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## The Charity Law and Practice Review

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# LEGAL STATUS OF NGOs IN THE RUSSIAN FEDERATION<sup>1</sup>

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### Constitutional guarantees for NGO activity

Article 30 provides the basic right: freedom of association. The same article also guarantees the freedom of action of public associations and further states that no-one can be forced to join a public association.

The constitution guarantees that Russia will be ideologically diverse, with many political partners and outlooks and no required government viewpoint (Chapter 1, Article 13(1)(2)(3); "Public associations are equal before the law" (1.13(4)). The constitution further guarantees freedom of religion and the equality of religious associations before the law (1.14(1)(2)).

The constitution also contains a broad spectrum of provisions in the realm of charity - social protection, education, culture, environmental protection, and such like (Ch 2, Arts 38-44). Charitable activity is itself a protected right (Art 39(3)), and the right to association in the various forms of charitable organisations is also guaranteed.

### Main governmental bodies that deal with NGOs

NGOs interact with a wide range of governmental bodies on the federal and local levels. First in importance is the Ministry of Justice, which has a central federal

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office, and numerous local offices and, through its Department of Public Organisations, is responsible for registering NGOs. The Duma's Committee on the Affairs of Public Associations and Religious Organisations oversees law projects in this area. Other important agencies include:

the Tax Inspectorate's Department for the Tax Obligation of Non-commercial and Co-operative Organisations;

the Ministry of Social Protection's Department for the Problems of the Family, Women and Children;

the Ministry of Culture; and

the Commission of the Administration of the Russian Federation on Humanitarian and Technical Aid

Most recently, the federal administration formed a new organisation dealing with NGOs. In February President Yeltsin created the Public Chamber where both political parties and NGO's are represented. The reason for its creation is to give advice to the President on the issues on which wants to be consulted. There has been considerable criticism about the work of this Chamber in the media because it can not do much without approval from the authorities, but the very existence of it is an important factor.

Local governments also have their own specialised branches dealing with NGOs. For example, the Moscow City Government has a Commission on the Affairs of Non-commercial Organisations and a Division for the Co-ordination of Charitable Foundations and Humanitarian Aid. It also has other specialised branches on freedom of conscience and public organisations.

NGOs will also find it helpful to approach the social welfare departments of their city districts and micro-regions. City officials in these local departments can provide invaluable assistance in co-ordinating volunteer programmes. For example, department officials in Moscow's VDNKh district provided a list of home-bound invalids to Earth Day Russia's "Babushka Relief Project". They can also prove helpful in organising and promoting conferences and special charitable projects.

### **Substantive rights NGOs possess**

NGOs that operate as juridical persons enjoy a full range of legal rights and privileges (Civil Code 23). These include the right to

- open bank accounts in rubles and hard currency

- open an office
- enter into contracts, including leases
- hire employees
- own property, including stocks (nb Civil Code, Arts 102-104; Law, "On ownership in the RSFSR", 1990 III.17, 18; "On public associations", III.18)
- appoint representatives and establish representation (nb Civil Code 66)
- conduct business activity and establish enterprises ("On Ownership, III.17, 18; Law, "On Enterprises and Entrepreneurial Activity", 25th December 1990 with subsequent changes, Arts V.2 and V.3)
- receive hard currency without mandatory sale into rubles (Law, Basic Provisions on Regulating Hard Currency Operations in the Territory of the SSSR, 24th May 1991, with subsequent amendments, Part I, Art 4(e); Instructions of the TsBR "On the Order of Mandatory Sale by Enterprises, Associations and Organisations of Part of Hard Currency Proceeds", 29th June 1992 with subsequent amendments, Art 4).

Under Moscow regulations on non-commercial organisations, registered representative offices of a foreign NGO can open a bank account, receive an official stamp and perform other operational necessities (Prilozhenie to the Rasporyazhenie of the Mayor of Moscow, 29th December 1992, No 598-RM).

### **NGO registration**

To enjoy any legal privileges, NGOs register.

To obtain legal status, i.e., status as a juridical person, most organisations will register with the Ministry of Justice - federal or local - or local agencies concerning non-commercial or public activities in the standard way. In Moscow, foreign representations also register as non-commercial organisations in order to gain formal recognition for their activities. Representations can also register with the Chamber of Commerce of the Russian Federation or local bodies authorising representations.

Though it does not grant official legal status, registration with the tax authorities is also necessary. This is necessary whether or not the NGO expects to owe tax. If the NGO has Russian employees, it will at least have to pay the requisite 39% social security taxes (pension fund, employment fund, medical insurance and social protection fund) and, in most instances, at least part of employees' personal income taxes. The NGO must also present accounts for purposes of the profit tax, property tax, etc. The requirements in this area are rather strict, and addresses and phone numbers of the requisite registering bodies vary from place to place and change frequently, so an NGO would be wise to seek the services of a knowledgeable accountant as soon as possible.

### **Main organisational forms of NGOs**

Legal status is obtained in Russia by becoming a "juridical person" (Civil Code, Ch 2, Arts 23-40). A juridical person bears legal responsibility for its actions, possesses property and other legal rights, and has the authority to establish representations. Affiliates and representations of juridical persons also can conduct transactions on behalf of the parent organisation, but they do not themselves have legal status as a juridical person (Ch 4, Arts 62-70).

The 1990 law "On public associations" and the April 1993 "Current Rules of Registration" continue to remain the central means for establishing legal status for most NGOs. They provide for various levels of administrative authority. All-Russian public associations, which must have activities in all or most of Russia, are registered by the federal Ministry of Justice. Interregional and international NGOs can be registered by either the Ministry of Justice or the corresponding body of one of the united republics. All other organisations are to be registered by the co-ordinate Justice division in the region in which they will be active ("Current Rules", 4). In this context, it is important to note that the term "international public organisation" does not include all international NGOs - only those "created" (V 24) in Russia and conducting activity in one or more foreign countries.

The specific form of the organisation is not addressed in the 1990 law, but in practice there are two options. The organisation can be a self-standing organisation with a core set of members who elect the officers and conduct business, or a branch office. Also, branch offices of All-Russian or International public organisations must register with the local authorities in the area in which they are working. To avoid this, an organisation may simply establish a representation, which can act on behalf of the parent organisation but lacks formal status as a juridical person.

These distinctions are particularly important for foreign organisations working on Russian territory, since the parent organisation often desires to maintain active oversight and control. The primary means of securing control are either to send

representatives or to create branch offices, with provisions in the by-laws to have officers and decisions made or approved by the parent organisation.

Another important aspect of practice is the formal title of the organisation. Western terms, such as "membership organisation", and "non-membership organisation" do not have formal, strict legal definitions. This can lead to some confusion, since most organisations do not conceive of their membership in terms of active participants, the only definition suggested in the law ("On public association", II.9). Likewise, "foundation" remains a flexible legal concept and does not engender separate regulatory regimes, as, for example, in the United States and Germany.

### **Registration procedures**

There are a number of ways to register an NGO, depending on its goals and the scope of its activity.

#### **1. Public Organisations**

The formal definition of public organisations is rather broad: "Voluntary formations, arising as a result of the free initiative of citizens, uniting on the basis of common interests" ("On Public Associations", I.1). Practically speaking, this includes charitable organisations except those singled out by special legislation (see 1, 2 and 3 above), political parties, mutual benefit societies and any other citizens' group.

In order to register, an organisation must meet several requirements. First, it must consist of at least ten Russian citizens. This is simply a basic membership requirement; these citizens need not have any capacity as directors.

An organisation must also file the following documents with the Ministry of Justice or its local branch:

- (1) The official application form for the Ministry of Justice, signed by members of the governing body;
- (2) The minutes of the public organisation's founding body, signed by representatives of all the members, including
  - the date and number of founders
  - selection of officers for the meeting (chairman, secretary)
  - agenda; creation and goals of organisation

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- legal address of the organisation
  - membership provisions
  - governing bodies and their members
  - powers of the organisers
  - procedure for control measures
  - approval of the by-laws
  - signatures of the chairman and secretary of the meeting
- (3) Two copies of the by-laws, which must include
- the organisation's name, goals, tasks, and territory of activity
  - membership procedures, rights, and duties
  - the organisation's sources of finance and property
  - procedures for amending the by-laws
  - procedures for dissolving the organisation
- (4) Documents confirming the organisation's legal address (guarantee letter or agreement for renting space)
- (5) The names, addresses, place of residence, date of birth, and passport data for founders that are physical persons; for founders that are not physical persons, the name of the association, legal address, date and place of registration of the by-laws, and bank account information
- (6) The names, addresses, place of residence, date of birth, and passport data for the officers of the governing bodies
- (7) A bank receipt confirming payment of the registration fee,
- Department of Justice for Moscow, 500 rubles
  - Ministry of Justice of the Russian Federation
- international organisation - 5,000 rubles

interregional organisation - 2,000 rubles

- (8) Documents proving the organisation's international or interregional status

According to the "Current Rules", the registration process will be completed within a two-month period from filing all necessary documents (18); the possible results are registration, refusal to register, and stopping the application without review (20). Amendments to the by-laws are to be registered in the same order and time as the by-laws themselves (23).

Organisations that wish to conduct professional activity in certain areas - such as medical work, education and culture - should also obtain the proper licence. Such licensing, however, is not needed to become a juridical person.

## **2. Religious Organisations**

The regime for religious groups, "The Order of Registering By-laws (Articles) of Religious Associations" is similar to that of public organisations, with the same requirements for minimum number of founders and similar requirements for the by-laws.

## **3. Non-commercial Organisation or Representative Office or Affiliate of a Non-commercial Organisation (City of Moscow)**

The Moscow City Government has responded to the federal policy's problems by adopting its own legislation on registering non-commercial organisations. There were two acts introduced by the Mayor of Moscow: "Regulations Statute (Polozenie) on the Procedures of Registration of non-commercial organisations in Moscow" N 598-PM enacted on 29th December 1992 and "Temporary Statute on Governmental Non-commercial Organisations in Moscow" N 298-PM adopted 30th April 1993. Both documents established much wider possibilities for NGO registration, of NGO allowing to act as founders not only as physical persons, but also public associations, religious groups, educational and cultural organisations, local territorial organs of self-governance and other non-commercial organisations formed in due course. These regulations are the only ones which are providing specific procedures for registering a representative office of a non-Russian NCO, and it self-consciously presents itself as an interim measure before the federal reform. Registration grants full rights as a juridical person, with the exception of representative offices of international organisations. As in registration

with the Chamber of Commerce (below), representatives possess rights only through their parent organisation.

Organisations contemplating registering as a public organisation should note that the Moscow City Government has become more selective as to the kinds of organisations it will register. The city, based on the Law of Public Associations, refers all membership organisations and mutual interest groups (philatelist clubs, numismatists, etc) to register with the local branch of the Ministry of Justice.

According to the regulations published on 29th December 1992, the material necessary for registering Russian non-commercial organisations includes written application, decision of the founders on creating the organisation, information on the founders, 4 copies of the by-laws, document concerning the legal address and receipt for payment of the registration fee. Accreditation as a representative office includes the application, decision to establish a representative office, copies of the by-laws, and a copy of the certificate of registration, with foreign documents translated and legalised in a Russian Consulate abroad. In each successive year non-commercial organisations must present to the city government an annual financial report.

#### 4. **Representative Office (Chamber of Commerce and Industry)**

International NGOs can obtain representation status by registering with the Chamber of Commerce and Industry, but this process is not specifically designed to accommodate non-profit entities. Rather, the procedure is designed for representative offices that will be engaged in business contracts and exchange of goods, or industrial co-operation with Russian enterprises and state bodies.

According to the rules promulgated by the Chamber of Commerce and Industry ("Documents Necessary for Accrediting a Foreign Firm in the Russian Federation"), the foreign representative office must meet the following requirements:

- (1) Written application, complete with name, when the firm was created and its location, subject of its activity, administrative bodies and directorship, agreement for representative office in accordance with by-laws, goals of opening representative office, activity, information on business connections with Russian organisations and concluded agreements or commercial arrangements, and also prospects for joint development.



- (2) By-laws or articles of incorporation of the firm (or other document, necessary in the local jurisdiction).
- (3) Certificate of registration.
- (4) Recommendation letter of a bank or banks serving the firm, containing information on the firm's financial resources.

All documents in (2), (3) and (4) must be translated into Russian and legalised in the Consulate of the Russian Federation abroad. Subsequent to registration, the organisation must present an annual report that notes commercial activity in the Russian Federation, all changes of foreign staff, all changes of Russian staff, and all changes of cars.

This mode of registration comes with steep costs: a \$1000 registration fee, tax status as a business rather than a non-profit or charity, and the absence of the property rights afforded public organisations or even self-standing, commercial enterprises. The office, with the designation of the main governing body, can rent an office and open bank accounts, but its activity can have legal status only through the main - not the representative - organisation. Moreover, recognition of the office is valid only for three years, after which time the Chamber has the right to review the organisation's activity and rule on whether to continue to validate it.

### **Liabilities of Members and Officers**

Article 36 of the Civil Code provides that members of any type of public organisation are not liable for the debts of the organisation. Likewise, organisations are not liable for the debts of their members, and if a branch organisation is a legal person, it is not liable for debts of the parent organisation, and vice versa. According to Article 104, buildings and "basic resources" of certain types of public organisations cannot be claimed in suits by creditors.

Directors of public organisations are liable to the degree that directors of any organisation in Russia are liable, depending on the specific circumstances occasioning criminal or civil liability. Details are found in their respective codes. The law on public associations further provides that directors going beyond the chartered goals or violating the law may be removed by the registering body (IV.20). In this context, it should also be noted that per Article 5.5 of the 30th April 1993 Moscow **rasporazhenie** (N.298-RM) on non-commercial organisations, directors are liable for their organisation's debts in the area of their competence.

### **Regulations on hiring Employees**

As noted above, employers must pay the requisite taxes on salaries. This includes payments to the pension fund, medical insurance, social protection fund, and employment fund; employers must also pay instalments on employees' personal income tax. There is also a tax on salaries above six times the minimum level of pay. Public organisations of invalids are exempt from paying into the pension, social protection, and employment funds; religious associations are also exempt from paying into the employment fund (**Postanovlenie** of the Supreme Soviet, 9th July 1993, No. 5357-1, reconfirmed for 1994).

With few exceptions, Russian employees must be paid in rubles (Letter, Central Bank of Russia, 1st October 1993, N.56, 1). The government also requires that legal entities register all paid foreign employees (Ukaz of the President, 16th December 1993, No. 2146). The latter is a new procedure with some uncertain provisions, and since non-compliance could result in deportation NGOs should take it seriously.

### **Reporting Requirements**

Registering bodies have the right to demand reports from registered organisations. The Moscow City Government requires that organisations file an annual financial report. In addition, organisations must make all requisite filings with tax authorities.

### **Government control over a Public Organisation**

The registering body also has a right of control over the by-laws themselves and the organisation's activity in pursuit of its chartered goal ("On public associations" IV.20). Whereas, say, in the US the federal government may deny tax exemption if the organisation has not taken certain steps meeting the requirements for tax exemption, in Russia the basis for official intervention is less clear.

### **Limits to NGO Activity**

The law "On Public Associations" bans public organisations that aim or work for the forcible overthrow of the Constitution (I.3). The first significant confrontations in this regard occurred in relation to banning the Communist Party and the Organising Committee of the Nationalist Party. This issue re-appeared in President Yeltsin's dissolution of Parliament in which he banned several opposition parties deemed to have fomented activity "against the law". (**Ukaz** "On urgent measures to provide for the regime of extreme emergency in Moscow", 4th October 1993, and **Rasporyazhenie** of the Ministry of Justice, "On suspending the

activity of several public associations in connection with the **ukaz** of the President of the Russian Federation, 4th October 1993, "On urgent measures to provide for the regime of extreme emergency in Moscow").

The December 1993 Constitution strengthens this provision. It forbids "the creation and activity of public associations, whose goals or activity is directed to violent change of the constitutional order and destruction of the unity of the Russian Federation, undermining the security of the government, creation of armaments, or fomenting social, racial, national and religious discord" (I.13(5)).

Another prohibition began as a protection against abuse by government agencies, political parties, and fraudulent charities, but soon became a hindrance to legitimate NGOs as well. Federal laws on privatisation, commodity exchanges, and investments specifically exclude from participation "legal entities with more than 25% of their charter capital held by the state, local Soviets of Peoples Deputies, public organisations (associations), charitable or other public funds." (See "On Privatisation of State-Owned and Municipal Enterprises in the RSFSR", 3rd July 1991; "On Commodities Exchanges", 2nd February 1993; and "On Investments", 8th August 1992).

After public organisations noted that this provision appears to freeze NGOs out of most stock holdings, the Ministry of Property clarified that the restriction only applies to "enterprises, located in the property of public organisations (associations)". It does not apply to "the public organisations themselves". (Telegram, Goskomuschestva RF, 10th February 1993, N.D-B22/951).

Public organisations are dissolved after the manner established in their by-laws (Civil Code, Chapter 2, Article 39) and can be reorganised only by the decision of their members or officers' meeting (Civil Code, Chapter 2, Article 39). Assets go to creditors, other public organisations, the co-ordinate government body, and goals consistent with the charter (Civil Code, 2.40; "On public associations", IV.22).

The above is only a basic survey of the most important legal provisions for NGOs in Russian law. The answers to the above questions indicate that despite weaknesses in definition and specificity, present law lays a legal foundation for the creation and maintenance of NGOs. Equally vital to the work of NGOs, however, is the provision made for them in the tax regime, and it is to that that we now turn.

### **Tax Policy**

Russian law does not have a uniform "tax-exempt" category; exemptions are law-specific.

Here a little history helps: prior to the widespread reform of commercial law in the early 1990s, tax advantages were given mostly to specifically named public organisations, and those, of course, were pro-government institutions. To a large extent the process of creating new advantages has been incremental rather than systematic, with exemptions regularly added for specific types and even specifically named organisations.

Perhaps the most important element on this front is the increasing advantage given to on-budget or government-affiliated organisations. For example, a May 1992 amendment to the law "On government fees" voided previous exemptions for "social protection" groups and replaced them with the government pension fund. Also, a December 1993 amendment to the enterprise profits included made donations to government theatres, museums, and so forth deductible up to 5%, a level formerly allowed only for Chernobyl groups. The deduction for donations to other NGOs, in contrast, can exceed no more than 3% of the taxable profit.

Special advantages also apply to specific types of NGOs. Organisations pertaining to invalids and the Chernobyl disaster enjoy the widest range of advantages, and in addition to specific exemptions in the main laws Chernobyl groups are also the subject of periodic resolutions and decrees granting special privileges. Invalid groups consistently enjoy the broadest privileges vis-à-vis the regular order of laws, such as the enterprise profits tax, road taxes, the Value Added Tax, etc.

In reporting to the tax authorities, groups that fall under any type of exempt activity - especially "charitable goals", a term nowhere defined by law - must take care to thoroughly document their exempt activities and be prepared to defend their privileged status before the tax authorities. The lack of precise definition in the laws means that NGOs may, and often do, encounter instances when the local office of the tax inspectorate does not agree that the NGO falls under the privileged category. This same lack of definition plagues the area of how enterprises run by charities may or may not relate to their chartered goals.

Problems in enforcement are not confined to ambiguities; officials have even been known to demand payment even when the law is clear. Alla Yaroshinskaya, a prominent author and director of her own charitable foundation, recently attempted to send material to Ukraine and officials demanded that all items be declared, in spite of the customs' laws concrete exemption for charitable freight. Charities must be prepared, as she was, to have all documents and accounts in order and at hand to challenge officials that either do not know the law or are simply looking for a bribe.

### **Receiving Charitable Funds from Abroad**

There are two ways to avoid taxation on money received from abroad. First, an NGO can have money donated to it by a physical person; such donations are

currently exempt from the profits tax. Keeping regular accounts, however, is the key to keeping tax authorities satisfied in Russia, and the more preferable and standard means of channelling funds from abroad is through grant programmes.

With regard to foreign grants, the 11th June 1993 Letter of the Government Tax Service is controlling. The letter concludes that if the donee can demonstrate that a grant came from a foreign charity, the grant is totally exempt from the profits tax. The donor and recipient must structure the funds into a grant "programme" - this is a rather broad concept, however, and a good lawyer familiar with the demands of Russia's tax authorities can structure a programme in a way that satisfies tax authorities even as it covers an organisations's normal operating expenses.

NGOs entering into grant arrangements must recognise that the demands of Russia's tax authorities differ markedly from other countries, and a foreign organisation trying to account for the use of its funds will find seeming irregularities that result from nothing more than the different expectations of Russia's accounting system.

Hard currency transfers are subject to another "tax", namely the mandatory sale of 50% of such receipts into rubles. As noted earlier in this article, however, hard currency transfers for charitable purposes are exempt from mandatory conversion. The transferor and recipient must be sure to inform the bank of the charitable nature of the transaction to avoid the sale.

The foreign charitable organisation should also provide the Russian grant recipient a copy of proof of its charitable status, such as, for American organisations, a determination letter from the Internal Revenue Service. Without this the tax authorities may question the charitable nature of the source of the funds and deem the grant taxable.

The donee must also account for how the grant was spent. The tax inspectorate letter declares that if money is used for anything but the designated activities, the grant amount must be paid into the state budget. This does not mean that changes cannot be made in the anticipated budget, just that such changes should be well-documented. In this, as in all financial matters, it is impossible to over-emphasise the importance of having a good Russian accountant.

#### **Taxation of NGOs' commercial activity**

With the exception of select types of associations and business, NGOs must pay tax on profits from their commercial activity that they conduct (Instruction, Government Tax Service of the Russian Federation, 6th March 1992, N.4, with subsequent amendments, 15). Engaging in commercial activity also makes an NGO liable for the property tax, from which it would otherwise be exempt

(Instruction, Government Tax Service, 16th March 1992, N.7, with subsequent changes, III.5).

The profit tax is calculated by subtracting expenses from receipts, with the appropriate tax to be paid on the profit. The after-tax profit can then be applied to the organisations's chartered activity. Also, the law provides that the following income is not included in calculating the profit tax: income designated for maintaining the NGO, including administrative expenses; income received from other enterprises and citizens; membership dues and shares and expenses on the account of the resources in question. Income and expenses from enterprise activity must be kept on a separate account (Instruction, 6th March 1992, 15; see also the Explanation of the Government Tax Services 14th September 1993, N. VG-4-UI/145H, questions 87 and 92).

Tax-planners in this area should take note that the law draws a sharp distinction between commercial activity conducted by an NGO and commercial activity by an enterprise - a business that is a separate juridical person - held as an asset by a public organisation or association. If the business is held as an asset and applies its profits directly to the public organisation's chartered activity, the profits are tax-exempt (Instruction, 6th March 1992, 21).

According to the customs code (Law of the Russian Federation, 21st May 1993, N. 5003-1), goods bought in as humanitarian aid (35e) and free assistance or for charitable goals by governments, administrations, or international organisations (35zh) are exempt from customs duties. The scope of 35zh extends to technical assistance.

Humanitarian aid is also exempt from the Value Added Tax. Certain other types of products are also exempt, including medical assistance (Instruction Government Tax System, 9th December 1991, N.9, with subsequent amendments, 14).

When importing humanitarian aid, an NGO must be certain to follow all of the necessary procedures in order to receive the privileges provided by law. These procedures are contained in the Postanovlenie of the administration of the Russian Federation, "On measures for conducting work with humanitarian aid", 18th March 1992, N.170. Important changes are made in the Postanovlenie of 10th August 1993, N.760. Two other postanovlenie detail the work of the Commission on Questions of Humanitarian and Technical Aid: 29th December 1991, N.89 and 23rd November 1993, N.1222.

It is important to note: that new legislation on NGOs is impending beginning next year might establish more clear legislation on certain types of NGOs (non-state "public associations" - "obshchestvennye organizatii", non-commercial and charitable organisations); and new taxation laws are also being prepared to be introduced in 1995. So the legal environment for NGOs in Russia is shaping up.