasing funds. The Civil Society Support Group (CSSG), which is composed of Irish Aid, CIDA (ECCO), DFID, Norwegian Embassy, and SIDA, has already started working with the CSA and agreed to have regular meetings in which concerns can be discussed. In addition, Pact Ethiopia, in close consultation with USAID and other members of the CSSG, is working on the Adaptation Facility, particularly on Domestic Resource Mobilization (DRM), Strategic Plan Development, and awareness-raising on the CSP.

#### **(d) CSOs' Individual Responses**

The challenge of the new law relates to the very existence of some CSOs, particularly those working on advocacy and human rights issues. Even before the adoption of the CSP the number of these organizations was insignificant.<sup>19</sup> The majority of CSOs in Ethiopia were and are religious and development (service delivery) organizations. Those Ethiopian CSOs engaged in restricted activities are now considering adaptation strategies individually and collectively. It appears that the majority of these CSOs are planning to be registered as "Ethiopian Resident Charities or Societies," abandoning work on advocacy and human rights areas. Very few, perhaps not more than three organizations, will be registered as "Ethiopian Charities or Societies" and focus on governance and human rights issues.

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<sup>19</sup> According to the official Estimation by Ministry of Justice, advocacy CSOs were about 125 out of 3,800 CSOs registered at the Federal level.

## **(2) Lessons Learned**

The CSOs and the international community did their best to avert the current situation, and are still working for a better legal environment. On the other hand, the Government, and particularly the ruling party, is determined to curb the activities of advocacy CSOs in Ethiopia through the legislation regardless of the pressures it faces at the international and national levels. Considering the active roles CSOs played in the 2005 National Election and in view of the upcoming (2010) National Election, the relationship between the CSOs and the Government remains strained, and there is no chance of amending the legislation in the near future.

One of the major challenges for CSOs in addressing the draft legislation was their inability to mobilize the public at large and the media. By contrast, the Government did much to attract public attention and to highlight all the evils of CSOs.

Many also agree that the sector itself contributed to the enactment of such a draconian law. Some of the major internal contributing factors to the adoption of the legislation include the following:<sup>20</sup>

- Weak accountability and transparency of CSOs to their constituencies and the public;
- Weak or no self regulation system;
- Weak institutional development;
- Absence of internal democratic administration;
- Programs and projects are mostly fund-driven;
- Lack of focus and commitment on organizational objectives; and
- Poor networking and collaboration culture.

## **(3) What Next?**

The CSOs and the international community should work in close cooperation toward alleviating the existing situation, particularly before advocacy CSOs perish in Ethiopia. The international community must use its leverage and exert all necessary influence on the Government, which so heavily relies on the financial support of foreign countries. Donors to the Ethiopian Government must ensure that their development agreements include the participation of CSOs as much as possible. The international community can facilitate constructive dialogue between the Government and CSOs on amending the legislation. They should provide due attention and extend their support to CSOs that are likely to be affected by the legislation.

Similarly, CSOs must continue their collective effort for the amendment of the legislation and establish a relationship with the Government that is based on trust and confidence. CSOs may want to challenge the constitutionality of the law both at the national and international levels. They should also engage in ongoing dialogue with the Government at the expert and political levels for the amendment of the law. Collectively they should support each other in efforts to adapt to the new legislation. Attention should also be given to the establishment of a strong self-regulatory system which ensures the independence, accountability, and transparency of CSOs.

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<sup>20</sup> The Role of NGOs in Protecting Democratic Values, the Ethiopian Experience: The Challenge of Democracy from Below, edited by Bahru Zewde et al., Forum for Social Studies, 2002, pp 125-129.

## ***Restrictions on Foreign Funding of Civil Society***

# **Russia**

**Aleksej Bogoroditskii<sup>1</sup>**

*While Russian legislation still contains numerous challenges in regards to activities of non-commercial organizations (NCOs), the Russian Federal Law on Non-commercial Organizations was amended in 2009,<sup>2</sup> bringing significant improvements to the regulatory environment for NCOs. Among other issues, the newly amended law has ushered in the following changes:*

- *Small NCOs that do not receive foreign funding and have no foreign founders will be exempt from formal reporting of annual revenue totaling less than 3 million rubles, or approximately US \$100,000;*
- *All NCOs may make required reports on their activities publicly available by either posting the reports on their website or publishing the report in selected media;*
- *Mandatory government audits of NCOs will no longer take place annually, but rather every three years—the same as for commercial enterprises;*
- *If an NCO does not submit all of the documents required for registration or if there are mistakes in the submitted documents, in lieu of an automatic denial of registration, the registration process may be suspended for up to three months, until the applicant completes or corrects the application. The registration body will proceed with registering an NCO once the application file is complete.*
- *In considering a registration application, the registration body may only request documents specified in the law; and*
- *Refusal to register a foreign NCO representative office may no longer be based on criteria such as “threats to the unique character, cultural heritage, or national interests of the Russian Federation.” These criteria have been removed from the law.*

*The election of the President Medvedev has fueled hope that the legal framework for civil society will continue to improve, eliminating other obstacles affecting NCOs, including barriers to foreign funding of NCOs discussed in this report. As the report makes clear, the funding constraints for NCOs were primarily introduced in 2006, prior to the election of President*

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<sup>1</sup> This paper is made possible with the generous support of the American people through the United States Agency for International Development (USAID). The contents are the responsibility of the authors and do not necessarily reflect the views of USAID or the United States Government.



<sup>2</sup> In June 2009, the State Duma adopted amendments to Russian Federal Law No. 7-FZ of January 12, 1996, “On Non-Commercial Organizations” (NCO Law) that came into force on August 1, 2009.

*Medvedev; indeed, the focus of this report is predominantly on that particular time – the events surrounding the lead-up and immediate aftermath of the legislative changes introduced in 2006. By focusing on these constraints – which are largely still in place – the article seeks to shed light on the political narrative surrounding the introduction of the constraints and thereby provide insight, which may be instructive for those in other country contexts.*<sup>3</sup>

## **I. Types of Restrictions on Foreign Funding of Civil Society**

### **A. The Nature of the Legal Restriction**

The main obstacles precluding non-commercial organizations (NCOs) from obtaining foreign funding are less related to legal restrictions *per se*, and more to the consequence of official government policy and the selective application of legal provisions. Special regulations pertaining to the registration, reporting, control and liquidation of NCOs provide a toolbox of legal provisions subject to selective application. In examining the nature of the legal restrictions, this section considers (1) the negative perception of foreign-funded NCOs; (2) legal barriers affecting representative offices of foreign organizations; (3) the government list of approved foreign grant makers; (4) legal and practical barriers affecting foreign-funded NCOs; and (5) the taxation of foreign financing.

#### (1) Negative Perception of Foreign-Funded NCOs

The Russian Government encourages negative attitudes toward foreign donors who fund NCOs and NCOs receiving foreign funding to work in the field of human rights protection, monitoring of the environment, law enforcement and migration, supporting volunteer initiatives, etc. This, in turn, furthers the societal perception of international NCOs and foreign-funded NCOs as an enemy. Russian human rights activists note the presence of “negative rhetoric on the part of authorities in regard to independent NCOs. This attitude frequently borders on outright animosity toward organizations obtaining foreign funding.”<sup>4</sup> It has also been noted that “NCOs funded from foreign sources are subjected to more frequent inspections and are required to submit additional reports, etc.”<sup>5</sup>

#### (2) Legal Barriers Relating to Foreign Representative Offices

The Russian Government has established special regulations pertaining to the registration and reporting of subsidiaries and representative offices of foreign and international NCOs, which create certain difficulties for carrying out their activities on the territory of Russian Federation. (Federal Law N 18-Φ3 of 01/10/2006 “On introduction of amendments into certain legislative acts of the Russian Federation”) The special regulations include:

- At the time of registration, foreign NCOs must submit a notary certification, receipt of Apostille, and documents relating to the founders of a foreign NCO, translated into Russian.

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<sup>3</sup> These introductory paragraphs were contributed by ICNL; Sections I-III, which follow, were authored by Aleksej Bogoroditskii and do not necessarily reflect the views of ICNL.

<sup>4</sup> <http://www.socpolitika.ru/rus/ngo/documents/document639.shtml>

<sup>5</sup> [http://www.lawcs.ru/index.php?option=com\\_content&view=article&id=226](http://www.lawcs.ru/index.php?option=com_content&view=article&id=226)

- Foreign NCOs must submit reports to the Ministry of Justice, on a quarterly basis, relating to the amount of income, its anticipated spending, and purposes of spending; and on an annual basis, reports on planned programs (no later than one month before the start of the implementation of the program in the Russian Federation). It is also required to inform the Ministry of Justice about any changes in the program no later than 10 days after making such a decision.
- Foreign NCOs have no right to use the simplified tax system, and therefore cannot benefit from the simplified tax-finance reporting (subsection 18 of section 3 of Article 346.12 of the Tax Code).
- Government agencies have been vested with expanded authority to control the activities of branches and subsidiaries of foreign and international NCOs, including the right to suspend certain programs, but are not subject to clear and reasonable criteria for the application of such measures and restrictions.

### (3) Government List of Approved Foreign Grant Makers

In order to give grants to Russian NCOs on a tax-exempt basis, foreign donors must be included on a government list. The adoption of the RF Government Decree № 485 of June 28, 2008 (“On the list of international organizations whose grants (free of charge assistance) extended to Russian tax-payers shall be exempt from the taxation levied against the revenues of Russian grantees”) decreased the number of foreign donors whose grants are free from taxation from a total of 101 to a mere 12. All private donors were excluded from the government list. Significantly, the 2008 Decree also failed to establish criteria for securing a place on the government list. Additionally, foreign organizations that were removed from the list are now liable to pay taxes to the state budget. In response, a number of donors and NCOs opted to enter into donation agreements, or into contractual relations (or fee-for-services agreements).

### (4) Legal and Practical Barriers Relating to Foreign-Funded NCOs

As mentioned above, the regulatory barriers relating to foreign-funded NCOs are less the result of specific rules applicable to foreign-funded NCOs and more the result of selective application of law. Russian NCOs receiving foreign funding face unfriendly attitudes on the part of state officials and business representatives alike when addressing the issue of financing social projects – primarily because foreign-funded NCOs are suspected of “hostile” activities. The state takes special steps to control the activities of foreign-funded NCOs through the following regulatory methods:

- Additional inspections, formal and otherwise. When preparing oversight plans, the authorized agency, as a rule, tends to give priority to inspecting foreign-funded NCOs;<sup>6</sup>
- Additional reporting to the authorized agency, despite the fact that these reports duplicate the reports filed with tax authorities.
- In practice, NCOs experience many difficulties when they try to implement projects/activities which are funded from foreign sources. For example, NCOs may have difficulty renting a public hall or conference room, or obtaining a

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<sup>6</sup> <http://www.kasparov.ru/material.php?id=48183BB91FB94>

permit to conduct a meeting/demonstration, or securing the participation of government officials in an event as a speaker. More generally, government agencies are often unhelpful and may use bureaucratic excuses to frustrate the performance of NCO activities.

- Additionally, government agencies often hinder NCOs in the implementation of projects by launching coordinated inspections and by demonstrating negative attitudes toward NCOs.

#### (5) Taxation of Foreign Financing

In addition to the government list of foreign donors described above, whereby foreign donors must be included on a government list in order to give tax-exempt grants, Russian law envisions a mechanism of advance registration for technical assistance projects where NCO-implementers are seeking tax benefits. (Decree of the RF Government № 1547 “On establishing the Commission on the international technical assistance” of December 25, 1998) The Commission on International Technical Assistance under the Ministry of Economic Development is responsible for registration of technical aid programs. Irrevocable technical aid constitutes assets and goods provided free of charge to Russian legal and/or physical persons by foreign countries, their federal or municipal bodies or international and foreign organizations, which is certified through registration of a project or a program on technical assistance. Technical assistance can be provided for two primary purposes: to support economic and social reforms and to conduct disarmament. The law requires implementers to register programs and projects only where implementers (NCOs) are seeking tax benefits.

In practice, however, the mechanism is not functional, due to excessive bureaucracy and a lack of transparency in the decision-making process. Tellingly, employees of the Commission themselves confirmed the lack of a number of norm-setting documents which are supposed to regulate certain procedural issues of the registration process.<sup>7</sup> As a result, NCOs must pay taxes – and in particular, VAT – within the framework of assistance projects.

#### **B. Early Warning Signs of Restrictions**

The concern with foreign funding of NCOs was first raised in then-President Putin’s Address to the Federal Assembly in 2004:

There are thousands of public associations and unions in our country which are engaged in constructive activities but not all of the organizations work for the benefit of people’s interests. For some organizations, obtaining funding from influential foreign funds has become the top priority, while for others this priority implies serving dubious vested and commercial interests. Meanwhile the most urgent issues facing the country and its citizens remain neglected.

In May 2005, Nickolai Patrushev, Director of FSB, in his report to Parliament, suggested toughening the legal regulation of NCO activities: “An inadequate legislative basis and the lack of efficient mechanisms of state control lay the foundation for carrying out intelligence gathering under the cover of charitable and other activities.”

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<sup>7</sup> [http://www.bclub-ngo.ru/Work/sdokl\\_sept.html](http://www.bclub-ngo.ru/Work/sdokl_sept.html)



In December 2005, Alexander Yakovenko, Deputy Foreign Minister, asserted the following: “There is little wonder that Russia’s foreign policy is perceived in a warped and distorted way abroad. This happens because Russian and Western media tend to quote NGOs generously funded by foreign capital.”

At the time of the adoption of the new legislation on NCOs in January 2006, then-President Putin commented that “the Government will support NCOs but shall see to it that their funding is transparent, which should guarantee their independence; otherwise they would dance to the tune of their foreign puppeteers.”<sup>8</sup>

In 2007, Putin maintained the same line: “There are those who craftily use pseudo-democratic phraseology for the purpose of returning to the not-so-distant past: some – in order to continue plundering the national wealth, rob our people and the state with impunity – the way they used to do it, while others do it striving to deprive our country of its economic and political independence. The flow of resources from abroad earmarked for direct interference into our internal affairs is steadily growing.”<sup>9</sup>

### **C. Impact of Legal Restrictions**

Most of the legal barriers described above became law with the enactment of the Federal Law № 18-ФЗ on April 18, 2006. Certain regulatory measures aimed at the partial liberalization of the NCO legislation are currently being prepared, but they fail to address the need to improve the climate for foreign funding of NCOs in Russia.

Since 2006, the number of NCOs seeking foreign funding has decreased. The number of NCOs and civic activists has declined and there is an exodus of young people from the civic sector. In addition, the prestige of charitable and civic activities has plummeted in the eyes of the general public. Furthermore, there is a decline of international exchange, mutual internships and implementation of new social technologies.

In sum, the Government has managed successfully to reduce foreign influence on the social and political processes of the territory of the Russian Federation.

## **II. Justifications**

Stricter regulatory control over NCOs and NCO activities has been justified by a range of supporting rationales, including the following:

- The need to enhance the efficiency of the registration process and supervisory oversight of NCO activities;
- The need to increase the transparency and accountability of NCOs, and in particular, the transparency of NCO funding and the use of resources;
- The need to prevent the use of NCOs for money laundering and tax evasion;
- The need to prevent interference in the affairs of the state, and to guard against attempts to exercise foreign influence on the internal affairs in Russia through foreign-funded NCO activities; and

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<sup>8</sup> <http://www.kommersant.ru/doc.aspx?DocsID=760462&ThemesID=132>

<sup>9</sup> <http://www.rb.ru/news/politics/2007/04/26/122445.html>



- The need to protect national security and to undertake measures aimed at fighting terrorism and extremism.

In justifying the restrictive regulations introduced in 2006, the Russian Government relied most heavily on the legislative goal of enhanced transparency and increased efficiency of registration and supervision. Statements by politicians and national security officers, however, belied an underlying motivation linked with a view of NCOs as a subversive threat to the state. Indeed, NCOs were perceived to have played subversive roles in the “colored revolutions” in neighboring countries, and the new restrictions were seen as necessary, at least in part, to guard against similar attempts by NCOs in Russia.

Foreign-funded NCOs in particular were viewed as politically affiliated and threats to the national security and national sovereignty of the Russian Federation. For example, according to one official of the national security system, “NCOs, tied to their foreign partners, are addressing one and only one issue on the territory of the RF: they are undermining the constitutional form of government and the very statehood of the RF.”<sup>10</sup> According to his colleague, “American and British agents are carrying out their activities behind the façade of non-commercial and faith-based organizations striving to give charitable grants to talented Russian citizens.”<sup>11</sup>

The governmental goal to enhance transparency and accountability of NCOs is legitimate, and likely complies with international standards. But the selective application of regulatory requirements vis-à-vis certain types of NCOs runs contrary to the standards of human rights established in the European Convention on Human Rights and Fundamental Freedoms, and also contradicts the standards proclaimed by the Council of Europe and the Constitution of the RF. Moreover, such a regulatory approach is incompatible with the very spirit of democracy and freedom.

### **III. Responses and Lessons Learned**

#### **A. Responses**

By the time amendments to the legislation on NCOs were adopted in 2005-2006, the Russian Government had taken considerable steps toward creating a public-private partnership, which, in practice, meant creating a system of informal control over civic initiatives of “the opposition NCOs” and engaging loyal NCOs in the system of management of the societal/government processes. As a consequence, the civil society community failed to take a consolidated stand in relation to the new legislation. Evaluation of the proposed amendments was critical, as a rule, but nonetheless varied from extremely pessimistic to moderately critical. The range of opinion depended, to a great extent, on the proximity of the NCO to the authorities and on the accessibility of government funding. Still, NCOs exerted considerable pressure and succeeded in removing the most odious and radical amendments from the draft law.

After the law was enacted in 2006, and during its implementation, NCOs managed to combine their efforts around monitoring of the implementation of the law and assessment of the impact of the 2006 legislation. The results of the monitoring research were presented to the country’s leadership. Separate assessments of the situation of civil society in Russia were

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<sup>10</sup> <http://pressa.irk.ru/number1/2007/51/006002.html>

<sup>11</sup> <http://www.profile.ru/items/?item=17473>

conducted by the Council of Europe and the European Parliament. These efforts, taken together, helped lead to “untightening the screws” and the eventual adoption of amendments to the law, which became effective in August 2009.

### **B. Lessons Learned**

Based on the experience of the past several years, NCOs have drawn the conclusion that the framework of formal institutions, such as public chambers and other forms of civil assemblies, are not necessarily conducive to the protection of the rights of NCOs, but rather serve the interests of the state in controlling civic initiatives. In light of this, it would seem more effective to develop informal networks and coalitions uniting NCOs for the purpose of collective protection and lobbying for the rights of NCOs. Moreover, there is a role for the international diplomatic community and local networks and coalitions may seek to draw on the support of the international community.

### **C. What’s Next?**

Two responsive strategies have been pursued and continue to be pursued by NCOs operating in the Russian Federation. First, NCOs have monitored and will continue to monitor how the law is being applied and the impact it is having on the sector. Second, NCOs have promoted and will continue to promote legislative initiatives in the interests of civil society at the national and regional levels.

***Restrictions on Foreign Funding of Civil Society***

**Sri Lanka**

**Rohan Edrisinha<sup>1</sup>**

The political and legal environment in which civil society organizations function in Sri Lanka has become increasingly difficult in recent years. Today there is a strong likelihood that legislation will be introduced to facilitate greater governmental control of nongovernmental organizations through various means, including tighter control of the receipt of foreign funding. Influential bodies within successive governments have routinely threatened the introduction of laws and regulations restricting foreign funding available to NGOs. The political narrative of Sri Lanka, however, at present suggests that the restrictions spring from political rather than economic motivations.

**THE PRESENT LEGAL FRAMEWORK**

NGOs generally seek legal incorporation through one of five laws or mechanisms:

1. Registration under the Societies Ordinance of 1891;
2. Registration under the Companies Act 2007;
3. Registration under the Cooperative Societies Act of 1992;
4. Registration under the Voluntary Social Service Organisations Act of 1980; or
5. Legal incorporation by an Act of Parliament sponsored by a Member of Parliament through the mechanism of a Private Members Bill.

Most of these laws and mechanisms set forth requirements and conditions that are binding on NGOs acquiring legal status under them. These include requirements relating to funding, the management and auditing of financial receipts, etc. This is an important point that is often ignored by advocates of greater regulation or control of NGOs—that there are regulatory procedures and mechanisms already in place. Before further restrictions are imposed to regulate NGOs, reasons should be adduced as to why the prevailing legal regime governing NGOs is found to be inadequate. One needs to consider the option that perhaps the existing laws could be amended to overcome deficiencies, if any.

**THE POLITICAL CONTEXT**

As stated above, recent attempts to intimidate and control NGOs are motivated by a complex political context that is created by a variety of factors. These include a growing authoritarianism in general, the tsunami of December 2004, the insecurities of the majority

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<sup>1</sup> Faculty of Law, University of Colombo. This paper is made possible with the generous support of the American people through the United States Agency for International Development (USAID). The contents are the responsibility of the authors and do not necessarily reflect the views of USAID or the United States Government.



community, and since 2005-2006, the election of a Government that essentially adopted a militaristic response to the island's civil war.

a) Authoritarianism

Since the early 1990s authoritarian political regimes have attempted to intimidate and harass prominent NGOs that were perceived to pose threats to incumbent Presidents and regimes. In 1990, for example, President Ranasinghe Premadasa appointed a Presidential Commission to investigate alleged malpractice, fraud and proselytism. It was widely accepted that the main motivation for the appointment of the Commission was Premadasa's fear of the political aspirations of the Sarvodaya Movement and its well-known leader, A. T. Ariyaratne. Since 2005, there have been several initiatives to intimidate NGOs engaged in human rights and conflict resolution-related activities that have challenged governmental policies.

b) The Tsunami of 2004

The tsunami and the massive influx of foreign assistance that was often channeled through international NGOs (INGOs) and local NGOs generated a greater sensitivity to the use and accountability of foreign funds. While some of these concerns were legitimate and raised valid questions as to the effective and responsible management of resources, the political groups that were hostile to NGOs for ideological reasons and reasons of self-interest exploited many of these apprehensions to further their ongoing concern to restrict the freedom of association of NGOs. The arrival of many groups with religious affiliations and the donation of funds by religious organizations from the West provided further ammunition to the argument that such funds were being used for "unethical conversions," particularly of Buddhists and Hindus.

c) The Insecurities of the Majority Community

A combination of factors – including ethnic conflict, the military success of the Liberation Tigers of Tamil Eelam (LTTE) resulting in their de facto control of parts of the northern and eastern provinces of the island, attempts by the Governments of Sri Lanka between 2000 and 2006 to reach a negotiated political settlement with international facilitation, and the growing internationalization of the island's ethnic conflict – generated insecurity and a defensive reaction on the part of the island's majority community, which is largely Sinhalese and Buddhist. This group, often referred to as a majority with a minority complex, began to view NGOs – which often depended on foreign funding for their activities – as agents of Western countries and entities that had their own political and ideological agendas that were viewed as hostile to indigenous values and the interests of the majority community.

d) The Presidential Election 2005

The election of Mahinda Rajapakse to the office of President in November 2005 marked a significant shift in the government's policy to the ethnic conflict, the LTTE, and the role of the international community. President Rajapakse depended on two small political parties for his electoral victory: the Janatha Vimukthi Peramna (JVP) and the Jathika Hela Urumaya (JHU). These two parties had a disproportionate influence on and access to the new President. This, together with a growing frustration with what was seen as a maximalist and intransigent LTTE on the part of many Sri Lankans and members of the international community, enabled the Rajapakse government to adopt a more hawkish and militarist response to the LTTE. The Government intensified the war effort employing strong military offensives that often violated international humanitarian legal norms, leading to bloody conflict and large-scale loss of lives.

Finally, in May 2009, the Government defeated the LTTE and brought the whole country under its effective control.

The political factors outlined above all contributed to a significant shift in the attitude of the government to NGOs and their freedom and autonomy. NGOs that had been at the forefront of campaigns for constitutional reform, conflict resolution through negotiation and political accommodation, media freedom, and human rights, by and large, worked closely with the Kumaratunga Administrations from 1994 to 2005. Though there were strains at various times, there was mutual self-interest and a similarity of broad goals on the part of government and such NGOs. The election of the Rajapakse Administration, with the presence of the two small ultra-nationalist parties, created a sharp divide between the government and the groups of NGOs described above.

## **DEVELOPMENTS FROM 1994-2005**

Despite the relatively positive relations that existed between NGOs and civil society groups on the one hand, and the government on the other, various legislative and regulatory changes were introduced during this period that weakened the freedom and autonomy of NGOs.

### a) Introduction of the Voluntary Social Service Organisations (Amendment) Bill 1998.

This Amendment Bill was introduced to the Voluntary Social Services Act (VSSA) of 1980 in extraordinary circumstances. Civil society groups lobbied successfully against the Amendment and received assurances from the Minister of Social Services that it would not be enacted. However, the Amendment remained on the Order Paper of Parliament. On a chaotic day when the Opposition had walked out of Parliament, the Government enacted all the Bills listed on the Order Paper, including the VSSA Amendment Bill. The Bill provided that where a Board of Inquiry appointed by the Minister reports that “there is evidence to support an allegation of fraud or misappropriation against a voluntary association,” the Minister may appoint an interim board of management in place of the existing board of directors of the association. The Centre for Policy Alternatives and several civil society activists challenged the constitutionality of the Amendment on the grounds that it violated the freedom of association. But the legal challenge was dismissed at a preliminary stage on the basis that the Sri Lankan Constitution prohibited judicial review of legislation.

### b) Introduction of Registration and Supervisory Requirements

Various regulations were promulgated in 1999, including a series through Gazette Notification No. 1101/14 of 15 October 1999, in which various requirements with respect to financial management and administration of NGOs registered under the Voluntary Services Act were introduced. There was uncertainty as to whether these regulations applied to all NGOs, including those not registered with the NGO Secretariat under the Voluntary Social Service Organisations Act. Since the Act refers to NGOs as those associations engaged primarily in social service activities, many NGOs engaged in research and advocacy work on issues such as governance and human rights took the view that these new requirements did not necessarily apply to them.

Soon after the tsunami of December 2004, various additional regulations were introduced as a prerequisite for registration with the NGO Secretariat. There were requirements that a local NGO must have a minimum of Rs 10 million while an INGO should have a minimum of US \$1 million. After approval by the Secretariat, the application is forwarded to the Ministries of

Defence and Finance for final approval. At the implementation stage too, various government officers in the districts exercise coordination with and supervisory functions over NGOs engaged in activities that are primarily socioeconomic in nature.

c) Introduction of Tax on Foreign Funding Received by NGOs

One of the proposals in the Appropriation Bill or Budget for 2005 was the introduction of a tax on foreign funding received by certain NGOs. The Inland Revenue (Amendment) Act of 2005 provided that 3% of the aggregate amount that was received by an NGO would be deemed the profit and income subject to tax. Here too the definition of NGO in the Act indicated that the provisions of the Act would apply to NGOs in the socioeconomic sector. An additional controversial feature of the new law was that it gave the Minister of Finance the power to enable the Commissioner General of Inland Revenue to reduce or remove entirely such tax in certain circumstances.

The justification offered by the Government for the introduction of the tax was confused. An official from the Inland Revenue Department who was interviewed stated that the justification was the need to regulate NGOs and the concern with inadequate regulation of NGOs.

## **DEVELOPMENTS SINCE 2006**

a) Continuation of Tax on Foreign Funding.

The Inland Revenue Act, 2006 (as amended in 2007 and 2008) basically continued the policy of taxation described above.

b) Appointment of a Select Committee of Parliament to Investigate NGOs

A motion was made by Nandana Gunatileke, a JVP MP, in August 2005 to appoint a Select Committee of Parliament to investigate the financial management and accountability of NGOs that received foreign funding, and the impact of NGO activities on the sovereignty and the territorial integrity of the country. The committee was appointed on 17 January 2006 under the chairmanship of Mr. Gunatileke.

Though the number of members on the Committee was increased from 19 to 26, it was clear that the representatives of the mainstream political parties were not very interested in the Committee's proceedings. The leadership and initiative came from the JVP and the JHU – the Sinhalese Nationalist parties that wielded considerable influence in the new Rajapakse Government. The Committee focused its attention on a few NGOs that had played an active role in supporting the Norwegian facilitated peace process that took place between 2000 and 2005. Apart from requiring these and other NGOs to furnish the Committee with large volumes of materials, including records, organizational details, accounts, reports, publications, and details about staff, some organizations were summoned before the Committee and questioned, often in the presence of media personnel sympathetic to the politicians providing leadership to the Committee.

One of the striking features of the report of the select Committee was that it seemed to lack appreciation of the scope of freedom of association and speech and expression in a democratic society. The Committee was critical of NGOs that advocated federalism on the basis that the President had been elected in November 2005 on a platform that promised to preserve the unitary character of the Constitution, and that the NGOs were acting in a manner

“contradictory to the mandate given by the people of the country.” Furthermore, many NGOs working in conflict affected areas were censured for engaging in activities prejudicial to national security.

The Committee proposed a comprehensive new legal framework for the regulation and supervision of NGOs and the repeal of most of the existing legislation. It proposed the establishment of a NGO Commission to monitor and supervise NGOs. The Committee also proposed restrictions on the grant of visas to foreign staff, the creation of a National NGO Fund to assist NGOs that render a service to society, created inter alia, by receipts from a percentage of funds received by NGOs.

A Draft Bill on NGOs has been prepared. As is the practice in Sri Lanka, this draft is not accessible to the public. The Bill has been prepared with little or no discussion with relevant stakeholders and therefore it is not clear how many of the Select Committee’s recommendations have been incorporated.

c) A Sustained Attack on NGOs in State Media

The appointment of the Select Committee of Parliament to investigate NGOs was accompanied by a sustained and aggressive series of attacks on prominent NGOs and their leadership. The Sinhalese nationalist leaders who were influential in the Rajapakse Government led the attacks which received widespread publicity in the state media and elements of the private media that were sympathetic to the Sinhalese Nationalist position.

The NGOs working in the areas of governance, human rights, and conflict resolution were the main targets. The main criticisms leveled against them were that they were engaging in activities prejudicial to the sovereignty and territorial integrity of the country; promoting a pro-Western, Judeo-Christian, and hence alien agenda; supporting Tamil separatism; and acting as traitors by making it difficult for the government to wage an effective war against terrorism. NGOs and their leaders were accused of being traitors if they advocated federalism or a negotiated settlement to the ethnic conflict or respect for international humanitarian law and human rights.

## **CONCLUSION**

The challenges faced by NGOs with respect to their freedom and autonomy are more political than legal or regulatory. While the existing legal and regulatory regime has become more repressive in recent years, restrictions have been directed primarily at NGOs engaged in developmental work with a socioeconomic focus. Loopholes in the law such as the definition of NGOs have enabled NGOs in the areas of human rights, governance, and conflict resolution to operate reasonably freely. The threats that these organizations have faced in recent years have been of an extra-legal nature. This dangerous development, coupled with the decline of the rule of law in the country, has made this period a particularly difficult one for these NGOs as well.

What promises to be a comprehensive Bill which deals with NGO regulation and which consolidates and “improves” the existing law seems to be in an advanced stage of preparation and could be presented in Parliament soon. It may be possible to challenge the Bill on the grounds of incompatibility with fundamental rights and freedoms. However, the politicization of the judiciary in recent years and its conservative approach to constitutional interpretation and deference to the legislature suggest that one cannot have too much confidence in the Constitutional Court (Supreme Court) of the country.

While there needs to be a robust defense of the freedom of association of NGOs in the political and legal arenas, there must also be a campaign to challenge the governmental discourse on sovereignty, which is essentially a statist as opposed to a people-based discourse; and a reaffirmation of the universalist and international dimensions of human rights and constitutionalism while also relating such concepts to local culture, religion, and history. NGOs should also demonstrate willingness to have reasonable and effective regulation that promotes accountability, transparency, and responsibility while preserving autonomy, which is not easy to achieve in a society that has become increasingly politicized as a result of the decline in independent institutions. Recent political trends suggest that the campaign to discredit and control NGOs will intensify both through legal and extra-legal means.



## ***Restrictions on Foreign Funding of Civil Society***

# **Venezuela**

**Marcos Carrillo<sup>1</sup>**

### **Introduction**

In order to understand the reality of the legal restrictions on foreign funding affecting civil society organizations in Venezuela, it is necessary to study not only the already enacted legislation but also the Draft Law on International Cooperation (hereinafter, “ICL”) that could be enacted in 2010, which reflects not only the Government’s intentions but also the government practice towards CSOs over the past few years.

### **I. Types of Restrictions on Foreign Funding**

#### **A. Prohibitions Against Foreign Funding**

*Current legislation:* Currently there are no direct legal restrictions targeting donors or recipients of foreign funding. Nonetheless, Venezuela is under an exchange control regime that indirectly may affect foreign funding. Thus, any cooperation must be accomplished in Venezuela’s local currency, Bolivares.

*The ICL draft,* however, establishes restrictions targeting foreign funding. Indeed, the object of the law is to determine the legal regime for international cooperation. (Article 1) The ICL applies to all activities carried out in the framework of international cooperation, including the reception, transfer, and interchange of goods, services, assets, public and private resources, human, financial, and economic matters, from other countries toward Venezuela and from Venezuela to other countries. (Article 2) Relevant restrictions include the following:

Article 18 of the ICL draft makes NGO “inscription in the Integrated Registry System [created by this same law] a prerequisite for proper recognition by the State to engage in international cooperation activities with counterparts in other countries.” If the ICL is enacted, inscription in the Integrated Registry System would also be required to access the fiscal incentives contemplated in Venezuelan tax regulations. (Currently, it is not necessary for CSOs to be registered before a governmental body created specifically to control CSOs; CSOs must only be registered in the public registry like any other legal entity.)

- In accordance with the first transitional regulation of the ICL draft, in the six months following the publication of the ICL, organizations that engage in any activities related to

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international cooperation must adjust their operational guidelines to those established by and emanating from the decentralized Institution in Charge of International Cooperation.

- Article 6 of the ICL subordinates the areas of international cooperation “preferable to those established in the National Plan for Development.” Hence, the areas of international cooperation will be determined by the National Plan.
- Article 7 establishes the priorities of international cooperation, which must be related to “energy, educational, cultural, scientific, technological, social, economic, financial, environmental, commercial, sporting and criminal matters, as well as support for emergency situations.” It is important to stress that among these priorities the promotion, protection, or defense of human rights is not included. Hence, foreign funding for these areas is clearly restricted.

Barriers can also appear through unwritten government practices. They have included “de facto” prohibitions to register new human rights NGOs or to register changes in their charters. Also, cases of direct governmental retaliation and prosecution against members of NPOs that exercise the right of freedom of speech or advocacy have been reported. The ICL could give the Government clear and direct legal support for such conduct.

### **B. Advance Government Approval**

*Current legislation:* Apart from the exchange control restrictions, which are applicable not only to CSOs but to every legal or natural person, government approval is not required to engage in international cooperation. There have been cases, however, of human rights CSOs whose registration has been obstructed by unwritten government practice.

*ICL draft:* Article 3 defines international cooperation as “all the range of actions, activities and procedures, conducted by countries, international organizations, NGOs and other types of organizations that engage in activities related to international cooperation, destined to transfer resources and capacity to support social, human and economical development. In this sense international cooperation is the means by which the Venezuelan State receives and transfers human resources, goods, assets, services and technology, with the objective of complementing and contributing to development efforts.” Article 10 establishes that “...the President will be able to create a decentralized institution which will be in charge of organizing, directing, controlling, coordinating and evaluating all activities related to international cooperation of which the Venezuelan State is part.” Reading these two norms together, it can be concluded that not only government approval will be necessary but also there will be complete control of the Government over any aspect of IC.

### **C. Penalties for Receipt of Foreign Funds without Official Permission**

*Current legislation:*

The Ley de Ilicitos Cambiarios (Illicit Currency Exchange Law) establishes penalties for any legal person – including a CSO – that violates exchange control laws. Activities considered to violate the Illicit Currency Exchange Law include the purchase or sale, or any conduct that implies receiving or granting, any foreign currency in any amount surpassing 10,000 USD carried out without Banco Central de Venezuela (Venezuelan Central Bank) intervention. Such conduct is subject to a penalty consisting of payment in Bolivars of the amount equivalent to twice the amount of the operation that is being sanctioned. If this amount surpasses 20,000 USD or its equivalent in any other currency, the sanction will involve a prison sentence for

a period of between two and six years, plus a fine amounting to twice the quantity of the operation that is being sanctioned.<sup>2</sup>

Where a CSO needs to buy foreign currency, and fails to declare the received foreign currency, or declares it in a period other than that which is permitted by law, the CSO will be subject to a fine. If the person or entity then fails to prove the legality of the exchange, CADIVI (the governmental body, within the Ministry of Finance, that is in charge of the exchange control regime) is entitled to confiscate the monies received in a suspicious or presumably illegal way.

In case a CSO requires foreign currency, it must file a request at CADIVI. Those who fail to use granted money for the alleged purposes will be considered to deviate or improperly use the assigned money and will also be subject to a fine consisting of the payment of twice the amount of the operation, activity, or conduct that is being sanctioned.

It must be observed that **Ley Orgánica Contra la Delincuencia Organizada** (Organic Law Against Organized Crime) does not limit or define the meaning of “illicit activities,” giving an ample margin of discretion to the governmental authorities to define what an illicit activity may be.

In 2004 two members of the NGO Súmate were prosecuted for receiving international aid from the National Endowment for Democracy (a U.S.-based organization), which was allegedly conspiring against the State’s integrity. The prosecution was based on the following:

- *Article 128* of the Criminal Code states that whoever in complicity with a foreign nation or with external enemies, conspires against the State’s integrity or institutions, or whoever by whatever means commits a hostile act, will be sanctioned with imprisonment for a period that ranges from 20 to 30 years.
- *Article 129* of the Criminal Code states that whoever, inside or outside Venezuela, attempts to threaten the country’s independence or its geographical integrity will be punished with imprisonment for a period that can range from 20 to 26 years. This sanction will also apply to whoever requests by any means the intervention of a foreign government to overthrow the Venezuelan Government.
- Finally, *Article 132* of the Criminal Code states that anyone who, inside or outside the national territory, conspires to destroy the country’s republican form of government, will be sanctioned with imprisonment for a period ranging from 8 to 16 years. This sanction will also be applied to those who request international intervention in Venezuelan internal affairs, or to those who through advertisement in the media encourage a civil war or defame the President or any diplomatic or consular officials with regard to the carrying out of their functions in the country in which the defamation is committed.

*ICL draft:* As stated above, Article 18 of the ICL draft establishes that NGO inscription in the Integrated Registry System (established in this same law) is mandatory and is a condition for the Venezuelan State to grant NGOs recognition as entities entitled to engage in international cooperation activities with counterparts in other countries, and also a necessary condition to access the tax incentive program contemplated in Venezuelan tax regulations.

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<sup>2</sup> See [http://www.cadivi.gov.ve/pdf\\_obj/ley\\_licamb.pdf](http://www.cadivi.gov.ve/pdf_obj/ley_licamb.pdf).

Although the ICL draft does not establish a penalty, general criminal law could be applied to the failure to comply, as explained in the preceding paragraphs.

#### **D. Routing Funding through Government**

*Current Law:* Under current law, there is no requirement to route funding through government ministries or through a designated fund. Due to exchange control, of course, everything related to foreign currency has to be supervised by Venezuela's Central Bank (Banco Central de Venezuela).

*ICL draft:* Article 3 of the ICL draft defines international cooperation as a means by which the Venezuelan State receives transfers and exchanges human resources, property, assets, services, and technology from cooperative sources either internal or external, with the objective of complementing and contributing with national efforts in development matters. Based on this definition, it can be concluded that the State is the only subject of international cooperation.

That said, Article 10 of the ICL draft establishes that regardless of the functions assigned to other ministries, the President will be able to create a decentralized institution that will be dependent on the ministry with competence in international cooperation (which is not specified in the draft and therefore will be appointed discretionally by the President), which will have administrative and financial autonomy and will be in charge of executing and supporting policies, plans, programs, and projects related to international cooperation carried out by the State, through lending and administering resources that are destined to activities related to international cooperation. This institution will also be in charge of developing activities related to the organization, direction, control, coordination, follow-up, and evaluation of everything related to International Cooperation in which the Venezuelan state is a part. Hence, it can be concluded that not only will government approval be necessary but also there will be a complete control by the government over any aspect of IC, all of this in accordance with Presidential orders. The funds coming from international cooperation would have to be directed through this entity.

Likewise, Article 13 of the ICL draft establishes that the Fund for International Cooperation and Assistance will count on resources from legacies, donations, and other assets received by the State from other governments, international organizations, and other institutions that are destined to support cooperation. This Fund will also be integrated by all other assets and resources received in accordance to the law.

#### **E. Mandatory Coordination of CSO Activities with Government Agencies**

*Current Law:* Currently there is no mandatory coordination of CSO activities with government agencies.

*ICL draft:* Article 8 of the draft ICL is clear about this issue, stating that "International Cooperation policies, as an expression of the States' foreign policy, will aim at coordinating and integrating efforts among international organizations, NGOs, both national and international, and all institutions, organizations, foundations or not-for-profit organizations, whether public or private, and civil society; with the common goal of incentivizing human development, social justice and social welfare."

## **F. Taxation on Foreign Funds**

*Current Law:* The current ICL (1958)<sup>3</sup> establishes conditions that are favorable for CSOs and NGOs receiving funds from Venezuela as well as from abroad.

*ICL draft:* In order to have access to tax exemptions or incentives, registration at a special designated governmental registry will be necessary under Article 18 of the ICL draft.

## **II. Early Warning Signals for the Legal Restriction**

In 2000 the Minister of Internal Affairs and Justice, Luis Miquelena, challenged the legitimacy of CSOs in an act that signaled a turning point in the relations between the National Government and CSOs. The case happened as follows: The Venezuelan Constitution establishes that three of the members of the Consejo Nacional Electoral – CNE – (National Electoral Council) must be nominated by civil society. When certain well-known members of civil society were nominated, the Minister challenged their legitimacy, alleging that their organizations did not elect them. Thus, the Government bypassed the Constitutional order and appointed people unrelated to civil society organizations.

Also in 2000 the Tribunal Supremo de Justicia – Supreme Court of Justice – issued three decisions related to CSOs:

- Defensoría del Pueblo vs. Comisión Legislativa Nacional 30-6-00;
- Veedores de la UCAB vs. CNE 23-8-00;
- William Dávila y otros vs. Ministro de Finanzas. 21-11-00.

The decisions set forth a restrictive view of civil society, according to which the foundation of civil society must be national security, in accordance with Article 326 of the Venezuelan Constitution. In relation to foreign funding one of the decisions (William Dávila) established that “[T]he Civil Society recognized by the Constitution is the Venezuelan Civil Society . . . . Thus, as national associations, the CSO representatives can be neither foreigners nor organizations directed, affiliated, funded, financed or supported, directly or indirectly by states, movements or groups influenced either by other states or by international associations, groups or movements with political or economic aims for their own benefit.”<sup>4</sup>

In 2004 the General Prosecutor prosecuted two members of the NGO Súmate (María Corina Machado and Alejandro Plaz), accusing them of receiving international aid from an international organization that was conspiring against the State’s integrity.

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<sup>3</sup> The current ICL draft is a rather innocuous statute of only nine articles. The draft reiterates the principle of International Cooperation (article 1), establishes the forms of International Cooperation (articles 2 and 3), provides that International Cooperation must be accomplished through agreements and/or treaties, and conveys special considerations for international cooperation in the area of construction. The statute does not restrict international cooperation and has no regulations relating to NGOs.

<sup>4</sup> The original text is “Que la sociedad civil, tomada en cuenta por el Constituyente, es la sociedad civil venezolana. . . . Resultado de este carácter nacional es que quienes la representan no pueden ser extranjeros, ni organismos dirigidos, afiliados, subsidiados, financiados o sostenidos directa o indirectamente, por Estados, o movimientos o grupos influenciados por esos Estados; ni por asociaciones, grupos, o movimientos transnacionales o mundiales, que persigan fines políticos o económicos, en beneficio propio.” Sentencia William Dávila y otros vs. Ministro de Finanzas Sala Constitucional del 21-11-00.

In 2006, the first draft of the ICL appeared, without previous consultations with CSOs, and was approved in the first discussion by the National Assembly. During the period 2006-2009 there have been recurring references by Congressmen to the necessity of controlling CSOs.

### **III. Impact of the Legal Restriction**

The Draft ICL has been approved in the first of two National Assembly discussions and it will officially enter into force when approved in the second discussion, which could happen in 2010.

As of 2010, there is a marked tendency toward government centralization in Venezuela. There have been laws passed directed at subordinating States and municipalities to the National Government.<sup>5</sup> Specifically, state and municipal authority in areas of work related to health, education, and security have been reduced and turned over to the National Government. This tendency toward centralization, although not directly targeting NGOs, may very well affect the available resources for their funding. In fact, if the Executive Branch increases control over these resources, the states and municipalities will have less budget capacity for NGO funding, which ultimately will diminish the diversity and independence of funding for NGOs.

### **IV. Justifications**

#### **1. Stated Justifications**

The sponsor of the ICL was the National Assembly, specifically the Commission on Foreign Affairs.

The official Government justifications include the following:

- Official government documents and declarations have stated that the Draft ICL is aimed at “protecting national sovereignty and the Latin American identity as a means of bringing welfare and dignity to all persons that have been excluded or affected as a consequence of the foreign imposition of an unfair and exclusive liberal policy model.”<sup>6</sup>
- NGOs must be accountable to the State.<sup>7</sup>
- The Government must control NGOs just as it does any other legal persons.<sup>8</sup>

Nevertheless, no other legal persons are subjected to double registration or subordinated to Government policies unless they need special permission for certain activities, such as acquiring foreign currency at preferential rates (due to the exchange control regime), import or export of merchandise, contracting with the State, and dealing with particular substances, amongst others. In these cases legal persons must be also registered before the competent office.

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<sup>5</sup> The three main statutes that have been passed to this purpose are the Reform of the Organic Law of Decentralization, Delimitation and Transference of State Competences, the *Ley Especial de Transferencia de los recursos y bienes administrados transitoriamente por el Distrito Metropolitano al Distrito Capital* (Special Law for the Transference of the resources temporarily administered by the Metropolitan District to the Capital District), and the recently approved (February 22, 2010) *Ley del Consejo Federal de Gobierno*.

<sup>6</sup> ICL Exposition of motives.

<sup>7</sup> Roy Daza, President of the Foreign Policy Commission of the National Assembly. *El Universal*, May 6, 2009.

<sup>8</sup> *Idem*.

## **2. Underlying Motivations**

The ICL has been framed in a political context that seeks to restrict citizen's rights and liberties. The ICL draft is based on a theoretical conception that inverts the natural relations between the State and its citizens, by promoting citizen submission to governmental will. According to the justifications of the ICL given by Congressmen, a further motivation for this statute is the desire to limit foreign influence in domestic affairs. To appeal to the nation's sovereignty is one of the most commonly used arguments to restrict rights in Venezuela today. Consider the following statements:

- “Lots of them [CSOs] receive money from the National Endowment for Democracy and other institutions linked with the CIA to carry out conspiratorial activities.”—Saúl Ortega, former President of the Foreign Affairs Commission of the National Assembly.
- “Organized groups – from civil society – must avoid promoting terrorism or getting involved with drug traffic.”—Saúl Ortega, former President of the Foreign Affairs Commission of the National Assembly, June 1, 2006.
- “The ICL will establish control of CSOs’ funding.”—Roy Daza, current President of the Foreign Affairs Commission of the National Assembly, May 12, 2009.
- “From a political point of view it is always important to control international cooperation....”—Roy Daza, President of the Foreign Affairs Commission of the National Assembly, May 6, 2009.
- “We cannot accept that lackey and obsequious organizations, that attend different interests from those of the State, distort the meaning of the law.”—Congressman Carlos Escarrá, April 17, 2009.
- “Of course we are going to control NGOs, because that is what the Venezuelan people want. Here we have to control the activities of a group of organizations, hidden behind an NGO and human rights defenders façade, that receive funds from the USA for political aims and to conspire against the Venezuelan Government.”—Declarations given by Iris Varela, Venezuelan Congresswoman, April 17, 2009.

## **3. Evaluation of the Justification**

The ICL is contrary to what is established in the Venezuelan Constitution regarding the freedom of association, since the Constitution recognizes not only that “every person has the right to associate with lawful ends in conformity with the law,”<sup>9</sup> but also that “the State is obliged to facilitate and permit the exercising of the right of freedom of association.”<sup>10</sup> In other words, it is a Constitutional mandate that all laws drafted must promote the exercise of rights such as freedom of association and under no pretext act in breach of the Constitution. Specifically, the ICL would violate the constitutional right to freedom of association, in that it would oblige NGOs to register with the Integrated System Registry as a condition for the State to grant NGOs proper recognition as entities entitled to engage in international cooperation activities with their counterparts in other countries (and as a condition to access the tax incentives contemplated in Venezuelan tax regulations).

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<sup>9</sup> See Article 52 of the Venezuelan Constitution.

<sup>10</sup> *Idem*.

In order to challenge the ICL, the following legal or policy or factual arguments might be available:

- Article 52 of the Venezuelan Constitution establishes the human right of freedom of association in the following terms: “Everyone has the right to associate with licit ends, in conformity with the law. The State will be obliged to *facilitate* the exercise of this right” (emphasis added). It is worth noting that the previous constitution did not include the latter State obligation.<sup>11</sup>
- Under the Venezuelan Constitution, government regulation, under normal circumstances, must seek to promote or foster CSOs, rather than to control them through State actions.<sup>12</sup>
- In addition, the ICL also violates or threatens basic rights of the Venezuelan Constitution, such as the right to meet publicly or privately, without obtaining permission in advance, for lawful purposes and without weapons;<sup>13</sup> the right to express freely one’s thoughts, ideas or opinions without censorship;<sup>14</sup> the right to freedom of conscience;<sup>15</sup> and the right of association for political purposes, through democratic methods of organization, operation, and direction.<sup>16</sup>
- The ICL also may violate rules established in the International Covenant on Civil and Political Rights.
  - Article 22.1 states that “*Everyone shall have the right to freedom of association with others. ...*” Furthermore, Article 22.2 states that “No restrictions may be placed on the exercise of this right other than those which are prescribed by law and which are necessary in a democratic society in the interests of national security or public safety, public order (ordre public), the protection of public health or morals or the protection of the rights and freedoms of others.”
  - The mandatory and duplicative registration envisioned by Articles 17, 18, and 20 of the ICL is a restriction that probably does not meet the standards of Article 22 of the ICCPR.
  - The ICL would establish the Fund for International Cooperation and Assistance, which would receive and channel all the international cooperation received by Venezuelan NGOs; this requirement also would probably amount to a limitation that violates Article 22 of the ICCPR.

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<sup>11</sup> Recent court decisions, however, are restrictive of this right, especially in relation to NGOs. See *Defensoría del Pueblo vs. Comisión Legislativa Nacional* 30-6-00; *Veedores UCAB vs. CNE* 23-8-00; and *William Dávila y otros vs. Ministro de Finanzas*. 21-11-00.

<sup>12</sup> In fact, CSO activities must be lawful. Hence the Government can intervene in their activities if a CSO is committing unlawful activities according to the law (e.g., Criminal Code, Law Against Organized Crime). The State can also restrict this right under Martial Law, which can only be declared under exceptional circumstances and is regulated by Articles 337-339 of the Constitution.

<sup>13</sup> Article 53 of the Venezuelan Constitution.

<sup>14</sup> Article 57 of the Venezuelan Constitution.

<sup>15</sup> Article 61 of the Venezuelan Constitution.

<sup>16</sup> Article 67 of the Venezuelan Constitution.



- The American Convention on Human Rights (ACHR) also protects the right of freedom of association and other rights.
  - Article 16 of the ACHR protects the right of freedom of association. According to Article 16, the right of freedom of association “shall be subject only to such restrictions established by law as may be necessary in a democratic society, in the interest of national security, public safety or public order, or to protect public health or morals or the rights and freedoms of others.” The ICL does not respect these standards.
  - Article 3 of the ICL runs counter to Article 13 of the ACHR. Article 3 regulates the transfer of “resources and skills” to support development, whereas Article 13 of the ACHR explicitly includes the right “to seek, receive an impart information and ideas of all kinds.”

## **V. Responses and Lessons Learned**

### **1. Responses**

#### **(a) Participation in the Drafting Process**

It is both a constitutional right and an obligation for the National Assembly to include civil society participation in the discussion of draft laws (Article 211 of the Constitution). In 2006, both a representation of universities and a representation of NGOs requested to have formal meetings with the Commission of International Affairs of the National Assembly. The university group was formally received by the President of the Commission and a group of advisors, but the meeting with the NGOs was suspended. None of the suggestions made either by the universities or the NGOs have been included in the draft law so far.

#### **(b) Collective Response of CSOs**

CSOs responded by rejecting the draft law, and supported their arguments on constitutional law and human rights grounds. The position taken by CSOs was to reject the draft law firmly, yet to seek to build bridges with the National Assembly in order to suggest changes. CSOs adopted a strategy along four lines:

1. A media campaign;
2. A campaign directly addressed to NGOs’ beneficiaries; and
3. Lobbying international donors. Communication with Congressmen from the Government party has been virtually impossible.
4. Drafting an alternative statute and eventually propose its discussion by the National Assembly.

#### **(c) Response of International Community**

A group of important donor country representatives have met several times with representatives of CSOs in order to coordinate responsive action. Donor representatives have played a very important role in lobbying the Government; the lobbying efforts have been very effective, since they have helped to delay the promulgation of the draft law. European countries in particular have made an important effort. The Venezuelan Government is very concerned with maintaining a good international image.

The Inter-American Commission for Human Rights, in its 2006 report on the Situation of the Defense of Human Rights Activists in the Americas, urged States to refrain from promoting laws and policies relating to the registration of human right organizations that use vague or imprecise definitions, as this restricts their establishment and operation. The Commission also urged States to refrain from restricting the financing of human rights organizations; States should permit and facilitate CSOs to access foreign funds, in the context of international cooperation in transparent conditions.<sup>17</sup> Its 2010 report on Venezuela evaluates in detail the situation of Human Rights in general and of freedom of association in particular.

Amnesty International also made comments referring to the draft ICL and said that Venezuelan authorities should ensure that the draft law complies with international law relating to human rights that guarantees the right to defend human rights, freedom of association, and freedom and expression.<sup>18</sup>

## **2. Lessons Learned**

In order to confront unjust laws and actions towards CSOs by strong governments, it is important for CSOs to:

- (1) Be organized;
- (2) Solidify CSOs national and international networks;
- (3) Promote cooperation among CSOs;
- (4) Have a clear, solid, and insistent media strategy;
- (5) Lobby international donors and organizations as well as the Government (if possible); and
- (6) Strengthen links between beneficiaries and CSOs.

## **3. What Next?**

The most recent official information about the status of the draft ICL was given on October 7, 2009, by the President of the Foreign Affairs Commission of the National Assembly, Mr. Roy Daza, in a radio interview. He said that they were going to discuss and approve the ICL soon, but did not specify a date. The priority at the present time is to discuss and approve the Foreign Service Act. Informal sources insist that the ICL could be approved before the end of 2010.

Some activities have proven effective in challenging the ICL and should be carried out in the future as well. For example:

- A group of NGOs has developed a national and international lobbying campaign in order to raise awareness of the consequences of the ICL. This campaign has been effective and must continue and be strengthened so it can reach a greater number of organizations and countries.

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<sup>17</sup> Taken from <http://www.aiven.org/profiles/blogs/la-propuesta-de-ley-sobre>.

<sup>18</sup> Taken from <http://www.aiven.org/profiles/blogs/la-propuesta-de-ley-sobre>.

- In addition, several seminars have been staged in the countryside and in the capital in order to inform not only NGOs but also NGO beneficiaries of the consequences of the ICL.
- Highly qualified professionals in different spheres must closely monitor this issue.
- It is necessary to strengthen NGOs and coordinate actions among NGOs.
- It is important to engage other segments of civil society, including pressure groups, syndicates, associations, churches, etc.

Eventually, if the law is ultimately passed, responsive strategies may include:

- Challenging the ICL as unconstitutional before the Constitutional Chamber of the Tribunal Supremo de Justicia; and
- Challenging the ICL before the Inter-American Commission on Human Rights, since the Judiciary in Venezuela is clearly biased in favor of the Government.

Finally, CSOs should promote and inform about forms of self-regulation, encouraging transparency and accountability.

*Article*

## **Maintaining Firm Control: Recent Developments in Nonprofit Law and Regulation in Vietnam**

**Mark Sidel<sup>1</sup>**

### **Introduction**

Vietnam remains committed to controlling the development of a nonprofit sector while gradually, and carefully, enabling some nonpolitical, service-oriented, charitable and research groups to carry out work that serves the interests of both citizens and the state. In recent years, the Vietnamese Party and government have pursued these policy goals through measures taken by government and security authorities, and by key decisions on the regulatory environment for the nonprofit sector.

This commentary outlines the key developments in nonprofit regulation in Vietnam over the past several years, particularly since a major debate on a Law on Associations ended in 2006 with a decision by Party and government officials to block adoption of the Law while continuing strict control and management of the emerging Vietnamese nonprofit community.

In recent years, Vietnam's diversifying voluntary sector has expanded to fulfill social needs from which the Vietnamese state is retreating and to play some research and advocacy roles in Vietnamese society. The emerging voluntary sector, broadly defined, now includes Party-related mass organizations, business, trade and professional associations, policy research groups, social activist and social service groups, religious groups, clans, charities, private and semi-private universities, social and charitable funds, and other institutions.

The state has sought to control and to encourage the growth of social organizations, at least partly to compensate for the inability of the state to keep pace with social needs in the reform period. At the same time, the state retains management and control over the sector at a level more detailed and specific than in many other countries, with special attention to a small number of organizations that are perceived to be potential political challenges or to harbor those who might emerge as potential challengers in political or policy terms. For the vast majority of the thousands of formal and informal organizations now active throughout the country, the Vietnamese state generally acquiesces in and even encourages their day-to-day activities, while retaining a detailed regulatory structure and making clear that the state and Party remain in control of the pace and direction of growth in nonprofit activity.

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During Vietnam's reform period that began in 1986, Party and government regulation of social organizations remained governed by regulatory documents enacted in 1957, during a period of strict control by the Party and state. Those 1957 regulations on associations severely limited rights to assemble and the ability of civic organizations to form, and the regulations adopted in the decades that followed continued that policy. Throughout this period the Party and state made special efforts to control groups that were perceived as potential political threats. In the early 1990s one such example was a veterans group called the Club of Former Resistance Fighters, which demanded better conditions for veterans and began to take their demands into the political realm. The key methods of control from the 1950s to the 1990s – and continuing to this day – have been the long and difficult processes of approval to establish a social organization or association, and the continuing control and supervision of organizations that have been approved for establishment.

There were some counter-tendencies as well, toward greater flexibility, generally for groups that the Party and state had to give more flexibility to. In 1992, for example, the then-relatively liberal Ministry of Science, Technology and the Environment was permitted to open a more flexible regulatory window for some research groups to seek a fully legalized, formal, state-recognized, and registered status. A number of urban voluntary organizations, including some of the most important policy research, social service, and social activist organizations then operating, were able to legalize under the 1992 Science and Technology Regulations and their successor, Decree 81 which now provides a protective regulatory umbrella for hundreds of science and technology research NGOs to exist.

Economic and social organizations, social and charitable foundations (funds), and other voluntary groups were also formally recognized as legal entities in the 1995 Civil Code. And in 1999 the government adopted a decree on social and charity funds that cautiously encouraged private charitable funding while maintaining strict state control over their formation and operations, using the traditional mechanism of dual control by a government management agency and by a government ministry or agency working in the particular substantive field of the fund (such as health or education).

Efforts to draft a national Law on Associations – a legislative topic of intense interest both to those who wanted to control the sector and those who wanted to facilitate it – began in the early 1990s, to replace the highly restrictive 1957 regulations on associations. Those efforts continued in various stages for nearly fifteen years, until a major debate erupted over the Law on Associations in 2005 and 2006 that provides the backdrop to recent developments in nonprofit law in Vietnam.

### **I. The 2003 Decree on the Organization, Operation and Management of Associations and Implementing Regulations (Decree 88)**

In 2003, the Vietnamese government promulgated new, detailed regulations governing the formation and operations of associations and related groups. Since 2003, Decree 88 has served as the guiding regulatory document for nonprofits in Vietnam, supplanted only in April 2010 by a revision of Decree 88, now called Decree 45, that maintained firm control over the registration, monitoring, and operation of associational groups while tweaking the regulatory framework and providing some special privileges for a small number of large, state-affiliated umbrella groups. The new Decree 45 is discussed further below.

Decree 88, in force from mid-2003 to July 2010, both restricts and facilitates associational activity with an emphasis on control. Vietnamese associational experience with Decree 88 helped to fuel growing conflict between the control orientation of the Ministry of Home Affairs, which is responsible for management of the sector, and the increasing efforts of national associations to maintain distance from government ministries. The 2003 Decree on Associations, like earlier regulation, explicitly excluded the mass organizations under the Party from its scope. These organizations – the Vietnam Fatherland Front, Labor Confederation, Ho Chi Minh Communist Youth League, Vietnam Peasants Association, Vietnam War Veterans Association, and the Vietnam Women’s Union – have long been governed directly by the Party through their own statutes.

The 2003 Decree provided long and complex processes for organizational formation (thereby discouraging most organizations from forming); broad prohibition clauses barring a wide range of activities and maintaining exceptionally wide Party and government discretion over associations; highly detailed organizational requirements; approvals needed for a wide range of organizational changes, including board and staff; restrictions on branches and on bank accounts; and, in some ways most important, retention of the tradition “dual management” system of associational governance by the state. The 2003 Decree also presaged a controversy over the scope that associations have to comment on Party and state policies, providing that associations may provide “advice and criticism on matters within the association’s scope of activities.”

In short, the 2003 Decree on Associations was a document for retained state control. In response to demands from associations and legal drafters, the 2003 Decree also included provisions for time limits on state discretion in certain stages of the formation process. Since its adoption, Decree 88 has been regarded by the Vietnamese associational sector as overly restrictive to the sector, preventing a range of organizations from registering and expanding their operations through maintenance of a highly detailed and restrictive system of approval (*cho phep*) rather than moving toward a registration system that provides associations with more flexibility. The Ministry of Home Affairs would seek to retain all of these provisions at the next stage, the drafting of the formal Law on Associations; in turn many in the associational sector would seek to weaken some of these management and control mechanisms. And the Ministry would seek to retain and strengthen these controls when the 2003 Decree was redrafted in 2008 and 2009, as discussed below.

## **II. Toward a Law on Associations, and the Aftermath of Debate on the Law**

The drafting of the Law on Associations had begun in the early 1990s, but it gathered steam again beginning in 2003 and 2004. It was a very difficult process. As the National Assembly, Vietnam’s national legislature, pointed out,

although [the Law on Associations] had been included in the legislative work programme [in 1995], up until now we have not yet promulgated any law that details the formation of associations – which is one of the fundamental rights of citizens provided in the Constitution. We might say that this is a difficult law .... Moreover, the ... development of associations and social organizations in Vietnam is very complex, [in keeping with] the level of social development. So new factors in the sphere of associations and social organizations continue to appear....

After a lengthy process of drafting by an inter-agency group headed by the control-oriented Ministry of Home Affairs, the draft Law on Associations was released by the Office of the Government in Hanoi in late 2005 for comment, setting off a firestorm of reaction from national associations representing intellectuals and business sectors. A wide range of associations opposed the draft Law because it maintained the most widely criticized elements of Decree 88 (2003) and added some new, negative features. These included

- the “dual management” form of state management and control structure by the Ministry of Home Affairs (as the key registration and supervision agency), and professional line ministries (for professional aspects of associational work);
- a complex, lengthy process for the formation of associations and other social organizations that was now termed “registration” rather than “approval” but retained most of the characteristics of the 1957 and 2003 approval systems, including wide state discretion;
- the exclusion of the six key Party-related mass organizations from the Law, prompting strong calls from other national associations either for preferential treatment for them as well, or for inclusion of the mass organizations in the draft Law;
- Geographic restrictions on associations that provided that only one association in each field could be legally formed in each locality;
- Very broad prohibited purposes and activities for associations;
- A very limited scope for advocacy and participation in public affairs, limited to (depending in part on the translation) “publiciz[ing] the objectives of the association.”<sup>2</sup>

In late 2005 and early 2006, this debate reached a point previously unknown in modern Vietnamese legislative history, when a team of specialists convened and supported by the Vietnamese Union of Science and Technology Associations (VUSTA) wrote their own alternative draft Law on Associations in response to the difficulty in forcing changes in the official draft. This appears to have been the first time in modern Vietnamese history that opposition to a government-drafted law had reached a level that a “rebellious” alternative law was formally drafted and made available for discussion.

The VUSTA alternative draft law, which relied in part on comparative legal provisions from outside Vietnam, provided different approaches on most of the issues under debate. It contained a simplified formation and registration procedure much closer to a registration (*dang ky*) model than an approval model. It further provided for a single system of state management, with specified roles for state management; a reporting mechanism for associations; and some differentiation among associations (registered and unregistered; public benefit and non-public benefit).

The alternative draft also made specific provisions for the legal treatment of “unions” or “federations” of associations (like VUSTA and the Vietnam Union of Literary and Arts

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<sup>2</sup> See Sidel and Vasavakul, *Report to the Vietnam Union of Science and Technology Associations (VUSTA) on the Draft Law on Associations* (2006).

Associations); provided for a national register of associations; would have broadened the rights of associations, particularly relating to advocacy and participation in public affairs; introduced the concept of particular privileges for a category of public benefit organizations; and provided at multiple points in the draft for more time limits for administrative action and some greater opportunities to challenge administrative action.

In 2006, the Party and government watched this unfolding and expanding conflict and – particularly in the wake of the “color revolutions” in Europe, which were unfolding at the same time – decided not to allow a Law on Associations to go forward. The Law was shelved in 2006 and is not scheduled to be reconsidered for at least several more years. The recent replacement of Decree 88 (2003) on associations by Decree 45 (2010) on associations, discussed further below, is likely to push this schedule back yet again.

Party and state control of associations and other social organizations tightened after the “color revolutions” and the debate on the Law on Associations. From 2006 to 2010, the Party and government continued to rely on the relatively strict control mechanism of the 2003 Decree on Associations. But developments accelerated in 2009 on several fronts as the Vietnamese social organization sector continued to grow and the Vietnamese Party and state sought to maintain control over the sector. These developments involved further tightening control over advocacy organizations, focusing on a particularly critical and influential research group; on developing new regulations for the registration and operations of foreign NGOs in Vietnam; and on revising the much-maligned 2003 Decree on the Organization, Operation and Management of Associations in the absence of a law on associations.

### **III. New Draft Regulations on Registration and Activities of Foreign NGOs in Vietnam**

In 2008 and 2009, the Vietnamese government drafted a new Decree on the Registration and Operation of Foreign Non-Governmental Organizations in Vietnam. The new Decree – which had not yet been promulgated as of spring 2010 – was intended to revise the much earlier, 1996 regulations governing foreign NGOs in Vietnam, Decision No. 340/TTg and the Regulations on the Operation of Foreign Non-Governmental Organizations in Vietnam (24 May 1996). ICNL provided comments on the draft Decree on the Registration and Operations of Foreign Non-Governmental Organizations to the drafters.<sup>3</sup>

The new draft Decree provoked some concern among foreign NGOs in Vietnam. In addition to some more specificity than the earlier 1996 regulations, it contained broad terms on prohibited activities for foreign NGOs, as well as a number of other vague and general terms that could lead to a substantial lack of clarity and predictability in foreign NGO activities in Vietnam. The draft Decree also broadly prohibited a full range of profit-making activities.

The draft Decree also did not take into account Vietnam’s obligations under the Bilateral Investment Treaties (BIT) that the government has signed with a number of foreign states, which may govern some aspects of its relations with foreign NGOs. ICNL urged the government to look into the specific NGO- and associational-related obligations it has undertaken in connection with those BIT agreements. For example, a number of BITs provide that once foreign

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<sup>3</sup> An English translation of the draft Decree is available at [http://www.eurochamvn.org/News/EuroCham\\_&\\_Member\\_news/Request\\_for\\_Comment\\_on\\_Draft\\_Decree\\_on\\_International\\_NGOS.html](http://www.eurochamvn.org/News/EuroCham_&_Member_news/Request_for_Comment_on_Draft_Decree_on_International_NGOS.html) and <http://www.amchamvietnam.com/2865>.



organizations have been permitted to enter, they must be accorded specific kinds of treatment. In some cases the terms of these BITs clearly include NGOs or associations.

To cite several examples, the Vietnam-Australia BIT covers “any corporation, association, partnership, trust or other legally recognised entity that is duly incorporated, constituted, set up, or otherwise duly organised” in Australia or Vietnam,<sup>4</sup> thus including, it appears, Australian NGOs within its scope. For such organizations, the BIT regulates treatment of movement of personnel, transparency of law, compensation for losses, transfer of funds, settlement of disputes, and other matters. There are similar provisions in other BITs Vietnam has signed, including with the United Kingdom<sup>5</sup> and other countries.<sup>6</sup> Vietnam, like most countries, has not yet recognized that the BITs it has signed may be applicable to foreign NGOs or associations.

The new draft decree also contained virtually no provisions on importation of goods and commodities by foreign organizations. ICNL recommended that this be clarified, primarily by raising into this new draft Decree the relatively clear and detailed provisions on importation of goods and commodities stipulated in the 1996 Guidelines for the Implementation of the Regulations on the Operation of Foreign Non-Governmental Organizations in Vietnam.

ICNL also noted that although some of the laws and regulations governing the registration and activities of foreign NGOs and their personnel in Vietnam are available on the website of the People’s Aid Coordinating Committee (PACCOM) (Vietnam Union of Friendship Organizations, VUFO),<sup>7</sup> not all are available. ICNL recommended that the government post all laws, regulations, and other legal documents (including all administrative guidance) relating to foreign non-governmental organizations in Vietnam on its own websites, including the VUFO-PACCOM website and that it make available all such legal documents (including administrative guidance) in Vietnamese and in English for web posting by the Hanoi-based NGO Resource Centre. The current haphazard availability of these legal documents is not beneficial to the functioning of the foreign NGO sector in Vietnam and is not fully transparent.

A number of other problems emerged in the new draft Decree on Registration and Operation of Foreign Non-Governmental Organizations in Vietnam, and some of those were pointed out by ICNL in its comments on the draft. They included:

- Defining “funds” and “foundations”: The definition of “social funds” and “private funds” in the Article on the scope of regulation and application (Art. 1(2)) refers to “social funds, private funds” in English, and to “quỹ xã hội, quỹ tư nhân” in Vietnamese. Assuming that this Decree applies to foreign foundations and their registration and operations in Vietnam, ICNL noted that it might be best to make clear the extent of the application to foreign foundations.
- The breadth and generality of prohibited activities: Article 4 of the draft Decree on prohibited undertakings is very wide and general and would give the authorities very broad

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<sup>4</sup> [http://www.unctad.org/sections/dite/ia/docs/bits/australia\\_vietnam.pdf](http://www.unctad.org/sections/dite/ia/docs/bits/australia_vietnam.pdf), Article 1(1)(d).

<sup>5</sup> [http://www.unctad.org/sections/dite/ia/docs/bits/uk\\_vietnam.pdf](http://www.unctad.org/sections/dite/ia/docs/bits/uk_vietnam.pdf).

<sup>6</sup> For a full list and text of all of the bilateral investment treaties signed by Vietnam, see <http://www.unctadxi.org/templates/DocSearch.aspx?id=779>.

<sup>7</sup> See [http://www.vietpeace.org.vn/express/express\\_para\\_v.aspx?id1=18&id2=134](http://www.vietpeace.org.vn/express/express_para_v.aspx?id1=18&id2=134), on the VUFO [www.vietpeace.org.vn](http://www.vietpeace.org.vn) website, under the PACCOM tab, in the “Văn bản” sub-tab.

discretion to define and punish activities, as they certainly desire. In particular, ICNL noted the dangerous breadth and generality of Article 4(1) (“Activities of religious and/or political nature or detrimental to the national interests, security and defense and/or the national solidarity of Vietnam”), and Article 4(4) (“Activities detrimental to social morals, fine habits and customs, national traditions and identity of Vietnam”).

ICNL noted that a number of these terms – such as “detrimental to the national interests,” “security,” “national solidarity,” “social morals,” “fine habits and customs,” and “national traditions and identity” – fail to provide foreign NGOs with the certainty and predictability needed, containing terms whose possible application is not foreseeable or predictable, and it urged the drafters to seek more precision in defining prohibited activities in order to give non-governmental organizations clarity and confidence as to which activities are permitted and which are prohibited.

- The prohibition on profit-making activities: The draft Decree also declares (in Article 4(2)) that prohibited activities include “profit-making activities.” That term is not defined in the draft Decree, and can lead to widespread uncertainty among foreign NGOs as to what kinds of revenue-generating activities may be permitted and what are prohibited. A key issue here is how the government wishes to regulate the distribution of profit or revenue amassed by NGOs.

For example, would the sale of local or minority handicrafts or other products, at a price above the cost of production, with the proceeds applied to an NGO’s charitable activities in Vietnam, be considered “profit-making” and thus prohibited? Would the sale of tickets to a benefit concert or dinner, at a price that gives the foreign NGO funds to conduct its activities beyond the costs of the concert, dinner, or other event, be “profit-making” and thus prohibited, even if all such proceeds were used for the organization’s charitable and humanitarian purposes?

ICNL suggested that the draft Decree either define this term more clearly and in more detail or remove it, noting that this provision in an earlier draft of the draft Decree had provided more useful specificity: In that draft, the prohibition was against “*Các hoạt động nhằm mục đích thu lợi nhuận mà không phục vụ mục đích từ thiện, nhân đạo của các dự án tại Việt Nam*” (“Profit-making activities which do not serve the charitable or humanitarian aims of a project in Viet Nam”).

- The problem of tax avoidance: Under Article 4(3) of the draft Decree, prohibited activities include those related to “tax avoidance.” This term is not defined in the draft Decree and, in the absence of any detailed provisions on the taxation of foreign non-governmental organizations in the draft, ICNL expressed concern that normal or appropriate attempts by foreign NGOs to access normally accorded tax exemptions could be defined as “tax avoidance” by overly eager administrative authorities through the exercise of too much discretion.

In addition, tax avoidance is in a very different category from “money-laundering” and “terrorism,” the two other prohibited activities listed in Article 4(3). ICNL suggested that “tax avoidance” be dropped from Article 4(3) and that clear tax provisions be added to the draft Decree, particularly with respect to the importation of goods and commodities.

- Multiple approval processes for foreign NGOs: In some sections of the draft Decree, there was substantial reference to multiple approval processes for foreign NGOs’ programs and projects (“approved by competent authorities of Vietnam”), at provincial and other

local levels, at ministry levels in Hanoi (sometimes multiple ministries), and through the Committee for Foreign NGO Affairs, also in Hanoi. ICNL suggested that a streamlining of these approval processes would be useful.

- Simplification of time limits for response on application and requirement of written notice of decision: ICNL noted that the draft Decree simplifies the time limits for response on applications and requires that the competent agency issue a written notice of decision. The 1996 Regulations specified that the competent authority “inform” the NGO “of the result” (*thông báo kết quả*) within 30 days (for an operating permit), 60 days (for a project office), and 90 days (for a representative office), not specifically requiring a written notice to the applicant NGO. The new draft Decree stipulates a time limit of 45 days for all types of applications, requiring the competent authority to “issue a written notice of the result to the applicant organization.”

- Termination of operations: The draft Decree provides in Article 17(1) for termination of operations of a foreign NGO “upon receiving a notice and/or decision of the competent authority....” It is not clear from the draft Decree whether Vietnamese law provides foreign organizations with a right to appeal such administrative decisions, or to request an opportunity for the administrative decision maker to remedy an error. If so, ICNL recommended that this Article should be revised to provide for those protections, and, if not, those protections should be considered. And the draft of Article 17(2) provided that upon termination, foreign NGOs shall wind up their affairs within sixty days – too short a period for most NGOs to terminate activities and end significant programs.

- Importation of goods and commodities: The draft Decree provided in Article 24 that importation of “necessary office equipment and supplies, vehicles and spare parts, [and] personal belongings” is subject to “current regulations of Vietnam.” ICNL called that provision vague and general and, in particular, noted that it did not reference or include the tax exemption provisions of the Guidelines for the Implementation of the Regulations on the Operation of Foreign Non-Governmental Organizations in Vietnam (7 August 1996) (Implementation Guidelines), which provide implementing guidance for the 1996 Regulations.<sup>8</sup> ICNL recommended that a revised version of the 1996 tax guidance be incorporated into the new Decree.

- Implementation and execution: The draft Decree (Article 31) stipulated that Decision No. TTg (May 1996) and the related Regulations on the Operation of Foreign Non-Governmental Organizations in Vietnam would be superseded by the new draft Decree. At the same time a number of other legal and administrative documents have been issued under or related to Decision No. 340/TTg and on the registration and operations of foreign NGOs in Vietnam since 1996. These include the August 1996 Implementation Guidelines referred to above; Decision No. 64/2001/QĐ-TTg on the Issuance of the Regulations on the Management and Utilization of Aid from International Non-Governmental Organizations;<sup>9</sup> and other legal documents.

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<sup>8</sup> An English text of the Implementation Guidelines may be found at <http://www.ngocentre.org.vn/node/69> (under Legal Documents). The Vietnamese text is at [http://www.vietpeace.org.vn/express/express\\_detail\\_v.aspx?id1=18&id2=134&id3=309](http://www.vietpeace.org.vn/express/express_detail_v.aspx?id1=18&id2=134&id3=309).

<sup>9</sup> Decision No. 64/2001/QĐ-TTg is available in English at <http://www.ngocentre.org.vn/node/69> (under Legal Documents), and in Vietnamese at

ICNL recommended that the government make clear whether the August 1996 Implementation Guidelines remain in effect, perhaps through direct reference to those and to other implementation guidelines in the draft Decree. Separately, and for the clarity of foreign NGOs and donors, the government may wish to address the continued applicability of Decision No. 64/2001/QĐ-TTg on the Issuance of the Regulations on the Management and Utilization of Aid from International Non-Governmental Organizations, or to clarify whether a revision of Decision No. 64/2001/QĐ-TTg is underway.

As of May 2010 the draft Decree on the Registration and Operation of Foreign Non-Governmental Organizations in Vietnam had not yet been issued, and there appeared to be no clear timetable for its promulgation.

#### **IV. Cracking Down on Particular Organizations, and on Policy Commentary and Criticism by Independent Groups: Decision 97 and the Vietnam Institute of Development Studies (VIDS)**

Since its founding in 2004, the Vietnam Institute of Development Studies (IDS) angered some senior officials in the Party and government for its wide-ranging discussions of development policy and commentary on government policy. But the Institute was difficult to attack directly, since the board was composed of some of Vietnam's leading intellectuals and technocrats and the Institute operated under the implicit sponsorship of former Prime Minister Vo Van Kiet. The Institute had been formed directly by these individuals under the relatively liberal regulations for forming science and technology research organizations, not under the Vietnam Union of Science and Technology Associations (VUSTA) or another umbrella.

In 2008, Vo Van Kiet died, and later in 2008 and in 2009 the Party and government began moving against IDS. In July 2009, the Prime Minister issued Decision 97/2009/QĐ-TTg limiting the areas in which individuals (like those who established the Institute of Development Studies) were allowed to form science and technology research, service, and other organizations. Though Decision 97 provided a long list of areas available for organizations to work in, it was most notable for the areas it omitted, making it, in effect, illegal for independent organizations (organizations established by individuals without the umbrella provided by Decree 81 or Decree 88) to work in those spheres.

Those prohibited areas included, for example, economic policy, public policy, political issues, and a range of other sensitive areas. Permitted areas of work included a range of fields and subfields in the natural sciences (including mathematics, computer science and information, physics, chemistry, mechanics, and other scientific fields, including ecology), social sciences (including psychology, economics and business, and sociology, but not including economic policy), the humanities (including history, philosophy, linguistics, literature, cultural studies, arts, cinema, radio, and television, but not political issues or public policy), engineering and other technical fields, health and medicine, agriculture, science and technology services, and information (including intellectual property and technology transfer).

Beyond the prohibition of work in some areas, Decision 97 also sought to limit the rights of such organizations to engage in commentary and criticism of government policy. Such organizations, the Decision provided (Article 2(2)), "may only conduct activities within the areas

under the List promulgated with this Decision. If they have feedback (*phản biện*) on the line, guidelines, or policies of the Party or the State those views must be provided to Party or State agencies with jurisdiction over such issues, and may not be released publicly....”

This was part of a broader set of steps to limit the ability of associations and other groups to express commentary or criticism of Party and state policies, a set of restrictions on the right to provide such views or commentary (*phản biện*). Such restrictions and making commentary and criticism dependent on Party and state discretion are also reflected in the revision of Decree 88 on the Organization and Management of Associations, discussed below.

Decision 97 also required national and local government agencies responsible for licensing science and technology groups (like the Institute of Development Studies) to review, revoke or re-register all such organizations, explicitly requiring such authorities to revoke organizations that do not comply with the Decision. The Decision took effect on September 15, 2009.

The Institute of Development Studies was one of the few such individually formed groups undertaking work in areas outside those permitted under Decision 97. It was clear in Hanoi that Decision 97 was directed against the Institute, as well as against the expression of policy views and commentary by other groups as well in its restriction of that right.

Facing this challenge, and knowing that the goal of the Decision was to terminate the Institute, the Institute challenged the validity of the Decision but also chose to go out of business of its own accord in September 2009 rather than have the government declare it invalid.<sup>10</sup> The director of the Institute, the well-known economist Nguyen Quang A, directly challenged the government’s authority to issue the Decision without an opportunity for comments and public notice, and threatened to bring the issue to the National Assembly.

What followed was correspondence on the validity of the Decision between Professor A and the Minister of Justice, who affirmed the legality of the Decision in the view of his Ministry.<sup>11</sup> That dialogue did not change the result – the Institute remained shuttered, and Decision 97 remained in effect – but the sight of a Vietnamese intellectual forcing the government, through the Minister of Justice, into such direct correspondence on a sensitive issue was perhaps unprecedented in modern Vietnamese politics.

The result, however, is unfortunate for the development of more independent policy commentary groups and think tanks in Vietnam. In effect, groups have been barred from work in certain important policy fields, and policy commentary itself has been reduced by Decision 97 to commentary that the Party or government itself requests and that is within the specific ambit of the work of the commenting organization. Decision 97 applies to the independently established research groups, but the Party and state’s policy seems clear, and broader – to discourage the independent commentary activities of some analytical policy groups.

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<sup>10</sup> For news reports on the closure of IDS, see <http://news.bbc.co.uk/2/hi/asia-pacific/8257061.stm>; <http://abcnews.go.com/International/wireStory?id=8576667>; <http://www.forbes.com/feeds/afx/2009/09/15/afx6885790.html>.

<sup>11</sup> For this correspondence and much more on the Decision 97 controversy, see <http://boxitvn.blogspot.com/> and <http://bauxitevietnam.info/>. The description of these events in this paper is an abbreviated version of a longer discussion by the author.

V. **Updating and Maintaining Control in Associational Regulation: Decree 45 (2010) on the Organization, Activities and Management of Associations**

In the absence of a Law on Associations, and in response to calls from government regulators for a more detailed regulatory document, from associations, the World Bank and other donors for a firmer regulatory footing, in 2009 the Ministry of Home Affairs completed a draft revision of the 2003 Decree on the Organization, Activities and Management of Associations under which most Vietnamese associations are registered (in addition to Decree 81 on science and technology research groups). The Ministry quietly released the draft revision for comments in the fall of 2009 preparatory to the promulgation of the new Decree, as required by Vietnamese law, and a number of critical commentaries were submitted by Vietnamese groups. The revised Decree 88, now Decree 45 (2010), was promulgated on April 21, 2010, and takes effect on July 1, 2010. The new Decree 45 (2010) continues to govern the registration, operations, activities, and management of a wide range of associational groups at the national, provincial, municipal, and sub-provincial level.<sup>12</sup>

Some of the key points of the new Decree 45 (2010), and the issues with this revision of Decree 88 (2010), are as follows:<sup>13</sup>

- Establishing a new category of associations, the “associations with special characteristics.” Decree 45 (2010) establishes a new category of associations, termed associations with “special characteristics” (*Hội có tính chất đặc thù*, in Articles 33-35). These are the major national umbrella organizations of associations that were not clearly stipulated in the earlier Decree 88. These umbrella groups (such as the Vietnam Union of Science and Technology Associations (VUSTA) and others) have long sought privileged legal protection akin to the special status given the mass organizations under the Party, like the Vietnam Women’s Union and the Peasants’ Union. This new category would replace a set of organizations that was defined in the Vietnamese Civil Code and replace it with a term and category of organization that is unrecognized in the Civil Code.<sup>14</sup>

- Privileges of the “associations with special characteristics.” Decree 45 (2010) would give these associations with “special characteristics” privileges that include “participation in formulating mechanisms and policies” directly related to their associational work, and participation in “consulting, providing feedback, and examining” various policies, programs, projects, and plans of government agencies “on issues within the sphere of activities of such associations in accordance with regulations of the Prime Minister.” Decree 45 (2010) also

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<sup>12</sup> For the Vietnamese text of Decree 45 (2010), see <http://legal.khaitri.vn/Index.asp?n=74655>, <http://www.icnl.org/knowledge/library/dlogin.php?file=Vietnam/Decree45.pdf>, and other sites.

<sup>13</sup> There are numerous other differences between the new Decree 45 (2010) and the original Decree 88 (2003), but space permits only a discussion of some of the key issues here. The author is preparing a longer paper outlining virtually all the significant differences.

<sup>14</sup> See *Một số góp ý cho Nghị định mới về Hội* (Some suggestions for the new Decree on Associations) (10 November 2009). The author of this commentary has not been publicly identified. The associations with special characteristics include the Vietnam Union of Science and Technology Associations (VUSTA), Vietnam Lawyers Association (VLA), Vietnam Union of Literary and Arts Organizations (VULAA), and a number of others. The mass organizations (to which Decree 45 (2010) does not apply), including the Vietnam Fatherland Front, Vietnam Confederation of Trade Unions, Ho Chi Minh Communist Youth League, Vietnam Peasants Union, Vietnam Veterans Association, and Vietnam Women’s Union. Decree 45 (2010) also does not apply to religious groups.



provides that the government will continue to provide budget funding to these groups (Arts. 34 and 35).<sup>15</sup>

The issues of the associations with “special characteristics” have provoked more discussion in Vietnam than perhaps any other aspect of the new Decree 45 (2010). In effect, this would satisfy demands by these umbrella groups for special recognition by creating a multi-tiered stratification of associational entities – with Party-related mass organizations (such as the Women’s Union) at the top, outside this Decree; the “special purpose” groups in a special category within Decree 45 (2010); and the rest of the associational sector in a third group with fewer privileges and rights. The problems in this approach have been outlined by Professor Hoang Ngoc Giao, a Vietnamese academic with long experience on these issues.

“Receiving subsidies from the State in this way, this kind of organization may continue to be subservient to and suffer the influence of state agencies.... When civil society is stratified in this way, [this part of the sector] can be increasingly ‘administrativized’ and ‘statified’ in their activities ... making it more difficult for them to play a positive role in the development of the country.”

In addition, the decision as to which groups have this special status, and how they obtain it, is left by the revised Decree to the discretion of the Prime Minister.<sup>16</sup>

- Continuing, significant obstacles and multiple steps and approvals to establishing associations: Some Vietnamese commentators perceive few positive changes in Decree 45 (2010) to the complex and bureaucratic requirements for establishing and operating an association that were stipulated in the original Decree 88 (2003). In particular, formation of an association under Decree 45 (2010) requires a certain number of founding members; and the Minister of Home Affairs will continue to provide detailed regulations and thus wield wide discretion over the conditions for establishing associations. According to one prominent Vietnamese commentator, this provision “gives too much discretion to the Minister of Home Affairs. There is no mechanism to supervise those regulations of the conditions for forming an association ... and additional new regulations making it much more difficult to form associations.”<sup>17</sup>

The new Decree 45 (2010) continues to provide that the process of formation and registration of associations will be highly regulated by the Ministry of Home Affairs, local governments, and other government agencies. Some procedures have changed from Decree 88 (2003), but firm control remains. In general terms, formation and registration of associations will now require a minimum number of individuals to formally seek approval, ranging from one hundred signatories for national associations to fifty individuals at the provincial level, to twenty at the county level and at least ten at the township level (Art. 5). An establishment committee is

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<sup>15</sup> Professor Hoàng Ngọc Giao, *Một số nhận xét về Dự thảo Nghị định thay thế Nghị định 88/2003/NĐ-CP Quy định về tổ chức, hoạt động và quản lý hội* (Some considerations on the Draft Decree to substitute for Decree 88/2003/ND-CP on the organization, activities, and management of associations) (11 November 2009).

<sup>16</sup> Hoang Ngoc Giao, *supra* note 15. See also Some suggestions for the new Decree on Associations, *supra* note 14, which reflects the view that the associations with special characteristics would, for most purposes, have no additional real powers beyond ordinary associations, though the Decree stratifies organizations and could create major differences among them.

<sup>17</sup> Hoang Ngoc Giao, *supra* note 15.

still required, with minimum numbers for the membership of that committee at the national, provincial, and lower levels (Art. 6(1)-(3)). That establishment committee must then be formally recognized by a national, provincial, or lower level government ministry or bureau, depending on the scope of the association (Art. 6(5)). The extension of authority to provincial and lower levels of government is an attempt to relieve the central government of some burdens for local groups, but also to bolster control of associational formation throughout the vertical networks of the state. The government's decision on recognizing an establishment committee must be taken within twenty days, and if the committee is rejected then written reasons must be provided (Art. 6(5)). The government's decision on whether or not to approve the formation of an association, after the establishment committee has submitted the many and detailed required documents (Arts. 7, 8), must be taken within sixty days, and written reasons are to be given if the approval is refused (Art. 9). In addition, the establishment committee must be recognized by the ministry or other agency working in that professional arena, a continuation of the "dual management" system of the past. No standards are provided for that recognition, nor for dealing with groups that cross over various fields of work and whether such groups must seek recognition from all the relevant ministries.<sup>18</sup>

Thus the government has, at the very least, two formal steps in which it can decline to approve the formation and registration of an associational entity, along with other requirements for formation that may discourage some groups from applying. If approval is granted, the association has ninety days from the date of approval to hold its establishment congress (Art. 10) with specified requirements (Art. 11) and reporting to the government (Art. 12) on that meeting. The government retains approval rights over the organizational charter approved at that meeting (Art. 13), and the Decree requires pre-reporting to the government before annual meetings of associations (Art. 24). The over-regulation of associational formation does not end there: After the relevant government agency or agencies have agreed to permit the formation of an association and after the organization of its founding meeting, the bylaws (charter) of the association must also be approved by the relevant agency or agencies. As a prominent Vietnamese commentator points out acerbically, "having had the decision to [permit] the formation of an association, the bylaws must still be reviewed to determine if they violate the law or not! This can only be another means to delay formation, without any standards being provided to government officials to guide their discretion."<sup>19</sup>

- Continuing constraints on speech and advocacy. The new Decree 45 (2010) continues the process of limiting associational speech and advocacy rights. For example the earlier Decree 88 (2003) provided associations with the right to "protect the lawful rights and interests of the association and its members." Decree 45 (2010) subtly limits that right by providing associations with the right to "protect the lawful rights and interests of the association and its members that are consistent with the guidelines and purposes of the association." (Art. 23(4)).

The earlier Decree 88 (2003) allowed associations to engage in "consultations and feedback on issues within the association's scope of activities at the request of organizations and individuals," itself a limitation of the feedback and commentary role to issues "within the association's scope of activities." The new Decree 45 (2010) permits organizations to

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<sup>18</sup> Hoang Ngoc Giao, *supra* note 15.

<sup>19</sup> Hoang Ngoc Giao, *supra* note 15.



“participate in programs, projects, research topics, consultations, feedback and social assessment at the request of government agencies....” (Art. 23(7)). This provision is intended to limit the commentary, advocacy, and feedback role to circumstances in which such views have been requested by government agencies.

- Continuation but perhaps also some blurring of the much-maligned “dual management” of associations by multiple government agencies. One possible improvement in the new Decree 45 (2010) – though how this will develop in practice is not at all clear – is that the new Decree fails to clarify to what degree full “dual management” of associations by the Ministry of Home Affairs and the relevant professional ministry at the national or local levels continues or not under the new regulations. Government control remains very strong, to be sure, including over formation, approval of charters, activities, leadership, merger, dissolution, changes of names, and other issues. And “dual management” certainly persists in some ways, for example in the requirement that the professional line ministry or agency is required to approve the establishment committee for an association seeking permission to form and register (Art. 6(5)).

But particularly in the post-establishment, post-registration phases of organizations, the lines of authority between the Ministry of Home Affairs (as registration and supervision agency) and professional line ministries or lower-level government agencies remain somewhat unclear in Decree 45 (Arts. 14, 37). The continuing strength of “dual management” will need to be assessed in the months and years ahead. Dual management of associations has long been criticized by the Vietnamese associational sector as imposing significant burdens on associations and keeping them highly dependent on the state, and on professional line ministries and local bureaux unprepared to undertake such supervision. Vietnamese organizations will be watching the possible evolution of dual management very carefully indeed.

As noted above, Decree 45 (2010) on the Organization, Activities and Management of Associations was just released in late April 2010. Only some of its key provisions are discussed above, and further judgement on Decree 45’s impact will need to await further analysis and the practice of government management and control in Vietnam.

## **VI. New Regulations on the Management and Use of Foreign Non-Governmental Aid: Decree 93 (2009) and Circular 7 (2010)**

The government promulgated the Regulations on the Management and Use of Foreign Non-Governmental Aid in October 2009, officially known as Decree 93/ND-CP,<sup>20</sup> followed by a detailed Circular providing implementing rules on this topic at the end of March 2010.<sup>21</sup> The new

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<sup>20</sup> The official English translation of the Regulations on the Management and Use of Foreign Non-Governmental Aid in October 2009 (Decree 93/ND-CP) are at the Official Gazette of the Socialist Republic of Vietnam (Cong Bao), November issue 01-02, 2009, reprinted at <http://www.linvn.org/cms/upload/FCKFile/file/Workshop/2009-%20Decree%2093.%20replace%20Decision%2064.%20eng.pdf>. The Vietnamese original text of the Regulations is available at <http://www.linvn.org/cms/upload/FCKFile/file/Workshop/2009-%20Decree%2093.%20replace%20Decision%2064.%20vnese.pdf>, among other sites.

<sup>21</sup> The implementing rules, Circular 7, are at <http://www.linvn.org/cms/upload/FCKFile/file/Workshop/2010%20-%20Circular%2007.%20receiving%20foreign%20aid.%20vnese.pdf>.

Regulations on the Management and Use of Foreign Non-Government Aid replace simpler regulations first promulgated in 2001 (Decision 64).

The new Regulations and implementing rules maintain and enhance state control over foreign non-governmental aid to Vietnam in expected ways, with more detailed provisions than in the past. The process of implementation will be crucial to understanding the full force and implications of these new Regulations, and that process is just beginning.

The new Regulations cover “non-refundable aid provided for not-for-profit purposes by donors for Vietnam to achieve development and humanitarian objectives.” (Art. 1(1)) “Donors” whose work is covered by these Regulations include “foreign non-governmental organizations and other foreign organizations and individual, including foreign investment groups and companies and overseas Vietnamese community that respect and observe Vietnamese law and have goodwill and directly provide non-refundable aid to support Vietnam’s socio-economic development and humanitarian objectives.” (Art. 1(2))

Eligible recipients include Vietnamese government, Party, legislative and other state agencies, mass organizations under the Party and government, officially recognized associations and other non-state actors, and organizations established under Decree 88, Decree 81, and other documents governing the burgeoning non-governmental (or “less-governmental) community in Vietnam, as well as businesses “providing public products and services” as defined by government regulation (Art. 1(4)).

The Regulations reassert government management and control over foreign non-governmental aid; require that such aid “comply with Vietnamese law and commitments with donors which have been approved by competent authorities”; notes that where “donors’ aid regulations or conditions differ from Vietnamese law,” Vietnamese law prevails; requires the government and Vietnamese institutions to refuse aid that “affect[s] political security and social order and safety or infring[es] upon interests of the State or lawful rights and benefits of organizations or individuals.” (Art. 2)

The Regulations go on to prescribe approval mechanisms for programs, projects and other forms of aid in Vietnam, generally restricting approval agencies to central Party and government units and provincial people’s committees (Art. 4) and not permitting the conclusion of program or project aid documents until the designated government agencies have approved such activities (Art. 6). Tasks are set for approval agencies and aid management agencies (Art. 8), as well as requirements for approval (Art. 9). Appraisal and approval mechanisms are stipulated (Arts. 10-12), with the Ministry of Planning and Investment playing a key role in this area. Approval levels are set for different amounts and types of aid at the levels of the Prime Minister; ministries and other government agencies; provincial people’s committees; and the Fatherland Front (for some forms of emergency aid) (Art. 13).

Additional provisions govern the administration of foreign non-governmental aid, also with an emphasis on state overall control over the process (Arts. 17-19). No detailed provisions are made for the tax treatment of donor aid, only a stipulation that “taxes on FNG aid amounts comply with current law regarding taxes on aid...” (Art. 20). Several articles govern monitoring and evaluation of aid implementation (Arts. 24-28), with an emphasis on reporting to state agencies, particularly the Ministry of Planning and Investment, Ministry of Finance, and the interagency Committee on Foreign Non-Governmental Organizations (Arts. 29-41).

## **Conclusion**

The Vietnamese Party and government are intent on establishing a differentiated regime of nonprofit regulation that encourages the growth of some service-oriented and some other groups that are viewed as contributory, while always under government observation and supervision. At the same time, the government has focused particular attention and stricter regulation on organizations that it views as a threat in one way or another – organizations that carry out independent and public commentary and criticism of Party and state policies, for example, and of course dissident organizations. The state also strictly regulates the religious sector, an arena outside the scope of this article.

Recent developments in Vietnam indicate clearly that the Party and state are working to implement this differentiated regime of nonprofit regulation. The Party and state decided not to proceed with a Law on Associations, in part because of concern for the flexibility and autonomy the law might provide to nonprofit groups. The government has revised the primary regulatory document governing the nonprofit sector through the issuance of Decree 45 (2010) on associations, and through that process has made some control provisions more strict. The Party and state have sought to limit commentary and criticism of policy, for example, both through regulation on the commentary process and by closing a key policy think tank. And the government has sought to provide new regulation of the foreign NGO sector as well. On the ground, the numbers and the range of activities of associations, science and technology research groups, other social organizations, clubs, and other entities continues to grow. These developments, and the Party and government's implementation of its mandate to control and manage this rapidly expanding sector, will bear close watching in the months and years ahead.

Article

## The NGO Law: Azerbaijan Loses Another Case in the European Court

Mahammad Guluzade and Natalia Bourjaily<sup>1</sup>

### Introduction

On 9 October 2009, Azerbaijan lost a case in the European Court of Human Rights (ECHR) under Article 11 of the European Convention on Protection of Human Rights and Fundamental Freedoms (Convention). The case, *Tebieti Mühafize Cemiyeti and Israfilov v. Azerbaijan*, addresses the dissolution of a registered public union.<sup>2</sup> This is the fifth time since Azerbaijan's ratification of the Convention in April 2002 that the ECHR has issued a decision against Azerbaijan on a case involving the freedom of association under Article 11 of the Convention. The purpose of this article is to provide a review of certain problems with Azerbaijani legislation relating to nongovernmental organizations (NGOs) that were identified in the case *Tebieti Mühafize Cemiyeti and Israfilov v. Azerbaijan*, and to recommend how to improve Azerbaijani legislation based on international law and best practices.

### History

Since 2002, citizens of Azerbaijan have submitted hundreds of applications to the ECHR. Many citizens faced problems with registering an NGO with the Ministry of Justice, as the authorized registration body. Domestic courts have not been supportive of NGOs and their founders in the lawsuits against the registration body. Frustrated founders have submitted several appeals for ECHR consideration relating, in particular, to problems with NGO registration. The ECHR swiftly resolved these cases with Azerbaijan losing all four considered cases: *Ramazanova v. Azerbaijan*,<sup>3</sup> *Ismailov v. Azerbaijan*,<sup>4</sup> *Nasibova v. Azerbaijan*,<sup>5</sup> and *Aliyev and others v. Azerbaijan*.<sup>6</sup> In all of these cases, the ECHR found Azerbaijan to be in violation of Article 11 (freedom of association) of the Convention. These four successful attempts of local NGOs to restore justice gave hope to many organizations having similar problems. Many similar cases relating to problems with registration of NGOs have also been submitted to the ECHR. As a result, the Government of Azerbaijan has improved the process of NGO registration, and has begun to settle issues relating to registration in favor of NGOs and their founders.

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<sup>2</sup> *Tebieti Mühafize Cemiyeti and Israfilov v. Azerbaijan*, 8 October 2009, application no. 37083/03.

<sup>3</sup> *Ramazanova and Others v. Azerbaijan*, 1 February 2007, Application no. 44363/02.

<sup>4</sup> *Ismailov v. Azerbaijan*, 17 January 2008, Application no.4439/04.

<sup>5</sup> *Nasibova v. Azerbaijan*, 18 October 2007, Application no.4307/04.

<sup>6</sup> *Aliyev and others v. Azerbaijan*, 18 December 2008, Application no.28736/05.

The ECHR appeared to be an especially effective mechanism to address issues with realization of the freedom of association in Azerbaijan. We hope the most recent ECHR case *Tebieti Mühafizə Cəmiyyəti and İsrəfilov v. Azerbaijan*, and the articles and analysis coming in its wake, will contribute to improving the legislation relating to dissolution of NGOs in Azerbaijan.

#### *Azerbaijani legislation on dissolution of NGOs*

The Constitution of Azerbaijan delegates the power to dissolve an association exclusively to courts.<sup>7</sup> In accordance with article 59 of the Civil Code of Azerbaijan, a legal entity may be dissolved by a court order, if:

- the legal entity was established with violation of legislation; or
- the legal entity engages in activities without the required permit (license) or in activities prohibited by law, or if it otherwise commits repeated or grave breaches of law, or if a public association or foundation systematically engages in activities that are contrary to the aims set out in its bylaws, as well as in other cases provided by law.

The Ministry of Justice, under Azerbaijani law, does not have authority to dissolve an NGO, including an association. However, the Ministry of Justice is required to supervise activities of NGOs to ensure that they comply with “objectives of the NGO Law.”<sup>8</sup> When it determines that an NGO violates a provision of the NGO Law or other legislation, it notifies the organization in writing, instructing it to correct the violations. If an NGO is notified more than twice in one year for violations, the Ministry of Justice may apply to court for dissolution of the NGO.<sup>9</sup> An NGO has the right to appeal a Ministry of Justice’s notification in court. However, in practice courts usually side with the Ministry of Justice taking into consideration only the Ministry’s findings and ignoring other facts presented by an NGO, such as whether a violation of a law took place in reality.

#### *Case review*

*Tebieti Mühafizə Cəmiyyəti* (TMC or Association), one of the first NGOs registered in 1995, operated until its dissolution by court in 2002. The local court justified its decision to dissolve the Association by arguing that its activities did not comply with the requirements of its own by-laws and domestic law. Specifically, it had not convened a lawful general assembly of its members from the moment of establishment. Before sending a dissolution request to the court, the Ministry of Justice issued several notifications to TMC in which the following violations of applicable law were listed:

- 1) not all members of the Association had been properly informed about the general assembly and thus had been unable to participate in it;
- 2) the Association’s local branches had not been equally represented at the assembly;
- 3) current membership records had not been properly kept and it was impossible to determine the exact number and identity of members; and

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<sup>7</sup> Article 58 (IV), Constitution of the Republic of Azerbaijan, 1995.

<sup>8</sup> Article 31.2. of the NGO Law.

<sup>9</sup> Article 31.4 of the NGO Law.

- 4) local branches of the Association had not held any regular local assemblies of members, and, as a result, members were unable to directly participate in governance.<sup>10</sup>

Before the ECHR, the Government of Azerbaijan stated that involuntary dissolution was the only sanction available under the domestic law against associations engaging in activities “incompatible with the objectives” of the NGO Law.

The European Court stated in the *TMC* case:

A mere failure to respect certain legal requirements on internal management of non-governmental organizations cannot be considered such serious misconduct as to warrant outright dissolution. [...] The immediate and permanent dissolution of the Association constituted a drastic measure disproportionate to the legitimate aim pursued. Greater flexibility in choosing a more proportionate sanction could be achieved by introducing into the domestic law less radical alternative sanctions, such as a fine or withdrawal of tax benefits.<sup>11</sup>

The ECHR underlined the following shortcomings of the NGO legislation of Azerbaijan in the *TMC* case:

- (i) The circumstances in which involuntary dissolution can be applied are not precisely defined;
- (ii) There are no alternative sanctions against associations engaging in activities “incompatible with the objectives” of the NGO Law; and
- (iii) There are no detailed rules governing the scope and extent of the Ministry of Justice's power to intervene in the internal management and activities of associations, or minimum safeguards concerning, *inter alia*, the procedure for conducting inspections by the Ministry or the period of time granted to public associations to eliminate any shortcomings detected.<sup>12</sup>

In this article, we will address each of the shortcomings identified by the ECHR and review relevant Azerbaijani legislation in light of international law and best practices.

*(i) The circumstances in which involuntary dissolution can be applied are not precisely defined*

In Azerbaijan, the legal provisions on involuntary dissolution of public associations are worded in rather general terms and may give rise to varying interpretations. For example, Article 59 of the Civil Code states that involuntary dissolution of a public association may take place if “the legal entity ... commits repeated or grave breaches of law, or if a public association or foundation systematically engages in activities that are contrary to the aims set out in its by-laws, as well as in other cases provided by law.”

Remarkably, the list of reasons for involuntary dissolution of NGOs is longer than the list for other legal entities. A public association and a foundation, but not a business, must be dissolved if it systematically engages in activities that are contrary to the aims set out in its bylaws, as well as in other cases provided by law. Taking into consideration that the law does not

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<sup>10</sup> Section 16, *Tebieti Mühafizə Cəmiyyəti and Israfilov v. Azerbaijan*, supra note 2.

<sup>11</sup> § 82, *Tebieti Mühafizə Cəmiyyəti and Israfilov v. Azerbaijan*, supra note 2.

<sup>12</sup> §§ 63-64, *Tebieti Mühafizə Cəmiyyəti and Israfilov v. Azerbaijan*, supra note 2.

set any limits on the purposes for which an NGO may be established, other than that the primary aim shall not be “generating profit,”<sup>13</sup> NGOs may be set up and operate for any legitimate purpose. From the legal perspective, it is irrelevant how the aim of an NGO is defined in its own bylaws. The law does not (and may not) set any requirement on how the aim of an association may be defined. Therefore, it is common and appropriate that an aim is defined very broadly, such as “achieving public good” or “improving health care.” Even if an NGO’s bylaws set as a specific primary aim, for example, an “increase in literacy,” would it be illegal for an NGO to engage in activities other than educational activities? Certainly, an NGO should not be punished for engaging in legal activities simply because such activities are not explicitly spelled out in its bylaws.

Moreover, the NGO Law in Article 31.2 obliges NGOs to comply with the “aims” of the NGO Law, as defined in Article 1 of the Law. Obeying the “aim” of the law, as defined, not only the provisions of the law, is a confusing requirement impossible to consistently implement.

These confusing provisions allowed the Ministry of Justice to request the dissolution of the association for failure to organize its internal management, in contravention of international law and best practices.

We will briefly review the actual violations that were cited in the Ministry of Justice notices to the TMC and served as the basis for its dissolution. While states can set limitations on the freedom of association, including reasons for involuntary dissolution of an association, the list of such limitations must be short and well-defined. Freedom of association is not absolute<sup>14</sup> and may under specific circumstances be restricted. Article 11, Paragraph 2 of the Convention sets the conditions for possible limitations. Restrictions on freedom of association may be allowed only if:

- a) the restriction is prescribed by law;
- b) it pursues a legitimate aim; and
- c) it is necessary in a democratic society.

All three conditions must be fulfilled cumulatively. Should any one of them not be met, the implied restriction will be considered in violation of the Convention.<sup>15</sup> It is clear that, for example, when an association misses its deadline for conducting a members meeting, it does not create a danger to a democratic society, and therefore, there is no necessity to restrict the activities of the association in order to preserve the democracy. Such a violation of internal governance rules may not be used as the basis for involuntary dissolution of an association, as such an action is an impermissible restriction of the right to freedom of association.

In addition, none of the violations listed in the Ministry’s notification to the TMC serving as the basis for dissolution comply with the technical condition of “being prescribed by law,” not to mention others. At the time of dissolution of TMC, Azerbaijani law did not regulate such

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<sup>13</sup> Article 2.1 of the NGO Law.

<sup>14</sup> One of the absolute rights guaranteed by the Convention is the right to freedom from torture, inhuman and degrading treatment or punishment embodied in Article 3 of the Convention. It is not subject to any limitations.

<sup>15</sup> *On the Right to Freedom of Association Under the European Convention on Protection of Human Rights and Fundamental Freedoms*, Zvonimir Mataga, LL. M, Legal Adviser at the European Court of Human Rights; Strasbourg, October 2006.

issues as (1) how properly to inform members about participation in a general meeting or assembly, as the highest governance body of an association; or, (2) requiring equal representation of all association branches at the general assembly; or (3) how to keep membership records properly; or (4) setting the requirement for local branches of an NGO to call their own assemblies. In fact, Azerbaijani law complied with international law and practice by not regulating these issues. It was the intervention by the Ministry of Justice in the internal activities of the NGO that the ECHR identified as a problem. The ECHR considered that “it should be up to the association itself to determine the manner in which its branches or individual members are represented in its central governing bodies. Likewise, it should be primarily up to the association itself and its members, and not the public authorities, to ensure that formalities of this type are observed in the manner specified in the association's charter.”<sup>16</sup>

Neither of the violations cited in the Ministry of Justice’s notification, which served as the basis for the local court’s decision to dissolve TLC, met the legal conditions, and therefore, could not serve as the basis for dissolution of TLC.

(ii) *There are no alternative sanctions against associations engaging in activities “incompatible with the objectives” of the NGO Law*

Azerbaijani law contains only one sanction, dissolution, for associations that violate the NGO Law or their own bylaws. The issuance of more than two warnings in a year suffices for the launch of a dissolution lawsuit before the domestic court.

In the *Tebieti Mühafizə Cəmiyyəti*, case the European Court underlined that “[...] involuntary dissolution was the only sanction available under the domestic law against associations engaging in activities ‘incompatible with the objectives’ of the NGO Act” and called this sanction “drastic.” Indeed, the Council of Europe Recommendations on the legal status of NGOs in Europe provide for dissolution of an NGO only in case of “serious misconduct.”<sup>17</sup> Regrettably, the Azerbaijani NGO Law does not differentiate the seriousness of misconduct in the case of infringement of an NGO’s bylaws or legislation. For these purposes, Azerbaijan may benefit from the positive experience of other countries that do provide for alternative sanctions, such as fines payable by the manager of an NGO, for NGOs acting against the legislative acts described below.

In regards to international common practices, NGOs, including public associations, and their managers are subject to similar sanctions as other entities. The general rule is that if a sanction does not apply to a business, for example, for the failure to gather a meeting of shareholders, no penalties should apply to NGO for the same failure. Interested persons—shareholders in the case of a business, and members in the case of an association—may always bring a civil lawsuit if their interests or rights have been violated. Other than the dissolution of an entity, as a last-resort punishment against the most serious violations, the most common sanctions are fines against the management of either a business or an NGO.

(iii) *There are no detailed rules governing the scope and extent of the Ministry of Justice's power to intervene in the internal management and activities of associations, or minimum safeguards*

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<sup>16</sup> § 78, *Tebieti Mühafizə Cəmiyyəti and Israfilov v. Azerbaijan*, supra note 2.

<sup>17</sup> § 44, *Tebieti Mühafizə Cəmiyyəti and Israfilov v. Azerbaijan*, supra note 2.



*concerning, inter alia, the procedure for conducting inspections by the Ministry or the period of time granted to public associations to eliminate any shortcomings detected.*<sup>18</sup>

As the ECHR noted, the NGO Law has afforded the Ministry of Justice rather wide discretion to intervene in any matter related to an association's existence.<sup>19</sup> The NGO Law does not explicitly provide the Ministry of Justice with authority to audit NGOs. Instead, Article 31.2 states that "in case of actions contradicting the objectives of the present law, the relevant body of executive power [the Ministry of Justice of Azerbaijan] may in writing notify the NGO or instruct the latter to remove the violations." Currently, the Ministry of Justice may audit NGOs at any time, on any subject, and without any procedural safeguards at all, in order to verify that NGOs' actions are in compliance with the NGO Law. The Ministry of Justice, for example, may participate in the internal events of an association, request any internal documents, and demand provision of any information about an NGO or its managers or members. A broad and vaguely defined responsibility to watch for "actions contradicting the objectives of the present law" is burdensome not just for NGOs, but for the Ministry of Justice itself.

Azerbaijani NGO Law does not specify the minimum period the Ministry of Justice must give to an NGO for eliminating the deficiencies found in its statutory documents or internal management. Whereas under domestic law, the procedure for convening the general assembly of an NGO required at least two weeks,<sup>20</sup> the Ministry of Justice in its warning to TMC gave a ten-day period.<sup>21</sup>

The mere fact that the Ministry of Justice had special authority to audit such internal affairs already contradicts international common practices. It is critical to mention that in the vast majority of European countries, the authority in charge of registration of an NGO, and in particular, a public association, does not carry *any* responsibility to supervise the activities of a registered NGO. Its responsibilities in regards to a particular NGO end immediately after incorporating information about the newly registered entity into the registry of legal entities. Other government authorities are responsible for compliance with the law of entities and individuals, such as a prosecutors, police, fire inspection, or tax inspection, and carry supervisory responsibilities over certain activities of entities and individuals. (However, some specific requirements might apply to certain special types of NGOs, especially those eligible for substantial tax preferences, such as charitable foundations.)

### *Conclusion and recommendations*

As the ECHR concluded in the *Tebieti Mühafize Cemiyeti* case, certain provisions of the Azerbaijan NGO law have assigned excessive authority to the Ministry of Justice to intervene in the internal activities of an NGO, and even to initiate its liquidation through a court when it has not violated the law. Such provisions, as illustrated in this article, do not meet international standards and best practices. Since the judgments of the European Court have binding force<sup>22</sup> for Azerbaijan and they are treated as grounds for appeal of judicial decisions in both criminal and

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<sup>18</sup> §§ 63-64, *Tebieti Mühafize Cemiyeti and Israfilov v. Azerbaijan*, supra note 2.

<sup>19</sup> *Ibid.*, §§ 61-62.

<sup>20</sup> Article 25.6 of the NGO Law.

<sup>21</sup> § 77, *Tebieti Mühafize Cemiyeti and Israfilov v. Azerbaijan*, supra note 2.

<sup>22</sup> In virtue of article 46 of the Convention.

civil cases (by the relevant decision of the Plenum of the Supreme Court of Azerbaijan<sup>23</sup>), Azerbaijani authorities should seek a permanent and sustainable solution to the legislative deficiencies by introducing amendments to the NGO legislation rather than merely solving the problem of one NGO that won a case in Strasbourg.

In order to implement the decision of the European Court, and to avoid appeals to the European court similar to the TLC case, it would be beneficial if the following improvements were introduced into Azerbaijani legislation:

- specify and limit the circumstances under which involuntary termination may be sought in court. For example, we would recommend applying the same list of reasons for dissolution of an NGO as are applied to business under Article 59 of the Civil Code, by eliminating the provision: "...or if a public association or foundation systematically engages in activities that are contrary to the aims set out in its by-laws, as well as in other cases provided by law."
- clarify the competence of the Ministry of Justice in regards to supervision over activities of NGOs. Our proposal would be to take away such power from the MoJ, as no such supervision is currently applied to businesses. If this is considered inappropriate, we would recommend at a minimum (1) to apply to MoJ audits the procedure for government audits applicable to all legal entities, setting up procedural safeguards for NGOs and making audits more efficient for the Ministry itself; and (2) to set up clear objectives for audits. More specifically, we would recommend revising Article 31.2 of the NGO Law, replacing the words "in case of actions contradicting the objectives of the present Law" with the words "in case of actions contradicting the Law."
- introduce a timeframe for correction of deficiencies along the lines of the Ministry of Justice's notification letters (for example, three or four weeks from the day of receiving a notification letter); and
- introduce alternative sanctions for NGOs apart from involuntary dissolution—for example, fines imposed on the managers of an NGO, as is applied to other legal entities, or withdrawal of tax benefits or other privileges.

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<sup>23</sup> Articles 455-456 of the Criminal Procedure Code (2000) and articles 431-1-431-3 of the Civil Procedure Code (2000) of the Republic of Azerbaijan.

*Article*

## **The Origin of the Species: Why Charity Regulations in Canada and England Continue to Reflect Their Origins**

**Peter R. Elson<sup>1</sup>**

*Numerous attempts have been made in the last ten years to push for the realignment of charity regulation in Canada. These calls for change have consistently included a proposed separation of tax policy and charitable regulation and the establishment of a Charity Commission-like agency, similar to the regulatory regimes in the United Kingdom and New Zealand. Like Australia and the United States, Canada has an integrated rather than an independent relationship between tax policy and charity regulation. This article argues that institutional origins and their positive reinforcement are critical to understanding both long-term regulatory regime development and the reluctance by governments to make substantial changes. The origins and evolution of England's Charity Commission and the 1930 amendment to the Income War Tax Act in Canada are presented as case studies. If desired regulatory change is to occur in Canada or elsewhere, it needs to start with a clear understanding of the context in which the original regulatory regime was created and reinforced.*

### **Introduction**

Numerous attempts have been made in the last ten years to push for the realignment of charity regulation in Canada.<sup>2</sup> These calls for change by charity lawyers and third sector representatives have consistently included a proposed separation of tax policy and charitable regulation and the establishment of a Charity Commission-like agency, similar to the independent regulatory regimes in the United Kingdom and New Zealand. Like Australia and the United States, Canada has integrated relationship between tax policy and charity regulation. While variations within these two forms of charitable regulation exist, the forms themselves have been highly resistant to change once they have been established.

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<sup>2</sup> Boyle, F. K. (1997). "Charitable Activity" Under the Canadian Income Tax Act: Definitions, Processes and Problems. Retrieved August 10, 2009, from <http://www.vsi-isbc.org/eng/regulations/reports.cfm>; Drache, A. (1999). *A Canadian Charity Tribunal: A Proposal for Reform*. Ottawa: Non-Profit Research Initiative, Kahanoff Foundation. Drache, A. (2001). *Hostage to History: The Canadian Struggle to Modernize the Meaning of Charity*. Retrieved August 10, 2009, from <http://www.drache.com/drache.cfm?view=articles.details&article=77&search=1>. IMPACS, & Canadian Centre for Philanthropy (2002). *Let Charities Speak: Report of the Charities and Advocacy Dialogue*. Vancouver: IMPACS - Institute for Media, Policy, and Civil Society and Canadian Centre for Philanthropy. Panel on Accountability and Governance in the Voluntary Sector (1999). *Building on Strength: Improving Governance and Accountability in Canada's Voluntary Sector*. Ottawa: Voluntary Sector Roundtable. Aptowitz, A. (2009) *Bringing the Provinces Back In: Creating a Federated Canadian Charities Council*. Toronto: C.D. Howe Institute.

This article argues that institutional origins and their positive reinforcement are critical to understanding both long-term regulatory regime development and the reluctance by governments to make substantial changes. The 1930 amendment to the *Income War Tax Act* in Canada is presented as an example of an integrated regulatory regime and then is compared to emergence of the independent Charity Commission in England in the early to mid-1800s. The article concludes with an analysis of why the origins of regimes hold important lessons for their reinforcement and the potential for change.

First and foremost, the modern regulation of charities takes place with highly institutionalized structures, either at the federal/central or provincial/state level. These institutionalized structures demonstrate adherence to established or highly organized protocols and procedures, which are positively reinforced each time the protocols and procedures are exercised.<sup>3</sup> In the case of charity regulation, protocols and procedures are exercised each time an application for registration is reviewed or revoked. That's not to say that change does not occur, as witnessed in changes manifesting from the *Charities Act 2006* in England.<sup>4</sup> However, even England's recent changes in charity law did not attempt to change the institutional configuration of the Charity Commission as an independent regulator or the HM Treasury as the source of tax policy. The premise of historical institutionalism is that contemporary regulatory policies constraints are embedded in these institutions and that because institutions are difficult to change, the origins of a particular institutional regime takes on added importance.

In Canada, the 1930 Amendment to the *Income War Tax Act* established the foundation on which all charities in Canada continue to operate. The 1930 amendment collectively introduced a universal tax deduction for charitable donations; defined the statutory term for charity; established a designated ceiling on income tax deduction for donations; and assigned the Department of Revenue as the designated regulator. These amendments to the *Income War Tax Act* still echo through the corridors of charity regulators and voluntary organizations across Canada. The immediate contextual importance of this legislation will be demonstrated through a profile of events leading to, during, and following its passage in the House of Commons on May 28, 1930. The longer-term institutionalization of the 1930 Amendment will be demonstrated through attempts by the voluntary sector to have statutory changes made by Parliament and the Supreme Court of Canada.

### ***Developments Leading to the 1930 Income War Tax Amendment***

A combination of tight moral control and extensive worker exploitation between the late 1800s and early 1900s was reflected in the growth of numerous reform movements in Canada.<sup>5</sup>

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<sup>3</sup> Pierson, P. (2004). *Politics in Time: History, Institutions, and Social Analysis*. Princeton, NJ: Princeton University Press.

<sup>4</sup> Charity Commission (2009). Charity Commission Consultations. Retrieved August 13, 2009, from <http://www.charity-commission.gov.uk/enhancingcharities/consultations.asp>. Charity Commission (2008). *Charities and Public Benefit: The Charity Commission's General Guidance on Public Benefit*. London: Charity Commission. Fries, R. (2006). Charity Commission for England and Wales. *International Journal of Not-For-Profit Law*, 8(2), 7-16.

<sup>5</sup> Andrew Armitage, "Canadian Social Welfare (1900 - 1988): Chronology," in *Social Welfare in Canada: Ideals, Realities and Future Paths* (2nd edition) (Toronto: McLelland and Stewart, 1988). Samuel A. Martin, *An Essential Grace: Funding Canada's Health Care, Education, Welfare, Religion and Culture* (Toronto: McClelland and Stewart, 1985).

This social and moral reform was undertaken by groups such as the Women's Christian Temperance Union, the Dominion Enfranchisement Associations, and other social gospel movements that promoted moral as well as physical well-being. These groups tackled issues related to women's education, urban public health, and sanitation, and promoted the establishment of recreational opportunities in both urban and rural areas.<sup>6</sup>

As charities were proliferating, so were other means of providing social support. Social justice aspirations and religious ideologies were integrated into service provision for much the same reason that Jesuit priests were the leading explorers of the early 1600s: the conversion of the masses to a particular faith-based life. The Moral and Social Reform Council of Canada is a case in point. This alliance of Anglican, Methodist, Presbyterian, and Baptist churches and the Trades and Labour Congress of Canada worked to get the federal government to enact the Lord's Day Act in 1906.<sup>7</sup> Another example is the National Social Service Congress in 1914, which has been described by Dennis Guest as a "display case of religiously motivated, social reform thought in Canada," where speakers represented the right wing, the center, and the left wing of the social gospel movement.<sup>8</sup>

Until this point, citizens and religious institutions were the primary drivers of voluntary sector activities and organizations. Governments provided funding when they were obliged to do so, but otherwise viewed social services as a means to control social unrest rather than a way to address social needs.<sup>9</sup> The prevailing view of the federal and provincial governments at the time was that social services and opportunities for employment were there for the taking, and it was only moral laziness or illness which stood in the way. (Laziness and moral decay were terms that were used to describe the "undeserving poor"; widows or those with a mental illness were considered the "deserving" poor.) This "hands off" approach by government was pervasive, and it was only by political or economic necessity that social action was taken. Income security measures resulting from the Winnipeg General Strike of 1919 and financial aid programs for World War I veterans and their families signalled the first major entry by the federal government into the area of social security.<sup>10</sup>

The proliferation of charities created to help the poor fostered social status for their benefactors and moral servitude for their recipients. It also resulted in the creation of local, centralized governing bodies such as the public Social Service Commission in Toronto in 1912, which was designed to streamline charity work and impose a degree of administrative efficiency and accountability, and led, over time, to the creation of the United Way of Greater Toronto.<sup>11</sup>

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<sup>6</sup> Allan Moscovitch, & Glenn Drover, "Social Expenditures and the Welfare State: The Canadian Experience in Historical Perspective," in A. Moscovitch & J. Albert, eds., *The Benevolent State: The Growth of Welfare in Canada* (Toronto: Garamond Press, 1987).

<sup>7</sup> Dennis Guest, *The History of Social Security in Canada*. Retrieved May 15, 2006, from [www.thecanadianencyclopedia.ca](http://www.thecanadianencyclopedia.ca).

<sup>8</sup> *Ibid.*, p. 33.

<sup>9</sup> Andrew Armitage, "Canadian Social Welfare (1900 - 1988): Chronology," in *Social Welfare in Canada: Ideals, Realities and Future Paths* (2nd edition) (Toronto: McLelland and Stewart, 1988).

<sup>10</sup> Janet Lautenschlager, *Volunteering: A Traditional Canadian Value* (Ottawa: Voluntary Action Program—Canadian Heritage, 1992).

<sup>11</sup> Paula Maurutto, "Charity and Public Welfare in History: A Look at Ontario, 1830-1950," *The Philanthropist*, vol. 19, no. 3 (2005), pp. 159-167. Gale Wills, *A Marriage of Convenience: Business and Social Work in Toronto 1918-1957* (Toronto: University of Toronto Press, 1995).

By the end of the 1920s, similar federated fundraising organizations were formed in major centers across Canada.<sup>12</sup>

According to social work historian Gale Wills,

There was an assumption early in the Depression that properly organized private charity would take the strain off the relief budget, partially because it used philanthropic rather than tax dollars, but mostly because of the persistent belief that unemployment was a matter of individual circumstances and that “good” [social welfare] casework would result in putting people back to work.<sup>13</sup>

This perspective eroded as the Depression continued, but it still dominated political and economic discourse throughout the decade.

By 1929 the Liberal government was being urged by the opposition Labour party to address the severe levels of unemployment and to assist provinces, regardless of provincial jurisdiction for welfare as defined by the *British North America Act*.<sup>14</sup> Immigration was exploding, growing from less than 50,000 per year in the early 1900s to 400,000 per year in 1913.<sup>15</sup> It was this massive immigration to Canada that led to the creation of so many ethnic-centred mutual support and fundraising organizations.<sup>16</sup> The National Council on Child and Family Welfare, for example, took a lead role in supporting the provision of relief across Canada and in the process developed strong political, economic, and community connections.<sup>17</sup>

The proposed personal tax deduction amendment to the *Income War Tax Act* was thus introduced in the context of a growing economic depression, accelerating unemployment, massive immigration adjustments, a traditional federal reluctance to provide support in areas of provincial jurisdiction, and a pending federal election. The 1930 *Income War Tax Act Amendment* itself was one of the last pieces of legislation passed by W. L. MacKenzie King’s minority Liberal government before a federal election resulted in the Liberals being defeated by the R. B. Bennett-led Conservative Party. What follows is an outline of how this legislation was introduced and debated.

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<sup>12</sup> Gale Wills, *A Marriage of Convenience: Business and Social Work in Toronto 1918-1957* (Toronto: University of Toronto Press, 1995).

<sup>13</sup> *Ibid.*, p. 65.

<sup>14</sup> House of Commons Debates, 16th Parliament, 3rd Session, Vol. I, February 15 Session. (1929) pp. 166-167.

<sup>15</sup> Jad Bitar, *The Emergence of Centraide in the Greater Montreal Area: A Case of Radical Social Innovation* (Montreal: HEC [École des hautes études commerciales], 2003).

<sup>16</sup> Janet Lautenschlager, *Volunteering: A Traditional Canadian Value* (Ottawa: Voluntary Action Program: Canadian Heritage, 1992).

<sup>17</sup> Canadian Council on Child and Family Welfare, “Proceedings of the Eleventh Annual Meeting: Canadian Council on Child and Family Welfare,” *Child and Family Welfare*, vol. VII, no. 1 (1930). Library and Archives Canada, Canadian Council on Child and Family Welfare, MG26-K, M-3179, pp. 604959 - 604961, Correspondence to R. B. Bennett, Prime Minister, 1933. Richard B. Splane, *75 Years of Community Service to Canada: Canadian Council on Social Development, 1920-1995*. (Ottawa: Canadian Council on Social Development, 1996). Paula Maurutto, “Charity and Public Welfare in History: A Look at Ontario, 1830-1950,” *The Philanthropist*, vol. 19, no. 3 (2005), pp. 159-167.

### ***Canada's 1930 Income War Tax Amendment***

A number of amendments to the *Income War Tax Act* were moved in the House of Commons by the Hon. Charles Avery Dunning, Minister of Finance, on May 1, 1930, as part of the Ways and Means Motion to implement his recently tabled budget. The amendments included provisions

... 2. That the income of co-operative companies and associations be exempt from income tax; and ... 3 (b) That donations, to the extent of ten per cent of the net income of the taxpayer to any church, university, college, school or hospital in Canada, be allowed as a deduction.<sup>18</sup>

The subsequent debate in Parliament on the motion evolved not around the justification for the deduction, which was readily acknowledged, but the type of charitable organization that would benefit.<sup>19</sup> This limited (i.e., institutional) tax provision was quickly met with vigorous opposition from community funds, federated charities, and non-sectarian charities. The Act also was seen to favor charities in Quebec, which were all affiliated with the Roman Catholic Church, over the non-sectarian charities that dominated in Ontario and the other provinces.<sup>20</sup> The proposed amendment attracted attention in the media, and the notice of at least one well-positioned business executive. The *Toronto Star* commented on the proposed income tax provisions in its Friday, May 2, editorial entitled "The Income Tax Concessions":

Among the concession to income taxpayers which Mr. Dunning makes in his 1930 budget, one of the most interesting is the provision that "donations to any church, university, college, school or hospital in Canada shall be treated as deductions from income up to a maximum of 10 per cent of the net income of the taxpayer." This type of deduction is quite new to the Canadian Act, but something of the sort has been many times suggested. ... [T]he new provision recognizes and encourages a type of contribution which is extremely valuable in every community.<sup>21</sup>

Further in the same May 2 edition of the *Toronto Star*, the 10 per cent limit on donation deductions received special attention. Reporting on the amendment from the perspective of churches (the "Biblical Budget," as it was called), it was reported that for the first time in Canadian history the biblical tithe was being used (by Finance Minister Dunning) to encourage and help the churches of Canada, irrespective of denomination. The benefit to schools, universities, colleges, and hospitals was also noted in the same article, as was the precedent for similar tax deductions which had been established in the United States.<sup>22</sup>

The *Toronto Star* continued its coverage throughout the month, including another editorial on May 6, 1930. Entitled "No Tax on Philanthropy," the editorial called the tax

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<sup>18</sup> House of Commons Debates, 16<sup>th</sup> Parliament, 4<sup>th</sup> Session, Vol. III, 1930, pp. 1677.

<sup>19</sup> John D. McCamus, *Report on the Law of Charities*, vol. 1 (Toronto: Ontario Law Reform Commission (1996).

<sup>20</sup> Rod Watson, "Charity and the Canadian Income Tax: An Erratic History," *The Philanthropist*, vol. 5, no. 1 (1985), pp. 3-21.

<sup>21</sup> *Toronto Star*, "The Income Tax Provisions" (editorial), (1930, May 2), p. 6

<sup>22</sup> Thomas Wayling, "Dunning Uses Bible Tithe to Aid Canadian Churches," *Toronto Star*, (1930, May 2), p. 9.

deductions for donations the most novel feature of the Dunning budget and continued with the comment that "...Unknown to the public a number of organizations engaged in important community work urged the Dominion government over a period of years to take the step now determined upon."<sup>23</sup>

The motion to amend section 3 (b) of the *Income War Tax Act* on tax deduction for donations to any church, university, college, school, or hospital was debated in Parliament starting on May 24. J.S. Woodsworth, an Independent labour Party MP at the time,<sup>24</sup> led the committee debate with a call to extend the exemption to community funds, or federated charities.<sup>25</sup> Dunning replied that this proposed extension was noteworthy, but still too narrow to reflect the wide range of representations he had also received. Opposition Conservative member R.B. Hanson stood in the House to advocate for the inclusion of the Victorian Order of Nurses and similar organizations:

If the minister is going to grant this exemption, he should cover the whole field. I am not opposed to the exemption; indeed it was urged upon the government by this party many years ago in the house, and I suggest to the minister that if he is adopting the principle, the exemption list is not wide enough.... The whole question [of exemptions] should be reviewed by the minister.... I have no doubt that representations have been made to him by every institution in Canada.<sup>26</sup>

Others made similar appeals for the inclusion of charitable and social agencies that existed at the time in most major cities.<sup>27</sup> Their exclusion from a deduction would create an undue burden on many worthwhile charities and their inclusion would support the voluntary community donations. Dunning, for his part, found merit in the suggestions that had been put forward, but was reluctant to proceed, citing the governments' lack of experience in knowing what the consequences would be. The opposition parties were also adamant that the government should not be given discretion to determine eligible charities.<sup>28</sup>

The eligibility floodgates continued to open, with museums and non-sectarian and federated charities being noted as worthy exemptions, complemented by continued references to the existing tax provisions in the United States.<sup>29</sup> Dunning indicated that he too was impressed with the wide range of representation he had received, but he declared that he was overwhelmed by potential implementation issues. Dunning appealed to the House to be allowed to start with

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<sup>23</sup> *Toronto Star*, "No Tax on Philanthropy" (editorial), (1930, May 6), p. 6.

<sup>24</sup> Woodworth was to become founder and leader of the Co-operative Commonwealth Federation, the precursor to the current New Democratic Party.

<sup>25</sup> House of Commons Debates, 16th Parliament, 4th Session, Vol. III, Sess. 2513 - 2519 (1930).

<sup>26</sup> *Ibid.*, p. 2513.

<sup>27</sup> Examples explicitly cited during the debate included: the Victorian Order of Nurses; Boys' Welfare; Montreal Hygiene Committee; the Social Hygiene Council; the Anti-tuberculosis Association; the King's Daughters; the Federated Charities of Montreal; the Child Welfare Association; the Family Welfare Association; the Children's Aid Society; the social settlement of boys' and girls' clubs; and the Red Cross Society.

<sup>28</sup> House of Commons Debates, 16th Parliament, 4th Session, Vol. III, Sess. 2513 - 2519 (1930).

<sup>29</sup> *Ibid.*



the provisions as outlined in the amendment and then to look to widen the exemptions in the future—e.g., in one year—once the government had gained experience.<sup>30</sup>

When the Ways and Means Committee continued its debate in Parliament on May 27, Opposition leader R.B. Bennett reiterated the government's own (biblical) position on the 10 per cent of personal income limit for tax deductions for donations to worthy causes, and pointed out the discrepancy between this principle and the proposed practice of only allowing donations to be deducted if they went to particular types of charities. W. D. Euler, Minister of National Revenue, and Finance Minister Dunning both restated their earlier position that the principle of allowing tax deductions for donations to charity was important, but the administrative and forgone tax revenue costs were unknown and caution was called for. At this point Dunning conceded that the use of the term "charitable institutions ... operated exclusively as such and not for the benefit of private gain" appealed to him, again acknowledging potential unforeseen administrative difficulties.<sup>31</sup>

On May 28, 1930, less than thirty days after the amendment to the *Income War Tax Act* was first introduced, W. D. Euler, Minister of National Revenue, stood in Parliament, and acknowledged the value of argument for the inclusion of federated charities, the Red Cross, and other organizations. Euler then stated that the government had decided that the clause should be broadened, but specific reference to charities by type would only create another wave of protests from those excluded. The term Euler proposed to include was "charitable organization."<sup>32</sup>

Euler then proposed the following amendment: "That section 3 (j) be amended by striking out the words 'any church, university, college, school or hospital' in lines 24 and 25, and substituting therefore the words 'any charitable organization.'"<sup>33</sup> Euler continued at this point to establish the legal foundation on which charities continue to stand in Canada, by quoting directly from Halsbury's Laws of England:

Only those purposes are charitable in the eye of the law which are of a public nature, whose object, that is to say, is to benefit the community or some part of it, not merely particular individuals pointed out by the donor. Accordingly gifts which are directed to the abstract purposes of relieving poverty, advancing education or religion are charitable... "Charity" in its legal sense comprises four principal divisions: trusts for the relief of poverty, trusts for the advancement of education, trusts for the advancement of religion, and trusts for other purposes beneficial to the community not falling under any of the preceding heads.

Euler continued, "I submit that this phrase embraces every organization of this kind." Section 3 (j), he said, would then read as follows:

Not more than ten per centum of the net taxable income of any taxpayer which has been actually paid by way of donation within the taxation period to, and receipted for as such

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<sup>30</sup> Ibid.

<sup>31</sup> House of Commons Debates, 16th Parliament, 4th Session, Vol. III, Sess. 2645 - 2651 (1930).

<sup>32</sup> Ibid.

<sup>33</sup> House of Commons Debates, 16th Parliament, 4th Session, Vol. III, Sess. 2714 - 2715 (1930), p. 2714.

by any charitable organization in Canada operating exclusively as such and not operated for the benefit of private gain or profit of any person, member or shareholder thereof.<sup>34</sup>

Opposition leader R. B. Bennett congratulated Euler for having introduced the amendment, expressed his satisfaction that the term “charitable organization” covered “every species of benevolence,” and said that the 10 per cent limit also protected the government from excessive foregone revenue.<sup>35</sup> The Bill was then reported, read the third time, and passed unanimously by the House of Commons.

The passing of the 1930 amendment to the *Income War Tax Act* marked the first time in Canada that a universal tax deduction was introduced for any charitable donation; the statutory term for charity was defined; a designated ceiling on income tax deduction on donations was imposed; and a regulatory body, the Department of Revenue, was assigned to administer the *Act*.<sup>36</sup>

If Euler’s reference to the Bible as a basis for capping allowable tax deduction for charitable donations to 10 per cent reflected a long religious history, it was no less profound in a legal context than his reference to the Halsbury’s Laws of England. The quote he used from Halsbury’s was a direct passage from the majority judgment in the House of Lords by Lord Macnaghten in the 1891 *Pemsel* case which was, and continues to stand as, the leading judgment and interpretation of “charitable purposes.”

### ***Developments Following the 1930 Income War Tax Amendment***

During R. B. Bennett’s term as Prime Minister from 1930 to 1935, additional amendments were made to the *Income War Tax Act* so that by 1935 eligible donations included not only gifts or property to charities and educational institutions but also donations to the “Dominion of Canada or any province or political subdivision thereof.”<sup>37</sup> The Act prudently reserved the right for the government to validate the value of the gift or property to prevent inflationary assessments, which the government still exercises to determine “fair market value.”<sup>38</sup>

As valuable as the deduction of donations to charities appeared to be at the time, the inability of charities to raise the funds necessary to provide services only expanded during the years of the Great Depression.<sup>39</sup> In the 1930s, millions of Canadians were unemployed; on the

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<sup>34</sup> *Ibid.*, p. 2715 (emphasis added).

<sup>35</sup> *Ibid.*

<sup>36</sup> Canada Revenue Agency, “The Future of Charities in Canada,” (1998) retrieved June 8, 2006, from <http://www.cra-arc.gc.ca/tax/charities/policy/ces/ces-004-e.html>. House of Commons Debates, 16th Parliament, 4th Session, Vol. III, Sess. 2714 - 2715 (1930). John D. McCamus, *Report on the Law of Charities*, vol. 1 (Toronto: Ontario Law Reform Commission, 1996).

<sup>37</sup> Harry H. Stikeman, *Income War Tax Act and Excess Profits Tax Act 1940* (Canada) (Toronto: Richard De Boo Ltd., 1947), pp. 265. David Walden, D, “The Tax Credit System: Blessing or Burden?” *Archivaria*, vol. 18, (Summer 1984), pp. 84-90.

<sup>38</sup> Revenue Canada Agency, IT-297R2, “Gifts in Kind to Charity and Others” (Ottawa: Canada Revenue Agency, 1990), retrieved May 3, 2007, from <http://www.cra-arc.gc.ca/E/pub/tp/it297r2/it297r2-e.html>. Harry H. Stikeman, *Income War Tax Act and Excess Profits Tax Act 1940* (Canada) (Toronto: Richard De Boo Ltd., 1947).

<sup>39</sup> Rod Watson, “Charity and the Canadian Income Tax: An Erratic History,” *The Philanthropist*, vol. 5, no. 1 (1985), pp. 3-21.

prairies, farmers were devastated by a seven-year drought.<sup>40</sup> In a letter to Prime Minister R. B. Bennett in 1933, Charlotte Whitton of the Canadian Council on Child and Family Welfare predicted that the number of families on relief would be at least 80 per cent higher than at the corresponding period the previous year.<sup>41</sup>

For support, charities turned to local municipalities. But they relied on property taxes for their income, and during the 1930s this source of revenue was either limited or in default. Increasingly, provincial governments had to assume the responsibility for debt relief. Yet some provinces were themselves in financial straits, and so the provinces in turn appealed to the federal government for support.<sup>42</sup>

The federal government responded under pressure from provincial governments to address the massive unemployment and years of drought on the prairies by increasing its funding for unemployment relief measures and passing an *Employment and Social Insurance Act* in 1935.<sup>43</sup> Meanwhile, relief in the form of soup kitchens, bread lines, clothing depots, and shelters for the hungry and homeless were provided by caring individuals, religious groups, and voluntary agencies such as the Red Cross.<sup>44</sup> This economic climate significantly increased the number of local organizations and local branches of national organizations to which tax-deductible donations could be made by those who were more fortunate.

### ***England's Charity Commission: Thirty-Four Years in the Making***

While Canada's charity regulator emerged in 1930 during the Great Depression, England's Charity Commission was formally created in 1853 for reasons that were founded in progressive educational reform, not economics or unemployment. While a body of Commissioners was established with the *Statute of Charitable Uses 1601* to ensure that charitable gifts were used for their intended purpose, costly legal remedies made the process impractical.<sup>45</sup> The industrial revolution in the nineteenth century combined with widespread dislocation and poverty and the emergence of a social reform movement brought the Brougham Inquiry into being. The Brougham Inquiry, headed by Lord Brougham and launched in 1819, lasted almost twenty years and resulted in the prosecution of almost 400 charities. The initial aim of Lord Brougham was that the Inquiry would address access to education by the poor, particularly educational charities and their benign neglect of general public education. Others associated with the inquiry were interested in more general charity abuses such as fraud and misallocation of

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<sup>40</sup> Janet Lautenschlager, *Volunteering: A Traditional Canadian Value* (Ottawa: Voluntary Action Program—Canadian Heritage, 1992).

<sup>41</sup> Library and Archives Canada, Canadian Welfare Council, Vol. 18-21, p. 0604959, Charlotte Whitton to Rt. Hon. R.B. Bennett, September 11, 1933.

<sup>42</sup> Andrew Armitage, "Canadian Social Welfare (1900 - 1988): Chronology", in *Social Welfare in Canada: Ideals, Realities and Future Paths* (2nd edition) (Toronto: McLelland and Stewart, 1988).

<sup>43</sup> *Ibid.*

<sup>44</sup> Janet Lautenschlager, *Volunteering: A Traditional Canadian Value* (Ottawa: Voluntary Action Program—Canadian Heritage, 1992).

<sup>45</sup> Fries, R. (2006). Charity Commission for England and Wales. *International Journal of Not-For-Profit Law*, 8(2), 7-16. O'Halloran, K., McGregor-Lowndes, M., & Simon, K. (2008). *Charity Law & Social Policy: National and International Perspectives on the Functions of the Law Relating to Charities*. New York: Springer.

funds.<sup>46</sup> The initial proposal was rejected by the House of Commons several times due to the influence of powerful universities, churches, and charities that did not want their “private” practices examined. Nevertheless, in 1819 the Inquiry into Charitable Endowments, or the Charity Commission, got underway.<sup>47</sup>

This initiative was by no means the only incident of reforming the general state of welfare in England at the time. In 1834 the Poor Law was amended to provide the right for administrators to distinguish between “deserving” and “non-deserving” poor, and for the institutionalization of workhouses, an initiative driven by middle- and upper-class interests that paid for the services provided.<sup>48</sup>

The Charity Commission was conducted by trained lawyers between 1819 and 1837 in a series of four approved commissions, reported semi-annually and surveyed nearly twenty-nine thousand charities.<sup>49</sup> According to historian Richard Thompson, the creation of the inquiry was an important step in the evolution of inquiry per se as well as the specific investigation of charity.<sup>50</sup> Without explicitly intending to do so, the Commission became an agent for reform without any of the bureaucratic trappings that would follow later. Between 1830 and 1837, previously informal reporting and examination processes were tightened up, and the training of Commissioners, attribution of reports, standardized corrective action, and a centralized advisory board were introduced.<sup>51</sup> The focus of the Commissioners’ activities, it must be noted, was on conducting inquiries as a legal research unit. It was in this context that its auxiliary function as an agency of reform was exercised.

Systemic action on the part of the authorities in response to these inquiries was often buried in a stormy sea of paper and political intrigue, as the Commission itself had no formal remedial powers.<sup>52</sup> Informally though, admonishment, mediation, and trusted advice were most often the tools of persuasion, as, when necessary, was legal action through the courts. Each renewal of the Commission presented an opportunity for opponents to limit its activities and for proponents to push for its renewal.

The fourth and last issue of the Royal Commission expired in 1837.<sup>53</sup> When Lord Brougham pushed to have the Education and Charities bill adopted there was serious and well-

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<sup>46</sup> Gilbert, M. (1922). *The Work of Lord Brougham for Education in England*. Unpublished Doctoral Thesis, University of Pennsylvania, Philadelphia.

<sup>47</sup> For example, many universities and any cathedral or collegiate churches or religious schools that had an internal affairs auditor (also called a special visitor) were exempt.

<sup>48</sup> Fingard, J. (1975). “The Relief of the Unemployed Poor in Saint John, Halifax, and St. John’s, 1815-1860.” *Acadiensis: Journal of the History of the Atlantic Region*, 5(1), 32-53.

<sup>49</sup> Thompson, R. (1979). *The Charity Commission and the Age of Reform* (Toronto: University of Toronto Press). Willson, F. M. G. (1958). The Parliamentary Charity Commissioner. *Parliamentary Affairs: The Journal of the Hansard Society for Parliamentary Affairs*, XII (1958-59), 180-198.

<sup>50</sup> Thompson, R. (1979). *The Charity Commission and the Age of Reform* (Toronto: University of Toronto Press).

<sup>51</sup> Ibid.

<sup>52</sup> Ibid., 49.

<sup>53</sup> The first commission was established in 1818 and focused on education charities. The second lasted from 1819 to 1830; the third from 1831 to 1834 and the fourth from 1835 to July 1837.

connected resistance to the directive nature of education portion of the bill and it was “discharged” by the House of Lords.<sup>54</sup> Expectations on the side of charity reform proponents that the Commission would be renewed for a fifth term were abruptly halted and a final report was quickly assembled. The final report of the Commission listed eleven faults in charitable trust administration. Among these were the expense and difficulty in replacing trustees; the risk of making loans based on personal security; the difficulty and legal expense incurred in changing the charter of a trust; and charity mismanagement and conflicts of interest. In short, although the report did not say so, there was an ongoing need for a new agency to oversee charities.

There are mixed views on the relationship of the Charity Commission Inquiry (1818-1837) to the formation of the permanent Board of Commissioners in 1853. Some, such as Richard Thompson, hold the view that the relationship was tenuous at best. Richard Mitcheson, writing in 1887, draws a much closer link. A Select Committee of the House of Commons was established in 1835 to review the incomplete reports that were then available from Lord Brougham’s Commission.<sup>55</sup> The Select Committee recommended the appointment of a board to superintend and sanction charities, including an audit of accounts, general governance of all charities, and legal action when necessary. Meanwhile, scandals associated with misuse and misdirected charity funds continued, as did the call for reform and sustained opposition from powerful and well-connected churches, universities, and corporations.<sup>56</sup> This dynamic was not restricted to charities; labor laws, poor laws, and a number of other measures were introduced and fiercely debated as public opinion, for the first time, started to manifest itself in the political sphere.<sup>57</sup> The Charity Commission Inquiry in 1818 was the first clear example of the fusion of social inquiry and the Royal Commission.

In 1849, a Royal Commission was appointed to once again examine the reports of Lord Brougham’s Commission. By this time all the reports from the earlier Brougham Commission were complete. The Royal Commission issued its findings in 1850 and agreed in almost every point with those of the Select Committee of 1835. This Commission resulted in the *Charitable Trusts Act of 1853*, which was in fact originally drafted by the 1849 Royal Commission.<sup>58</sup>

### **Charitable Trusts Act of 1853**

While the *Charitable Trusts Act of 1853* incorporated many of the recommendations of the Royal Commission, there were two exceptions of note. First, the commissioners initially had no power of audit, although they did require the submission of annual financial accounts. Second, the power to divert welfare charity funds to useful purposes was not included, although they could authorize the sale or exchange of lands held by a charity.<sup>59</sup> What the Act did include was the appointment of a permanent commission;<sup>60</sup> powers to conduct inquiries into the condition and management of charities; taking action on charitable property, including its

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<sup>54</sup> Ibid, 49.

<sup>55</sup> Mitcheson, R. E. (1887). *Charitable Trusts: The Jurisdiction of the Charity Commission, Being the Acts Conferring Such Jurisdiction, 1853-1883* (London: W. Maxwell and Son).

<sup>56</sup> Ibid, 49.

<sup>57</sup> Ibid, 49.

<sup>58</sup> Ibid, 54.

<sup>59</sup> *Charitable Trusts Act, 1853, s24.*

<sup>60</sup> An exemption to this oversight existed for Roman Catholic charities until 1859.

transfer to a new trust; and sanction of the commissioners as a condition for any legal action against a charity. Judges could make decisions in chambers on certain charities,<sup>61</sup> including authorizing trustees to remove unfit or incompetent officers;<sup>62</sup> and to the relief of many, the practice of making vexatious suits against charities for the sake of costs was curtailed.

The Charity Commission itself consisted of three permanent members, and a fourth member, along with the secretary, held office at the pleasure of the Crown.<sup>63</sup> The three permanent members were paid and had judicial tenure of office, meaning that they operated independently and were non-political. The unpaid commissioner was an M.P., although there were ongoing questions as to the particular role of this person who acted in part as a buffer between Parliament and the Commission. When the work of the Endowed Schools was added in 1869, the work not only became heavier, it became a political lightning rod for sectarian education issues. It would be almost one hundred years before full independence was achieved.<sup>64</sup>

While amendments to the Act were introduced in 1855 and 1860, the basic role of the commission remained: namely, that of inquiry and advice, property transactions, sanctioning judicial proceedings and remedial schemes. In 1860 the Commission was given de facto judicial powers, restricted to applications made by the majority of trustees where the income of the charity exceeded fifty pounds. Appeals to the district or county court were made where the income of the charity was less than fifty pounds.<sup>65</sup> The result of this latter measure was that regulation of charities shifted from the courts to the Commission.

This development didn't stop opponents of the Charity Commission from trying to circumvent its jurisdiction through private Acts of Parliament and legal rulings. Consequently, a further amendment was passed in 1862 decreeing that no Act of Parliament or decree of the Court of Chancery related to charities could circumvent the jurisdiction of the Charity Commissioners. The power of the Commission was further enhanced in 1869 when the work of the Endowed Schools Commissioners was transferred to the Charity Commissioners. This added responsibility brought with it a raise in the number of Commissioners from three to five.<sup>66</sup> The power of the Commission was increased again in 1872 with the passing of the *Charitable Trustees Incorporation Act*. In this case the Commissioners were granted the power to grant certificates of incorporation. Over time further modifications were made with the intention of increasing the discretion and authority of the Commission. Until 1899, that is: in 1899 the endowed school work was removed from the Charities Commission and their responsibilities returned to the supervision of non-educational charities.

The presence of the parliamentary charity commissioner in the operations of the Charity Commission slowly diminished until the person was rarely seen except at the formal induction.<sup>67</sup> This political absence was raised during Lord Nathan Committee on Charitable Trust Law in

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<sup>61</sup> Charities with annual incomes above thirty pounds.

<sup>62</sup> *Charitable Trusts Act, 1853, s. 22.*

<sup>63</sup> *Ibid*, 54.

<sup>64</sup> Willson, F. M. G. (1958). The Parliamentary Charity Commissioner. *Parliamentary Affairs: The Journal of the Hansard Society for Parliamentary Affairs*, XII (1958-59), 180-198.

<sup>65</sup> *Ibid* 54.

<sup>66</sup> *Ibid* 54.

<sup>67</sup> *Ibid* 54.

1952. Subsequently, with the Charities Act 1960, P.M.s became ineligible to sit on the Charity Commission and the link to Parliament became the Home Secretary.

The work of the Nathan Committee is well known and documented, as is the Charities Act 1960 and its successors, the Charities Acts of 1992, 1993 and 2006.<sup>68</sup> What is less well known and appreciated is that the very structure of the Charity Commission has been held intact since its initial inception by the Select Committee of the House of Commons in 1835, which was struck to review the reports from Lord Brougham's Commission.

### ***Findings and Analysis***

The 1930 amendment to the *Income War Tax Act* was a critical event in voluntary sector/government relations in Canada. Paul Pierson points to the path-dependent processes and positive feedback mechanisms that can be highly influential at the early stages of policy development.<sup>69</sup> In the overall context of income tax in Canada, 1930 is within the early stage of its development. The *Income War Tax Act* was first introduced in 1917 and no systematic provision for charitable deductions had been implemented prior to the First World War. The 1930 amendment to the *Income War Tax Act* established a path-dependent process that tax deductions to charities would be constrained to a limit of 10 per cent of personal income. This measure was applied annually to subsequent individual and then corporate tax returns, and has been in place, with small variations, to the present day. The millions of taxpayers who annually apply charitable deductions to their income tax forms and the thousands of charitable registration applications received by the Charities Directorate of the Canada Revenue Agency continue to reinforce this integrated governance structure.

While there have been periodic increases in the level of charitable deduction allowance, there has been no attempt to either roll back or eliminate this deduction. The annual use of this same deduction by millions of individual Canadian taxpayers and its promotion by eligible charities to donors combine to represent a positive feedback mechanism and ongoing reinforcement of the tax deduction policy. Charitable deduction regulations were institutionalized through the growth of the internal mechanisms established in the Department of Revenue to administer these deductions and related regulations, including the centralized registration of all charities in 1967. One of the characteristics of path dependency is that the further the government progressed along this path, the greater the likelihood it would continue, and the harder it would be for any alternative to be considered, which has indeed been the case.

In England, the basic separation of tax policy and charity regulation has also been consistently reinforced. The Charity Commission currently operates under Schedule 1A of the *Charities Act 1993*.<sup>70</sup> The number of members of the Commission has not expanded a great deal, given the vast increase in the volume of its activities. The current Commission allows for a minimum of four and a maximum of nine members, including the Chair. Members must

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<sup>68</sup> Nathan, L. (1950). *Report of the Committee on the Law and Practice Relating to Charitable Trusts: Abstract [electronic source]*. London: Charitable Trusts Committee, <http://www.bopcris.ac.uk/bopall/ref9691.html>, 6. P., & Leat, D. (1997). "Inventing the British Voluntary Sector by Committee: from Wolfenden to Deakin." *Non-Profit Studies*, 1(2), 33-45.

<sup>69</sup> Paul Pierson, "Not Just What, But When: Timing and Sequence in Political Processes," *Studies in American Political Development*, vol. 14, no. 1 (2000), pp. 72-92.

<sup>70</sup> Charity Commission (2008). *Charity Commission Governance Framework*, retrieved January 4, 2010, from <http://www.charity-commission.gov.uk/tcc/govframe.asp#1>.

collectively have knowledge and experience of the law relating to charities, charity accounts and the financing of charities, and the operation and regulation of charities of different sizes and descriptions. At least two members continue to require appropriate legal qualifications, while at least one must have knowledge of the Welsh context and be appointed following consultation with the National Assembly for Wales.<sup>71</sup>

The Charity Commission in England continues as a non-Ministerial Government Department. It is part of the Civil Service and reports annually to Parliament. The Charity Commission is independent of Ministerial influence and independent from the sector it regulates. The *Charities Act 2006* continued this precedent by restating that: “In the exercise of its functions, the Commission shall not be subject to the direction or control of any Minister of the Crown or other Government Department.”<sup>72</sup> The Charity Commission continues to exercise a number of quasi-judicial functions where it uses powers similar to those of the High Court, as were specified in the *Charitable Trusts Act 1853*. Like the original Brougham Commission, the Charity Commission operates with the benefit of considerable powers of persuasion rather than relying solely on punitive regulatory measures or court action.

In Canada, the 1930 amendment to the *Income War Tax Act* has also been legally and politically institutionalized. The act itself established the terms under which organizations could register for charitable tax status and those terms remain firmly in place. Challenges to the Supreme Court of Canada have upheld the right of Parliament to define charitable purposes and several political appeals have been rebuffed. In fact, a recent ruling by the Supreme Court of Canada reinforced the integrated tax and regulatory relationship by viewing foregone tax revenues as a legitimate factor in the consideration of charitable tax status.<sup>73</sup>

The 1930 amendment to the *Income War Tax Act* established the regulatory limit on charitable deductions, but unlike the statutory definition of charitable purpose, it has undergone several modifications that were directly driven by budgetary tax changes introduced by the Department of Finance. Increases in deduction allowances were introduced in 1972, 1995, and 1996, to 20, 50, and 75 per cent respectively. The latter two increases corresponded to significant budget cuts to the voluntary sector which were designed to mitigate the political backlash from the funding cuts and foster voluntary sector independence from government grants by providing greater access by donor markets. For the same reason the deduction of public traded securities to charities in 2006 followed a massive cut in voluntary sector funding.<sup>74</sup>

It has only been since 2000 that the Charities Directorate of the Canada Revenue Agency has initiated any form of “soft” regulation, intermediary sanctions, and general charity education.

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<sup>71</sup> Ibid.

<sup>72</sup> This statement is contained in *Charities Act 2006* (c. 50) Part 2 — Regulation of charities Chapter 1 — The Charity Commission.

<sup>73</sup> A.Y.S.A. Amateur Youth Soccer Association v. Canada (Revenue Agency), [2007] 3 S.C.R. 217, 2007 SCC 42. Also see A. Parachin (2009). “Legal Privilege as a Defining Characteristic of Charity.” *Canadian Business Law*, vol. 48, no. 1, 36.

<sup>74</sup> Hon. Jim Flaherty, The Budget Plan 2006 (Ottawa: Department of Finance, 2006), retrieved June 15, 2006, from <http://www.fin.gc.ca/budget06/bp/bptoce.htm>. Andy Levy-Ajzenkopf, “Surprise! Budget Cuts 2006,” Charity Village Cover Story (October 2, 2006), retrieved October 2, 2006 from [www.charityvillage.com](http://www.charityvillage.com).



Even now, charity education is restricted to meeting regulatory requirements rather than any general form of governance or operational guidance.<sup>75</sup>

### **Conclusion**

The 1930 amendment to the *Income War Tax Act* is a critical event in voluntary sector/government relations in Canada. The statutory and regulatory mechanisms put in place on May 28, 1930, have been positively reinforced over time and consolidated and enhanced in 1967 with the development of the central registration and regulation of charities by the Canada Revenue Agency. The explicit desire by the federal government to balance support to charities and limit foregone revenue has been consistently maintained through both the registration and taxation processes.

Taxation and regulation issues raised by voluntary sector representatives during the Voluntary Sector Initiative in Canada in 2000-2005 were rebuffed, not just by the representatives of the Department of Finance, Treasury Board and the Canada Revenue Agency, but by more than seventy years of positive reinforcement for the statutory role first established by the federal government in the 1930 Amendment to the *Income War Tax Act*. In England the Charity Commission continues to enjoy the independence that was first set down by the *Charitable Trusts Act, 1853*.

The regulatory regimes for charities in England and Canada both emerged under a general climate of economic and social upheaval, one in context of the industrial revolution, the other one hundred years later during the Great Depression. What history and the institutionalization of these two regulatory regimes for charities have demonstrated is that the origins of a regulatory regime lead to its positive reinforcement regardless of the extent to which external circumstances or its efficiency may change. Changes may take place at the periphery, and this has occurred in both Canada and England, but the core regulatory regime is likely to remain true to its origins.

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<sup>75</sup> Elson, P. (2010, forthcoming). *High Ideals and Noble Intentions: A New Understanding of Nonprofit and Voluntary Sector Relations in Canada* (Toronto: University of Toronto Press).

*Article*

## **Legal Forms of Civil Society Organizations as a Governance Problem: The Case of Switzerland**

**Georg von Schnurbein<sup>1</sup> and Daniela Schönenberg<sup>2</sup>**

*Associations and foundations are typical legal forms of Civil Society Organizations (CSOs) in Switzerland. During the past years, several transformations of associations into foundations can be observed. This study analyzes the legal and managerial aspects and consequences of CSO transformations. It highlights the differences in the governance structures, and displays the changes in terms of members' rights, control, and accountability. The managerial analysis gives a preference to the foundation governance structure according to coordination, decision-making, and innovation.*

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### **1. Introduction**

In Switzerland, associations and foundations are the most common legal forms of civil society organizations (CSOs). Under certain conditions, both are CSOs. However, there are considerable differences between these two legal persons under legal and managerial governance aspects. Although the choice of the legal form is of long-term influence, it is rarely done based on strategic considerations. Often, the choice is mainly influenced by reasons of practicability, costs, or habit. While the organization develops, the legal form might become inappropriate or even restraining. However, if a CSO changes its legal form, some legal constraints have to be taken into account. From a managerial perspective, the changes in the strategic management of an organization have to be respected.

Until now, the literature has put an emphasis on analyzing the influence of different governance structures among profit, public, and nonprofit organizations (NPO) (Eldenburg and Krishnan, 2003). While the differences between these varying legal structures can be demonstrated, less knowledge has been gained about the differences within legal forms of nonprofits. This article analyzes the reasons for and the consequences of CSO transformations in the Swiss context. In Switzerland, a trend of transformation of associations into foundations can be observed (von Schnurbein, 2008). Employment in foundations grew much more than in associations. This extreme difference cannot simply be explained by the growth of the

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foundation sector during the last years. The other reason is the shift from associations to foundations through legal transformation. Hence, our research question focuses on two major aspects: What are the legal and managerial consequences of CSO transformations for the governance structure?

**2. Legal differences and reasons for CSO transformations**

The study is based on theoretical considerations from literature reviews and the analysis of Swiss law. It is an interdisciplinary paper where legal and managerial aspects are taken into account. The article is enriched with results drawn from different case studies of CSO transformations in Switzerland.

Under Swiss law, associations and foundations are both legal persons regulated in the Swiss Civil Code (CC). However, there are quite significant differences (table 1). Associations are corporate entities whereas foundations represent establishments.

Associations are constituted by owners of fractional interests in the entity’s assets (members) who have decision-making power. The articles of association may be changed in the general meeting.

Foundations are legal entities constituted by a founder by dedicating the assets to a particular purpose (art 80 CC). Modifications of the organization and the purpose of the foundation can only be made under certain conditions (art 85 *et seq.* CC). Foundations have no members but do exist exclusively of legally independent assets. Foundations are set out with its own governance bodies, i.e., the foundation board. Foundations are in contrast to associations subject to supervision by a public authority.

*Table 1: Differences between associations and foundations under Swiss law:*

	<b>Association</b>	<b>Foundation</b>
Legal person	Corporate entity	Establishment
Member	Juristic persons or natural persons as members	No members
Alteration of the will	Will may be altered by the members	Will may not be altered
Change of articles	Articles of association may be changed by the general meeting	Articles may be changed by the founder under the conditions of art 86a CC
Liquidation	Association may be liquidated through a decision of the members	Association may not be liquidated through a decision of the founder or the foundation board
Reassignment of assets	Not possible because of tax reasons	Not possible because of regulations in the CC
Supervision	No supervision by a public authority	Supervision by a public authority

There exist considerable differences between associations and foundations with regard to members and the decision-making process. An association that transforms into a foundation tries to benefit from the advantages of the newly chosen legal form. There are various reasons that can move an association to transform into a foundation, e.g., because of the desire for independence

(ZEWO<sup>3</sup>), governance (Brot für alle, Freunde der SOS Kinderdörfer, Helsana), asset protection (Huelfsgesellschaft Winterthur), or access to new donors (Verein Kinderschutz Schweiz).

The Huelfsgesellschaft Winterthur, which has supported persons in need in the city of Winterthur for nearly 200 years, may be mentioned as an example. The association was transformed into a foundation in 2007 to secure its assets for the long term. The association worked in a similar way to a foundation by distributing assets to beneficiaries. It was difficult to engage members actively, and the benefit of the membership was restricted to the ideal support of the association. The board of directors worked independently, and was confirmed or complemented at the annual general meeting by a modest number of members. The transformation from an association to a foundation served to secure the assets and left out the possibility to make some organizational changes in the future (von Schnurbein, 2008).

Statistical evidence of the increased number of transformations can be taken from the official statistics of employment. In the period from 1995 to 2005, employment in associations grew by 3.8 per cent, in foundations by 45.9 per cent, and in the economy in general by 4.2 per cent. The development of working units<sup>4</sup> shows even more significant differences. Among associations the number of working units decreased by 20.5 per cent, while the number of working units among foundations rose by 26.3 per cent (the general economic development rate was 0.1%). These figures allow the assumption that the growth among foundations is not only due to new establishments, as foundations usually do not employ many people. Moreover, we assume that the increase is partly a result of the transformation of associations into foundations.

Compared to establishment of a legal person, a transformation is a decision where legal and managerial aspects have to be taken into account (Nowotny and Fida, 2007). Thus, the following section analyzes the legal and managerial aspects and consequences of the transformation of CSOs.

### **3. Legal aspects of the transformation under Swiss law**

The federal law on merger, demerger, conversion, and transfer of assets and liabilities (subsequently referred to as *Merger Law*) entered into force in 2004. This law regulates amongst other things the adaption of the legal structures of associations and foundations in connection with mergers, demergers, conversions, and transfers of assets and liabilities (see art 1 para 1 *Merger Law*). However, the direct conversion of an association into a foundation is not possible even though there are associations with activities similar to those of foundations (e.g., the allocation of assets for certain purposes).

The transfer of assets and liabilities from the association to the newly established foundation (art 69 *et seq* *Merger Act*) may serve as an alternative option. This transfer regards only the association's assets and not the members' rights. The latter exist until the liquidation of the association. As the liquidation of the association is not imperative, the association may continue to exist as a sponsor of the new foundation. However, it could lead to a factual liquidation of the association if all assets of the association are transferred to the foundation. The association's members lose their rights with the liquidation of the association. The question then arises on how the former members may be integrated in the new structure.

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<sup>3</sup> Switzerland's leading association of donation-funded charity organizations.

<sup>4</sup> A working unit is a geographically distinct unit of an organization (e.g., a company) with a minimum paid working activity of 20 hours per week.

The transfer contract shall be concluded by the supreme managing or administrative body of the association (see art 70 Merger Law). According to art 69 CC, this is the board of directors. If all assets are transferred, a two-thirds majority of the members of the association is needed. A re-transformation from the foundation back into the association or any other legal form is not possible.

It may be seen as a positive aspect that, due to the new governance structure, the foundation could gain independence from the democratic structures that dominated the member-based association. In a foundation, the duties are concentrated on fewer persons as the organs of a foundation are usually smaller, and there are no members with a right to participate. The board of a foundation has the decision-making power. Therefore, higher flexibility in the management of a foundation may be achieved as there are no changeable wishes of members that must be respected; thus, long-term planning becomes easier.

The downside of this transformation may be seen in the fact that, because of the absence of members in a foundation, there is no possibility to integrate donors directly into the legal person. Furthermore, the purpose of a foundation as set forth by the founder is, in principle, fixed and cannot be modified after the establishment of the foundation. This inflexibility may be seen as a disadvantage to a CSO, which should be adaptable to new trends.

In the following section, the legal consequences of the transformation are analyzed with regard to members' rights, control, and accountability before and after the transformation.

### *Members' Rights*

As mentioned above, the main difference between an association and a foundation is that the former has members whilst the latter does not. The question arises how the former members' rights might be preserved after the transformation of an association into a foundation. This section (i) outlines what rights the members have in an association; (ii) discusses whether former association members may be regarded as founders of, and therefore exert influence on, the new foundation; (iii) tackles the possibility of former association members, or some of them, being appointed to the foundation council; and (iv) discusses possible ways through which former members may be protected.

(i) An association has at least two organs: the general meeting (art 64 para 1 CC) and the board of directors (art 69 CC). The general meeting has different indefeasible competences (e.g., the authority to change the articles of association, supervision authority, and the right to recall the board of directors). Thus, the general meeting may change the articles of association in order to adapt to changing circumstances.

In Switzerland a lot of associations do exist. They are, for example, used for sports clubs and choirs. The members have the right to administer the association and use its assets. However, the members also have the right to be protected. Art 75 CC protects the legality of corporate life: Each member shall be entitled by force of law to challenge in court, within one month of his having gained knowledge thereof, resolutions that he has not consented to, and that violate the law or the articles of association.

The Swiss NPO Code<sup>5</sup> is devoted to safeguarding the interests of association members. According to § 7 para 1 of the Swiss NPO Code, all members are entitled to voice their opinion

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<sup>5</sup> The Swiss NPO Code is a governance guideline for non-profit organizations in Switzerland, which was edited in 2006 by the Conference of the Presidents of Large Humanitarian and Relief Organizations of Switzerland.

on the items on the agenda, and to exercise their corresponding right to vote on the occasion of the general or delegates' assembly. However, it has to be mentioned that the protection of members' rights under the Swiss NPO Code is not as broad as under the Swiss Civil Code since the Swiss NPO Code is only subject to the rule "comply or explain."<sup>6</sup> If an association does not adhere to a regulation laid down in the Swiss NPO Code (if this is possible under the Swiss law), it has to be publicly and clearly justified.

(ii) May the former members of the association exert influence on the new foundation? May they, for example, modify the purpose of the foundation? There is a difference between if the association as a legal person acts as founder and if its members become the founders of the foundation.

Since the revision of the Swiss foundation law, there has existed a new art 86a CC (in force since 1 January 2006), according to which a founder may request for modification of purpose. However, according to art 86 para 3 CC, if the foundation is a legal entity, the right to modify its purpose lapses, at the latest, upon the expiration of 20 years after its establishment. If several persons have established the foundation, they may only jointly request modification of the purpose of the foundation (art 86a para 4 CC). If the association as a legal body is the founder, it may request modification of purpose. However, it should be kept in mind that the association should not be liquidated after the transfer of assets to the foundation, as otherwise nobody may claim founders' rights. If the founders are the former members of the association, the modification of the purpose of the foundation will often fall short of the required unanimity in art 86a para 4 CC, especially if there are a large number of former members. Based on these considerations, it makes sense that the association becomes the founder, as the decision-making regarding the modification of purpose may be made with a quorum other than unanimity.

(iii) As the association's members cannot become members of the foundation (because the foundation does not have members), the question arises whether the former members may have influence on the foundation in another way. Is there a possibility for them to be entitled to a seat in the foundation board?

To start with, it has to be mentioned that the foundation board – in contrast to the members of an association – does not have any influence on the formation of the will of the foundation. A foundation is not able to form a will, as it is bound to the will expressed by the founder upon the formation of the foundation. However, the foundation board has discretion,

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Organizations that decide to submit to this code will declare in their annual reports, according to the principles of "comply or explain," to what degree they can apply the different recommendations of the code and, if not, on which points they cannot follow and their reasons for not respecting the "best practice." The Swiss NPO Code is a joint undertaking by 20 large and autonomous Swiss humanitarian non-profit organizations (NPOs) that joined forces to define up-to-date principles for the responsible and transparent Corporate Governance of Swiss NPOs. According to § 1 Swiss NPO Code, the code addresses, based on the Swiss GAAP FER 21 definition, the governing bodies of large non-profit organizations domiciled in Switzerland which provide charitable services in the general interest, and publicly address an undefined number of donors, receive pro bono donations, and/or dedicated public funding. The Swiss NPO Code may be applied under certain conditions to associations (II. title, cipher 1 Swiss NPO Code) and foundations (II. title, cipher 2 Swiss NPO Code).

<sup>6</sup> Swiss NPO Code, page 25: The "comply or explain" principle forms the basis of the European code-based approach to Corporate Governance. Non-adherence to a specific aspect of the Swiss NPO Code has to be publicly and clearly justified. Conversely, non-adherence to R-principles ('Recommendation') requires neither disclosure nor explanation.

within the foundation's purpose, on the fulfillment of its tasks. If the purpose of the foundation is broadly formulated, the foundation council has greater discretion.

The founder, i.e., the association or the former association's members, has the right to name the first foundation board members in the deed of foundation or regulations, and to regulate the appointment of their successors. There is a possibility to appoint the former association's members as members of the foundation board. The members may be appointed for life. Nevertheless, it becomes problematic if a plurality of former members claims a seat in the foundation council. Although the size of the foundation board is not regulated under Swiss law, its ideal size results from the function of the foundation board as supreme leading organ. Baumann (2009) determines that, for the purpose of efficiency, small and medium foundations should have at least three and a maximum of five members in the foundation board, and big foundations at least seven and a maximum of nine members. The former members would have the chance to become a member of the foundation board, one after another, if a limitation on the mandate is introduced and the procedure on the appointment of successors is regulated.

(iv) The Swiss NPO Code protects the former members and co-founders, as well as donors/sponsors as they support the foundation financially without getting the rights of the members of an association. According to § 11 para 1 of the Swiss NPO Code, full disclosure in the form of a business report is required in order to inform co-founders and donors/sponsors of the use of their contributions; they are to be granted information on the development of the organization and the strategic management-body's business policies. According to the commentary of the Swiss NPO Code, the willingness to engage in a dialogue should be encouraged with this regulation. Former members of the association have another right, according to § 12 para 2 lit. h Swiss NPO-Code: The members of the council of governors have to keep all members regularly informed, ensuring transparency concerning the use of funds.

To conclude, in comparison to an association, a foundation has no members. With the transformation from an association to a foundation, the members lose all their statutory rights. The former members of the association may still have a certain influence on the foundation. On one hand, they have as founders (i.e., the association or the former members of the association) the right to modify the purpose of the foundation. On the other hand, the former members may take a seat in the supreme corporate body of the foundation, which may have discretion in the implementation of the purpose of the foundation. The Swiss NPO Code grants the right to information regarding the foundation to the former members of the association. However, under certain conditions, this right does not have to be respected. In addition, the greater the number of members, the more difficult the division of founders' rights becomes. Thus, in many cases the association is not liquidated but remains as a donor club with close connection to the foundation. With all this said, it has to be stressed that the former members of the association have far less rights in the foundation than in the association, and lose some rights as well (e.g., the right to change the articles of association).

### *Control*

The control of an association lies within the power of the general meeting, which is constituted by its members. The general meeting is the supreme corporate body of the association (art 64 para 1 CC). It supervises the activity of the organizational bodies and may, at any time, dismiss them without prejudice to the contractual rights of the dismissed persons (art 65 para 2 CC). The supervisory right as well as the demission right are indefeasible rights of the

supreme corporate body. The general meeting may exercise control over the board of directors and dismiss the same if it does not agree with its actions.

There is no possibility to restrain the autonomy of the general meeting to issue or amend the articles of association. The right of the meeting to change the articles of association may be seen as a certain possibility for control.

A foundation does not have members – also the founder cannot be a member – who may control the actions of the foundation's organs. How can the former members of an association proceed against the actions and omissions of the foundation board? In principle there is no possibility to challenge the decisions of the foundation board in court. An exception is the declaration of nullity of such a decision. According to art 84 para 2 CC, the supervisory authority shall ensure that the assets of the foundation are used according to their purpose. The supervisory authority has to ensure that the foundation board does not violate the law, the foundation deed, and relevant regulations, and that it does not exercise its discretion incorrectly. The doctrine deduces from art 84 para 2 CC the right to file a complaint with the supervisory authority. The supervisory authority has to look into the complaint and grant party rights. Anyone with a close interest in the foundation has the right to file such a complaint. These include, for example, the actual and potential beneficiaries of the foundation, the founder and his or her heirs, a potential executor of the founder's last will, as well as the organs of the foundation and its members (e.g., the overruled members of the foundation board). If the former members of the association are not the founders of the foundation, members of the foundation board, or potential beneficiaries, there is no possibility for them to file a complaint with the supervisory authority. They only have the right to report their observations to the supervisory authority, according to art 84 para 2 CC. As this is not a proper legal remedy, they do not get party rights, nor is there a possibility for them to appeal against a possible negative decision of the supervision authority.

It is possible to give the former members of the association the right to dismiss the foundation board to assure their influence on the foundation. The foundation deed or regulation may provide for a regulation stating that the foundation board or third persons may dismiss members of the foundation board.

There is a difference between an association and a foundation with regard to the separation of powers. The separation of powers is a crucial element of the Swiss NPO-Code, which states in it § 6 that strict separation has to be observed between individuals serving in the strategic management body and those serving in an operative management capacity. § 10 Swiss NPO Code is devoted to the separation of responsibilities with regard to the foundation. It is possible that the council of governors assumes both the function of the highest governing body as well as of the strategic management body. If the foundation board has such double function, it has to ensure full transparency with regard to how this double function is carried out (see § 10 para 2 Swiss NPO Code).

To sum up, it may be stated that state control through the supervision authority cannot be compared with the control exercised by the members in an association. First, the former members have only, under the above-mentioned conditions, the possibility to do something against the acts and omissions of the foundation organs. Second, state control takes place retrospectively. The supervision authority will hardly be able to impede imminent misuses in time. Thus, granting the former members the right to dismiss those members of the foundation board who do not fulfill the expectations should be considered. The separation of powers



between the strategic and operative management bodies does not go as far in a foundation as in an association.

While the exertion of control through members offers democratic legitimacy towards the public, the state supervision of foundations ensures an independent control mechanism. As accountability is becoming more and more important today, independency of supervision is rated higher than democratic legitimacy.

### *Accountability*

The members of the board of directors of an association and the members of the foundation council are binding as bodies of the legal entity through the conclusion of legal transactions as well as through their conduct otherwise (directors' and officers' liability) (see art 55 para 2 CC). Furthermore, persons in acting positions shall be personally liable for their fault (art 55 para 3 CC). Therefore, the liability of the above-mentioned persons for culpable action is not excluded. Art 55 para 3 is not an independent liability rule; for example, the conditions in art 41 of the Swiss Code of Obligations for general liability in tort have to be fulfilled. The board of directors has the right and the duty to attend to the affairs of the association, and represent the association in accordance with the activities conferred to it under the articles of association (art 69 CC). It is responsible to the general meeting (see art 65 para 2 CC).

The board of directors of the association are not only liable to the members of the association and third parties but also to the association itself. In the latter case, a member of the association may file an action against the association and claim for payment to the association. This claim may only be made if the members of the board of directors did not file the action. The association may discharge the members of the board of directors from liability. With this procedure, the association renounces making a claim during a certain period of time. The discharge is only valid for facts that are known at the time of the resolution. The right to claim of members that did not agree expires upon six months after the resolution (in analogy to the right to claim in corporations). The resolution with regard to the discharge does not have external effects. The creditors' rights to claim will not be restricted.

The foundation board may become liable to the foundation as well as to third parties (beneficiaries and creditors). In principle, the foundation and the supervision authority (but not the beneficiaries) are authorized to file an action. The enforcement of such rights often fails for lack of interest among the members of the foundation board. Due to the fact that a foundation does not have members who take care of the interests of the foundation, the supervision authority has to enforce the claims. In foundation law, there is no possibility for either the supervision authority or anybody else to grant the foundation board discharge from its liability (Sprecher/von Salis-Lütolf, 1999). Although this is mentioned in § 9 para 2 lit. e Swiss NPO Code, there is no possibility to give discharge to the council of governors.

A question arises concerning to whom the foundation board is responsible. A foundation may be responsible to the beneficiaries, to the supervisory authority, or to its donors. In practice, nonprofits have a tendency to report primarily to their donors (Callen, Klein, and Tinkelman, 2003). To secure their donors, foundations often create complementary donor clubs that "copy" the principles of associations but without the democratic influence on the organization's activities.

In conclusion, we can say that, in contrast to the law of associations, foundation law does not recognize the possibility to give discharge to the foundation board. Discharge may only be given to a board of directors of an association with regard to the association, but the board of directors remains liable with regard to third parties if certain conditions are met. While the members of an association may enforce their rights, comparable claims in a foundation can only be made by the supervision authority.

#### **4. Managerial consequences of the transformation**

The legal aspects of the transformation are concentrated in the process of transferring assets and liquidating the association. However, from a managerial perspective, the differences in the governance structures and the coordination before and after the transformation are of special interest. Usually, the operations and external perception of a transformed nonprofit do not change considerably. However, on the strategic level extensive differences can be observed. Schwarz et al. (2005) differentiate five management tasks of nonprofits, which comprise the structure that will be used for our analysis: organization, leadership, decision-making, coordination, and innovation.

##### *Organization*

As mentioned before, members are a constitutive criterion of associations. The members execute various roles within the association (Schwarz, 2005). First, they are the constitutional body of the association, and they contribute financially to the association through member fees. Second, the members invest time as volunteers, and members of boards and advisory groups. Third, the members profit from the services of the association and might profit from special conditions. Thus, the members are, at the same time, a legitimating body and primary beneficiaries of the association. This constellation is not possible in a foundation, which has no members at all.

The foundation is an independent organization that is structured centrally. A foundation can be a member of an association or a federation itself. However, federal structures beyond membership have to be organized via contracts. Most importantly, regional or local organizations cannot become members of a national organization that is a foundation. Apart from drafting contracts, another solution is to guarantee the regional units a position in the board. However, this limits the board's capacity to act independently. Moreover, there are no direct possibilities for the beneficiaries of a foundation to participate in decision making.

##### *Leadership*

Democratic elections are the primary means of leadership enactment in associations. In federal structures, a stepwise procedure assures the legitimacy of the elections at all levels. Regional units elect their delegates, who vote for the members of the board of trustees. Finally, the board of trustees elects the CEO and the board of directors. At every stage, the voting organ is afterwards in control of the elected organ. Member fees are another instrument of leadership enactment. If the members are unsatisfied with the association's leaders, they can express their complaints by leaving the organization (Hirschman, 1970). If this happens significantly, the association's leaders will have to react. A notable example in Switzerland was the dispute between Swissmem, the trade association of the metal industry, and *economiesuisse*, the umbrella organization of the Swiss economy in 2006. Swissmem, the biggest payer of fees to *economiesuisse*, threatened to leave the organization because it was unsatisfied with the latter's

policy. After several negotiations, Swissmem remained a member but with a reduced membership fee; in addition, the president-elect of *economiesuisse* lost his post in the following elections.

### *Decision-making*

The decision-making process in associations is shared by organs on several levels. In reality, the absence of participation of a major part of the members and the high influence of the elected boards tips the association away from democracy and creates a tendency towards oligarchy. In contrast, a foundation is per se an oligarchy, and decisions are taken independently and by one board. Thus, the decision-making in foundations can be realized more easily and more quickly. This is because, one, the foundation's board recruits its members mostly through co-optation, thus reducing the danger of fragmented boards because the existing board members vote for people like themselves; and two, foundations do not have to ask for legitimacy as long as they follow their stated purpose.

### *Coordination*

Coordination encompasses the planning, quality management, and accountability of an organization (Schwarz, 2005). Strategic planning does not only mean goal definition but also the strategic coordination of planning in general. In the legal section, it became evident that associations can change their statutes and purpose at any time on the basis of members' votes. This allows them to react to changes in their environment. However, the purpose of a foundation basically cannot be changed. It can only be interpreted, but it remains rather inflexible. Thus, through the transformation the organization takes a decision with long-term consequences.

The major difference in the accountability of the organization is the change from membership supervision to state supervision. The supervision of members has a reputation for amateurism, and growing regulations are leading associations into external revisions. State supervision offers an independent opinion, which is dominantly reduced to formal and legal aspects.

### *Innovation*

Innovation is oriented toward organizational development and the ability to implement organizational change. In associations, two ways of development are possible. On the one side, innovation can start at the top level of the organization, initiated by the board of directors or the board of trustees. On the other side, the members can develop innovative ideas and bring them into the organization. Thus, the active participation of the members is a stimulatory element of organizational development. On the contrary, the members can consequently prohibit innovation and make organizational development impossible. In a foundation the board has much greater assertiveness and can easily implement change processes. However, the foundation lacks the innovative potential of member participation. Thus, organizational development is always a top-down process.

To conclude, the advantages and disadvantages of the transformation from an association to a foundation have been analyzed from a managerial point of view. The foundation has an advantage in having lean structures and smaller human resource requirements. On the one side, in times of decreasing voluntary action, foundations have a strategic advantage. On the other side, they are lacking subunits where interested and engaged members can gain their first

experiences in voluntary boards. Foundations have the potential to make and implement decisions faster than associations can.

In contrast to the tedious and sometimes uncontrollable democratic processes of associations, the management of and coordination within foundations are better organized. Nevertheless, in practice there are many foundations with encrusted structures and old-fashioned management concepts. One reason for this might be that foundations do not feel external pressure to change, even from their members.

## **5. Conclusion**

The main legal differences between foundations and associations lies in the fact that foundations have no members, have no influence on its purpose, and are under state supervision. If an association is transformed into a foundation, the crucial question arises of how the rights of the former members of the association may be respected in the new structure and what the effects on the control and accountability are.

There may be various reasons for a transformation (e.g., due to governance considerations). Due to the fact that there is no possibility to change an association directly into an association, one has to make the detour of transferring the association's assets to a newly founded association.

In transforming an association into a foundation, the advantages and disadvantages of the different legal forms have to be kept in mind. Every foundation that wishes to be transformed should analyze carefully if its intended goals can really be achieved. All the same, foundations are becoming more attractive, and there have been more transformations observed recently. There are differences as well between foundations and associations under a legal and an economic point of view. In most cases, these differences do not have any effects on the business operation as the transformation seldom attacks the character of an organization. Hence, it seems reasonable to allow the direct change from an association to a foundation without having to take the detour of transferring assets. Such a possibility would fulfill the need of an association with tasks similar to that of a foundation (e.g., associations with a fairly small number of members, which distribute their assets to beneficiaries).

Considering the legal restrictions of a transformation, Riemer (2001 and 2003) would appreciate the possibility of a direct change from an association to a foundation in art 54 para 5 of the Merger Law. In his view, the argument of the members losing their rights is de facto not valid. From a managerial perspective, the relatively small impact of a transformation on the organization's operations and external appearance simplifies the realization.

The managerial analysis shows that foundations have some advantages, especially in terms of decision-making, coordination, and innovation. However, the implications for the strategic level are not trivial. Hence, a transformation has to be well planned and executed in order to avoid problems in the structure of the foundation later on.

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