

www.ecnl.org

ICNL

International Center for Not-for-Profit Law 1126 16th Street NW, Suite 400 Washington D.C. 20036, USA Tel: +1 202 452 8600 Fax: +1 202 452 8555 www.icnl.org

A COMPARATIVE OVERVIEW PUBLIC BENEFIT STATUS IN EUROPE*

I.	INTRODUCTION	2
II.	CONCEPT AND RATIONALE	3
III.	REGULATORY CONTEXT	
1. 2.	REGULATION OF A "PUBLIC BENEFIT STATUS"	
IV.	CRITERIA FOR RECEIVING PUBLIC BENEFIT STATUS	8
1. 2. 3. 4. 5.	QUALIFYING ACTIVITIES/PURPOSES ELIGIBLE ENTITIES PRINCIPLE PURPOSE TEST GOVERNANCE REQUIREMENTS OTHER CRITERIA/CONDITIONS	11 12 13
V.	DECISION-MAKING BODY	16
VI.	CERTIFICATION / REGISTRATION PROCEDURES	22
VII.	BENEFITS FOR PUBLIC BENEFIT ORGANIZATIONS	25
VIII.	OBLIGATIONS OF PUBLIC BENEFIT ORGANIZATIONS	26
1. 2.	RULES REGARDING USE OF PROPERTY, TRANSFORMATION AND LIQUIDATION SUPERVISION AND ACCOUNTABILITY	
IX.	CONCLUSION	31

The current revised and updated version of the paper is prepared by ECNL for the Macedonian Center for International Cooperation (MCIC).

^{*} Prepared by David Moore, Katerina Hadzi-Miceva and Nilda Bullain (European Center for Not-for-Profit Law). The first version of this paper was prepared and published in 2005 by ECNL, the National Foundation for Civil Society Development in cooperation with the Academy for Institutional Development with the support of the United States Agency for International Cooperation/Croatia. The first version of this paper was also published by the International Center for Not-for-Profit Law (ICNL) in 2005 in "Selected Procedures for Granting Charitable, Public Benefit, and Tax-Exempt Status Around the World" with the support of United States Agency for International Development, Save the Children, and the Institute of Urban Economics, Moscow.



To52 Budapest
Apaczai Csere Janos u. 17, Hungary
Tel: +361 318 6923 Fax: +361 266 1479
www.ecnl.org

International Center for Not-for-Profit Law 1126 16th Street NW, Suite 400 Washington D.C. 20036, USA Tel: +1 202 452 8600 Fax: +1 202 452 8555 www.icnl.org

I. INTRODUCTION

The legal framework for civil society organizations (CSOs)¹ typically permits organizations to be created in different forms to pursue any legitimate aim, including both private benefit and public benefit aims. In most countries, however, the state does not want to extend benefits to all CSOs indiscriminately; instead, the state typically extends benefits to a subset of these organizations, based on their purposes and activities. In return it requires a higher level of governance and accountability for these organizations. By providing benefits, the state seeks to promote certain designated activities, usually related to the common good. CSOs pursuing such activities are given many different labels, including "charities" and "public benefit organizations." Moreover, in some countries, there may be no explicit status defined in the law, but certain purposes and activities are nonetheless linked to state benefits (tax benefits, state grants etc.). In this article, we use the term "public benefit" to refer to this special status – however described in the national context – and the term "public benefit organization" (or PBO) to refer to organizations legally recognized as having this status.

The practice of distinguishing PBOs from those that are established for private interest and facilitating their activities is deeply rooted in European society. Codification of the common law system dates back to 1601 and the English Statute of Charitable Uses, whose purpose was to enumerate charitable causes and to eliminate abuse. Over time, the notion of public benefit was expanded beyond the relief of poverty to include caring for the sick, training of apprentices, building of bridges, maintaining roads and other related purposes. In the civil law tradition, foundations – which were dedicated to a public benefit purpose – existed in Europe in the fifth century BC. Today, most civil law countries extend tax preferences to both foundations and associations, contingent upon public benefit purposes.

This article seeks to present an overview of European practices for regulating organizations with public benefit status.² In analyzing the status, we will focus on the (1) characteristics and rationale, (2) regulatory approaches; (3) criteria; (4) decision-making authority; (5) procedures and conditions for certification/registration; (6) state benefits; and (7) obligations of PBOs, supervision and accountability issues.

¹ The term CSO in this paper will refer to associations, foundations and non-profit companies. The paper will also refer to other entities country specific laws give them the right to obtain PBO status.

² All laws in this cited in this paper can be found in ICNL's online library: www.icnl.org



www.ecnl.org



International Center for Not-for-Profit Law 1126 16th Street NW, Suite 400 Washington D.C. 20036, USA Tel: +1 202 452 8600 Fax: +1 202 452 8555 www.icnl.org

II. CONCEPT AND RATIONALE

In most continental European countries, recognizing a certain organization to be of "public benefit" indicates that the organization has obtained a "**status**" and not that it has been registered as a separate legal form. Public benefit status is granted after the organization has been registered as a legal entity (most commonly in the form of an association or a foundation).³ If the public benefit organization ceases to fulfill the conditions for having this status, it would lose the status and the benefits associated with it, but it could still continue to operate.⁴ Public benefit status is generally considered to be **voluntary**. Having public benefit status might be required to obtain certain benefits, but its existence in the legal framework generally does not inhibit the right of individuals to establish an organization for private purposes and does not prevent an organization to operate without having such status, even if it is established for public benefit purposes.⁵

The approach to public benefit is different in the United Kingdom, in that all organizations with exclusively public benefit purposes are considered 'charities'. In England and Wales, those with charities with income above 5,000 British pounds are required to register with the Charity Commission for England and Wales (with some small exceptions). Those with income below 5,000 British pounds may voluntarily choose to register. In Scotland they are registered with the Office of the Scottish Charity Regulator. Charities based in Northern Ireland do not, and indeed cannot, register; the need to apply to the Inland Revenue to obtain a charitable status for tax purposes.

The underlying rationale for introducing public benefit status is usually **to promote public benefit activities**. Governments recognize that PBOs serve more effectively the needs of local communities and society as a whole. By addressing social needs they complement or supplement

³ Depending on the legal framework, an organization can apply for public benefit status at the same time when it submits the documents for registration as a legal entity, and it will obtain the status once registration is approved. Or it can apply at any time after registration, as long as it fulfills the criteria prescribed by law.

⁴ The laws, however, establish rules about transformation and dissolution of property to ensure that the public money that the public benefit organizations have received do not get channeled to private interests, after the organization loses its status.

⁵ A Draft Order is under discussion in Northern Ireland, which aims to define charities and establish a Charity Commission, and a Charity Tribunal. http://www.dsdni.gov.uk/index/voluntary_and_community/charities_advice.htm

⁶ Charities can be unincorporated or incorporated. Unincorporated charities are not recognized as bodies by the law, and as such cannot own land or investments, employ people or enter contracts in their own name. These tasks are undertaken on their behalf by the trustees, who are also personally liable for all the charity's debts. Unincorporated charities include membership associations and trusts ('trusts' are an arrangement whereby money or property is owned and managed by several physical or legal person, for the benefit of the public). Incorporated charities are recognized as legal bodies, and as such can own land and enter into contracts. Typically, there is also limited liability for trustees ('directors') in the event of dissolution. Incorporated charities include charitable companies and the newly created Charitable Incorporated Organizations (http://www.charitycommission.gov.uk/registration/charcio.asp).



European Center for Not-for-Profit Law 1052 Budapest Apaczai Csere Janos u. 17, Hungary Tel: +361 318 6923 Fax: +361 266 1479 www.ecnl.org International Center for Not-for-Profit Law 1126 16th Street NW, Suite 400 Washington D.C. 20036, USA Tel: +1 202 452 8600 Fax: +1 202 452 8555 www.icnl.org

obligations of the state or provide services that are under-supplied. They often identify and respond to social needs more quickly than governments and are capable of delivering services more efficiently and directly. In addition, in the provision of their services, PBOs may raise private funds, which complement and save state money and mobilize larger community support.⁷

In addition, states across Europe have adopted this status also to:

- Encourage flow of private resources to CSOs through creating incentives for private giving to PBOs e.g. corporate and individual donations (Hungary), percentage mechanism (Poland).
- **Facilitate state-CSO relationship** in provision of social services. In Poland, PBOs are eligible to bid on tenders for social services on equal footing with the government's own agencies. The Hungarian Act on PBOs introduced two tiers of public benefit status: basic and prominent. Organizations can obtain the status of "prominent public benefit organization" if they undertake state or local government responsibilities, usually by having a contract with a state body.
- Strengthen relationship between CSOs and public. With the introduction of the PBO Law in Poland, it was expected that creating a pool of more transparent and more accountable NGOs will help improve the generally poor image of the sector and increase trust in civil society organizations.

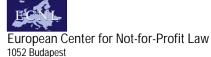
Through introducing public benefit status, governments generally want to ensure that tax benefits granted to NGOs are related to purposes and activities which are of benefit for the public and the society. In theory, therefore, the status is considered as an issue of fiscal regulation. States generally introduce this status as a response to the question: who should be eligible for state benefits and under what requirements; how can we assure that funds from the local private donors are channeled for purposes of public benefit. Consequently they link fiscal (tax) benefits to publicly beneficial activities or organizations with public benefit status. For example, in Croatia, tax benefits are only available for donations to organizations pursuing the types of activities listed in the tax laws, while in Hungary tax benefits for donors are linked to organizations which have obtained a PBO status. Further, the tax laws will either grant exclusive benefits to such activities and organizations, or give them the right to greater benefits than those of organizations that have not received the status. In Poland PBOs are exempt from corporate income tax (as well as real estate tax, civil actions tax, stamp duty, and court fees) on all income devoted to the public benefit objectives listed in the law⁸; while in Hungary PBOs have a right to a higher-threshold exemption on income from economic activities.

In the past few years, some countries have also linked **other types of state support**, which can come in the form of grants, subsidies, payments for providing certain services, percentage designations, to public benefit activities or public benefit status. Thus, if the organization wants to apply and receive state grants or be eligible for other types of benefits, it might need to have

_

⁷ "A Supportive Financing Framework for Social Economy Organizations", by Katerina Hadzi-Miceva, 2007 © ECNL and OECD

⁸ http://www.usig.org/countryinfo/poland.asp#exemption



Apaczai Csere Janos u. 17, Hungary

www.ecnl.org

Tel: +361 318 6923 Fax: +361 266 1479



International Center for Not-for-Profit Law 1126 16th Street NW, Suite 400 Washington D.C. 20036, USA Tel: +1 202 452 8600 Fax: +1 202 452 8555 www.icnl.org

obtained such status (e.g., only PBOs in Poland can receive designations through the 1% law⁹). Even if the state does not require organizations to have public benefit status, they might draft the criteria in a law or tender in a way that the criteria closely correspond to the public benefit criteria. For example, the Hungarian Law on 1% mechanism does not require organizations to have obtained public benefit status; however, the criteria for such status are closely linked to those in the PBO law.

Furthermore, public benefit status contributes towards enhanced **accountability and better governance** of PBOs. In exchange for the benefits granted by the state, PBOs are generally subjected to more stringent supervision to ensure that they are using their assets for the public good. They are also required to adhere to more specific rules of governance and accountability.

III. REGULATORY CONTEXT

Public benefit status can be conferred to CSOs explicitly by including provisions in framework legislation (e.g., basic law that governs associations and foundations), in separate laws concerning public benefit status, or in tax laws. In some countries, various activities and criteria concerning public benefit can be found in different laws.

1. Regulation of a "Public Benefit Status"

Public Benefit Status in Framework Laws

CSO framework legislation specifically defines public benefit status in Bosnia, Bulgaria, and other countries. This approach makes most sense when there is one law that governs both the associations and the foundations and the public benefit status extends to these legal forms. These laws generally address a full range of regulatory issues relating to public benefit status, including the definition of public benefit status, the criteria for obtaining it, and the obligations it imposes. In these situations, it is important that the reform of tax laws which introduce benefits for PBOs is adopted parallel to introducing this status. Otherwise, if such status does not entail any financial benefits the organizations may have no incentive to obtain it. In Bulgaria, for example, two years elapsed between the introduction of the public benefit concept (through a new CSO law) and the provision of some benefits for PBOs (through revisions to the tax law).

Public Benefit Status Laws

An alternative approach is to adopt specific, separate "public benefit" legislation, in an effort to regulate the status comprehensively and consistently. This approach is usually adopted in countries where associations, foundations and other entities, which may obtain this status, are governed by separate laws. Thus having one distinct law on PBO status (vs. regulating it in the separate laws) helps to ensure that it is harmonized and applied consistently in the system.

⁹ The Percentage Mechanism allows every taxpayer to designate a certain percent of the tax owned to organizations that fulfill the criteria prescribed in the law. So far, the following countries have adopted such laws: Hungary (1% to NGOs and 1% to religious organizations from individuals), Slovakia (2% from companies and individuals), Poland (1% from individuals), Lithuania (2% from individuals) and Romania (2% from individuals).



ICNL

1052 Budapest Apaczai Csere Janos u. 17, Hungary Tel: +361 318 6923 Fax: +361 266 1479 www.ecnl.org International Center for Not-for-Profit Law 1126 16th Street NW, Suite 400 Washington D.C. 20036, USA Tel: +1 202 452 8600 Fax: +1 202 452 8555 www.icnl.org

Examples include Hungary, Poland, and Latvia. Hungary adopted public benefit legislation in 1997¹⁰, Poland enacted a Law on Public Benefit Activities and Volunteerism in 2003, and in 2004 Latvia adopted a Law on Public Benefit Organizations. Similarly to situations when PBO status is regulated in framework laws, these specific laws also regulate all issues relating to the status. In addition, separate PBO laws also prescribe more explicitly the benefits that the organizations who have acquired this status will gain.

Section 6, Act on PBO, Hungary

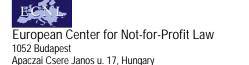
Preferences due to public benefit organizations, supporters of public benefit organizations and recipients of public benefit services

- a) public benefit organization is entitled to:
 - 1. corporate tax exemption with respect to its targeted activity as defined in its founding document.
 - 2. corporate tax preference with respect to its business activity,
 - 3. local tax preference,
 - 4. fee preference,
 - 5. customs preference,
 - 6. other preferences defined by law;
- b) recipients of services provided by a public benefit organization as targeted grants are entitled to personal income tax exemption with respect to the granted service;
- c) supporters of a public benefit organization are entitled to corporate tax or personal income tax preference with respect to support given to fulfill the purposes of the public benefit organization as defined in the founding document (hereinafter: donation);
- d) in case of a durable donation, the supporter described in clause c) is entitled to an extra preference from the second year of the support.
- (2) Within the sphere of its targeted activities, a public benefit organization is entitled to employ persons performing civil service.
- (3) A public benefit organization is not entitled to these preferences, if it has public debts as defined by the Act on the Order of Taxation.

Public Benefit Status in Tax Laws

The activities that are of public benefit and therefore deserve specific benefits can be regulated in tax law, which are functional equivalents of the operational provisions of public benefit legislation.

¹⁰ In Hungary, organizations with the same purposes and activities, but different legal forms (e.g., one being an association, the other a foundation) received different tax treatment. One of the main reasons for introducing the PBO status was to remedy this situation.



www.ecnl.org



International Center for Not-for-Profit Law 1126 16th Street NW, Suite 400 Washington D.C. 20036, USA Tel: +1 202 452 8600 Fax: +1 202 452 8555 www.icnl.org

In many countries, such as Estonia, Germany and the Netherlands, tax legislation lists public benefit activities and defines fiscal privileges for CSOs pursuing those activities. The advantage of this approach is administrative simplicity; since public benefit status is an issue of fiscal regulation, it is natural to regulate public benefit issues through the tax code. The disadvantage is that, in some legal traditions, it is inappropriate to impose operational requirements (such as requirements addressing internal governance and reporting) through the tax law. In addition, legislators can relatively simply (and with a certain freedom for exercising discretion) modify a single provision in a complex tax law, while the same modification to a specific public benefit law would be more conspicuous and subject to the scrutiny of public debate.

2. Regulating Public Benefit Activities in Different Laws

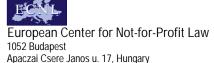
In some countries, the activities that are of public benefit and therefore deserve specific benefits are regulated through provisions in various laws (e.g., tax laws, government grants laws, humanitarian assistance laws, donations law). However, in these cases the regulation does not amount to a designated "public benefit status"; rather, it addresses various activities and various organizations which are eligible for various benefits.

The Lithuanian Law on Charity and Support gives the right to entities enumerated in the law to apply for the so-called "support receivers' status" if they are engaged in socially useful purposes listed in the law. The benefit of this status is that the organizations become eligible to receive support from individuals and legal entities and allocations through the 2% mechanism. Eligible organizations include not-profit entities established by private persons or the state. However, apart from the requirement that the organizations must be engaged in socially useful purposes, there are no other criteria to receive this status. As a result, in practice, virtually any organization with legal form prescribed in the law receives this status.

Regulating public benefit activities, which are entitled to state benefits, through various laws can bring to an inconsistent application of the concept. For example, in Croatia different laws refer to activities which are of public benefit (e.g., Law on Humanitarian Assistance, Profit Tax Law, and Personal Income Tax Law). The lists refer only to limited categories of public benefit activities (e.g., education, humanitarian) and fail to include other, equally important activities (e.g., human rights, children rights). Even more, the benefits provided in the tax laws do not embrace all activities which are recognized as of public benefit in the other non-tax laws. In addition, different laws also introduce a publicly beneficial status for certain types of organizations (e.g. humanitarian organizations, fire brigades) which lists specific criteria, and benefits that they are entitled to. As a result, the Croatians have concluded that they need to reform the system in order to introduce a coherent policy concerning public benefit status.11

_

¹¹ Ivanovic Mladen, Legal Framework for the Activity of Public Benefit Organisations in the Republic of Croatia - State of affairs on 31 May 2005, published by ECNL and National Foundation for Civil Society Development (2005)



www.ecnl.org



International Center for Not-for-Profit Law 1126 16th Street NW, Suite 400 Washington D.C. 20036, USA Tel: +1 202 452 8600 Fax: +1 202 452 8555 www.icnl.org

IV. CRITERIA FOR RECEIVING PUBLIC BENEFIT STATUS

The criteria for receiving public benefit status differ among countries and are drafted to reflect the goals of the legislation, the needs of the society and the local circumstances and traditions. Generally the following criteria are considered when granting public benefit status: Qualifying activities for public benefit status, eligible organizations, extent to which PBOs must be organized and operated for public benefit, target beneficiaries, and financial and governance requirements.

1. Qualifying Activities/Purposes

Type of purposes considered as publicly beneficial

Generally laws regulating public benefit activities enumerate certain specific purposes which are deemed to serve the common good. A public benefit activity is therefore defined as any lawful activity that supports or promotes one or more of the purposes enumerated in the law. The list below contains virtually all of the public benefit activities recognized in one or more countries in Europe:

- (a) Amateur athletics;
- (b) Arts;
- (c) Assistance to, or protection of, physically or mentally handicapped people;
- (d) Assistance to refugees;
- (e) Charity;
- (f) Civil or human rights;
- (g) Consumer protection;
- (h) Culture;
- (i) Democracy;
- (i) Ecology or the protection of environment;
- (k) Education, training and enlightenment;
- (l) Elimination of discrimination based on race, ethnicity, religion, or any other legally proscribed form of discrimination;
- (m) Elimination of poverty;
- (n) Health or physical well-being;
- (o) Historical preservation;
- (p) Humanitarian or disaster relief;
- (q) Medical care;
- (r) Protection of children, youth, and disadvantaged individuals;
- (s) Protection or care of injured or vulnerable animals;
- (t) Relieving burdens of government;
- (u) Religion;
- (v) Science;
- (w) Social cohesion:
- (x) Social or economic development;
- (y) Social welfare...



European Center for Not-for-Profit Law 1052 Budapest Apaczai Csere Janos u. 17, Hungary Tel: +361 318 6923 Fax: +361 266 1479 www.ecnl.org International Center for Not-for-Profit Law 1126 16th Street NW, Suite 400 Washington D.C. 20036, USA Tel: +1 202 452 8600 Fax: +1 202 452 8555 www.icnl.org

It is important that countries choose public benefit purposes that reflect their needs, values, and traditions. In the Netherlands, for example, the public benefit purposes developed in fiscal jurisprudence include purposes that are ecclesiastical, based on a philosophy of life, charitable, cultural, scientific, and of public utility. German tax law includes public health care, general welfare, environmental protection, education, culture, amateur sports, science, support of persons unable to care for themselves, and churches and religion. In France, the tax law defines public benefit to include, among others, assistance to needy people, scientific or medical research, amateur sports, the arts and artistic heritage, the defense of the natural environment and the defense of French culture. In Hungary, separate public benefit legislation lists 22 different purposes, including health preservation, scientific research, education and culture. Similarly, Polish law lists 24 public benefit activities.

Section 2, Public Benefit Law, Latvia

"A public benefit activity is an activity, which provides a significant benefit to society or a part thereof, especially if it is directed towards charitable activities, protection of civil rights and human rights, development of civil society, education, science, culture and promotion of health and disease prophylaxis, support for sports, environmental protection, provision of assistance in cases of catastrophes and extraordinary situations, and raising the social welfare of society, especially for low-income and socially disadvantaged person groups."

• Are there limitations to activities that can be pursued?

Many countries exclude certain activities or goals from qualifying as public benefit. Restrictions commonly include political and legislative activities, such as direct lobbying and campaigning for political parties. For example, Hungary prohibits involvement in direct political activities and the provision of financial aid to political parties. Some countries exclude purposes related to sports and religion; others do not.

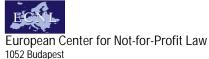
Section 2, Public Benefit Law, Latvia

"The following deemed not to be public benefit activities:

- 1) activities, which are directed to the support of political organisations (parties) or the election campaign thereof; and
- 2) activities of such a scope as it is directed only to the members or founders of the association and foundation and persons associated with them for the satisfaction of private interests and needs, except activities which promote an association or foundation, which is founded and is engaged in order to protect of the rights and interests of socially disadvantaged person groups and low-income persons and families."

• Is the list of activities exclusive?

Almost all countries include a "catch-all" category, which simply embraces "other activities" which are deemed to serve the common good. This is an effective way to ensure that enumerated purposes are not interpreted in an overly restrictive manner, and that the concept of public benefit remains flexible, keeping pace with changing social circumstances. Public benefit definitions lacking such a "catch-all" category may impede the inclusion of emerging activities that serve the



Apaczai Csere Janos u. 17, Hungary

www.ecnl.org

activities.

Tel: +361 318 6923 Fax: +361 266 1479



International Center for Not-for-Profit Law 1126 16th Street NW, Suite 400 Washington D.C. 20036, USA Tel: +1 202 452 8600 Fax: +1 202 452 8555 www.icnl.org

public benefit. The law may simply include a provision similar to the following: "Any other activity that is determined to support or promote public benefit." Such "catch-all" categories are not uncommon, even where the law enumerates a list of specific purposes, as in Latvia and Bulgaria. The Polish law does not contain a catch all category; however it provides that the Council of Ministers may add new tasks. The Hungarian law provides a closed list of activities.

However, so far the Parliament has amended the law several times to include other types of

Charities Act, the U.K.

As a common-law country, the United Kingdom relied on case precedent to define "charitable" purposes. Over time, courts in the United Kingdom have classified charitable purposes under four broad categories relief of poverty, advancement of education, advancement of religion, and other purposes beneficial to the community. They have accepted the principle that the definition of "charitable purpose" changes to reflect developing social conditions. Recognizing the need for modernization the British government reformed the legislation in 2006. Part I (2) of the new Charities Act sets a framework listing the main charitable purposes as follows:

- (a) prevention or relief of poverty;
- (b) advancement of education;
- (c) advancement of religion;
- (d) advancement of health or the saving of lives;
- (e) advancement of citizenship or community development;
- (f) advancement of arts, culture, heritage or science;
- (g) advancement of amateur sport;
- (h) advancement of human rights, conflict resolution or reconciliation or the promotion of religious or racial harmony or equality or diversity;
- (i) advancement of environmental protection or improvement;
- (j) the relief of those in need by reason of youth, age, ill health, disability, financial hardship or other disadvantage;
- (k) advancement of animal welfare;
- (l) the promotion of the efficiency of the armed forces of the Crown, or of the efficiency of the police, fire and rescue services, or ambulance services, and
- (m) other charitable purposes.¹²

¹² Subsection (4)of paragraph 2 further defines that:

[&]quot;The purposes within this subsection (see subsection (2)(m)) are—

⁽a) any purposes not within paragraphs (a) to (l) of subsection (2) but recognized as charitable purposes under existing charity law or by virtue of section 1 of the Recreational Charities Act 1958 (c. 17); Charities Act 2006 (c. 50)

⁽b) any purposes that may reasonably be regarded as analogous to, or within the spirit of, any purposes falling within any of those paragraphs or paragraph (a) above; and



www.ecnl.org



International Center for Not-for-Profit Law 1126 16th Street NW, Suite 400 Washington D.C. 20036, USA Tel: +1 202 452 8600 Fax: +1 202 452 8555 www.icnl.org

2. Eligible entities

The second criterion in determining public benefit status is the type of legal entities that can obtain it. As mentioned above, the public benefit status is usually granted either during the time of or after registration of the organizations. Hence, the organizations must have been registered (or recognized) as legal persons before they apply for public benefit status.¹³

Public benefit status is generally available for associations and foundations which are basic forms in most European, countries. In addition, depending on the country, this status can be given to a range of other organizational forms.¹⁴ In Hungary, public benefit status is available to associations, foundations and non-profit companies. In Latvia, religious organizations and religious institutions can obtain this status as well. However, during the application for this status, they are required to submit a letter of recommendation issued by the Ministry of Justice Board of Religious Affairs. In Poland¹⁵, an association of unit of local governments can also obtain this status.¹⁶

Article 3, paragraph 4, of the <u>Polish law</u> provides the list of organizations that cannot apply for PBO status:

- 1) Political parties;
- 2) Trade unions and organizations of employers;
- 3) Professional self-governments;
- 4) Foundations founded solely by the State Treasury and/or a unit of self-government, unless:
 - a) separate regulations state otherwise,

(c) any purposes that may reasonably be regarded as analogous to, or within the spirit of, any purposes which have been recognized under charity law as falling within paragraph (b) above or this paragraph."

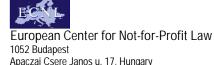
¹³ This is of importance, since in most of the European countries registration is voluntary and thus many organizations operate without being registered. However, in continental Europe, if the organization wants to obtain a public benefit status then it would need to first acquire a status of a legal person.

¹⁴ Usually countries distinguish between two types of non-profit organizations: those of general purpose such as associations, foundations, non-profit companies; and those established for specific purpose which are regulated with separate legislation (trade unions, political parties etc) and are generally outside of the public benefit system.

¹⁵ The Polish Law is an interesting example as it provides a definition of non-governmental organization:

[&]quot;Non-governmental organizations are legal entities or entities with no legal personality created on the basis of provisions of laws, including foundations and associations, taking into consideration par. 4. Non-governmental organizations are not bodies of the sector of public finances in the understanding of regulations governing public finances, and operate on a not-for-profit basis." (article 3, par.1).

¹⁶ Under specific conditions enumerated in the law, PBO status can also be obtained by legal entities and organizational units operating on the basis of regulations governing the relation between the State and Catholic Church in the Republic of Poland, the relation between the State and other churches as well as religious unions, and the guarantees of the freedom of faith and conscience, provided their statutory goals include the performing of public benefit activities.



www.ecnl.org



International Center for Not-for-Profit Law 1126 16th Street NW, Suite 400 Washington D.C. 20036, USA Tel: +1 202 452 8600 Fax: +1 202 452 8555 www.icnl.org

b) the property of the foundation does not belong entirely to the State or its municipal bodies, or is not financed with public resources under the framework of the Law on Public Finances, or

- c) the foundation performs its statutory activities in the field of science or humanities, particularly for the sake of science or humanities;
- 5) Foundations established by political parties;
- 6) Companies operating pursuant to the regulations governing sport activities."

3. Principle purpose test

Other criteria often used to decide whether one organization should obtain a public benefit status are the extent to which the organization must be organized and operated for public benefit and its beneficiaries (target group).

Many countries require that the organization **be organized and operated principally to engage in public benefit activities**, however defined. An organization is "organized" principally for public benefit when the purposes and activities contained in its governing documents limit it to engaging principally in public benefit activities. An organization is "operated" principally for public benefit when its actual activities are principally public benefit. "Principally" may mean more than 50% or virtually all, depending on the country. There are different ways of measuring whether the "principally" test has been satisfied – for example, by measuring the portion of expenditures or the circle of beneficiaries.

In the Netherlands, the decisive factor is the **circle of potential beneficiaries**. If the activities are aimed at serving too restricted a group of persons – persons belonging to a family, for example – then the organization is not eligible for public benefit status. If the organization serves both its members and engages in public benefit activities, it may qualify for public benefit status if its public benefit activities make up at least 50% of its overall activities. Similarly, in France, in order to qualify as a PBO, an organization must engage primarily in at least one public benefit activity and provide services to a large, undefined group of individuals in France.¹⁷

England

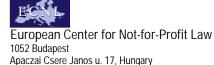
There are five main principles which show whether an organisation provides benefit to the public. These are:

The Benefit: i. There must be an identifiable benefit, but this can take many different forms.

ii. Benefit is assessed in the light of modern conditions.

_

¹⁷ There are two forms of public benefit status in France: (1) general interest status and (2) public utility status. Qualifying for general interest status, as stated in the text, is satisfied when an organization engages primarily in a public benefit activity and provides services to an appropriate group of beneficiaries. Qualifying for public utility status additionally requires adopting statutes in compliance with model statutes provided by the Conseil d'Etat (containing requirements regarding internal structure, use of funds, and distribution of assets upon dissolution) and satisfying other requirements relating to financial viability and size of the organization.





International Center for Not-for-Profit Law 1126 16th Street NW, Suite 400 Washington D.C. 20036, USA Tel: +1 202 452 8600 Fax: +1 202 452 8555 www.icnl.org

The Public:

www.ecnl.org

- iii. The benefit must be to the public at large, or to a sufficient section of the public.
- iv. Any private benefit must be incidental.
- v. Those who are less well off must not be entirely excluded from benefit. 18

In general, a purpose is *not charitable* if it is mainly for the benefit of a named person or specific individuals. It will also not be charitable if the people who will benefit from it are defined by a personal or contractual relationship with each other. For example, if the beneficiaries are related or connected to the person who is setting up the charity, or where they are defined by common employment or by membership of a non-charitable body, for example, members of a professional institute.¹⁹

Similarly, Germany requires that an organization receiving tax benefits carry out its public benefit activities *exclusively*, *directly and unselfishly* (with disinterest). Notably, Poland also requires that a public benefit organization engage *exclusively* in public benefit activities.

4. Governance requirements

Some countries also prescribe a special governing structure for organizations that wish to obtain public benefit status. For example, the mandatory requirement for a two-tiered governing structure aims to ensure that the organizations will have additional internal supervision over their activities and that they are indeed undertaking activities and spending the public funds according to their status and other conditions stipulated in the public benefit legislation.

Bulgarian law follows this approach by requiring that public benefit organizations must have a "collective supreme body and managing body". This requirement is important mainly for the foundations, as generally they can have only one body, and it can be a one-person body. However, if they wish to obtain public benefit status they must have two bodies, one of them collective.

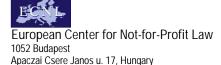
Article 10 (1) Act on PBO, Hungary:

"If the annual income of a public benefit organization exceeds five million HUF, the establishment of a supervisory body separate from the governing body is mandatory, even if such obligation is not prescribed by other laws."

The Polish law also obliges the organization to have a statutory collegiate institution that will ensure monitoring and supervision, which is separate from the management board and not supervised by the management board. Its members "cannot be members of the management

¹⁸ For more, and updated information please visit: http://www.charitycommission.gov.uk/spr/pblp.asp

¹⁹ http://www.charitycommission.gov.uk/publications/cc21.asp#7. Further, according to the Hungarian law any related beneficiaries must receive the same services and aid as any and all beneficiaries; i.e., it does not prohibit related beneficiaries to receive benefits, but it requires equal treatment with non-related ones.



www.ecnl.org



International Center for Not-for-Profit Law 1126 16th Street NW, Suite 400 Washington D.C. 20036, USA Tel: +1 202 452 8600 Fax: +1 202 452 8555 www.icnl.org

board, nor be their relatives, in-laws or be in work-based dependence; cannot have been pronounced, with a lawful verdict, guilty of a deliberate crime; and may receive, due to their duties in such institution, reimbursement of relevant expenditures or remuneration not exceeding the limit set in art. 8 point 8 of the Law on Remuneration of Persons in Charge of Certain Legal Units, dated March 3, 2000."²⁰

5. Other criteria/conditions

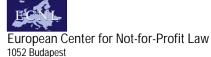
In addition to the key criteria mentioned above, some laws prescribe additional criteria which must be met if the organization wishes to receive public benefit status or to be included in the list of organizations eligible for tax and other benefits. Those additional criteria include: restrictions on conducting economic activities, restriction on engagement in political activities, financial management, asset management and distribution, remuneration of board and employees etc.

Chapter II, PBO Act Hungary

- § 4. To be registered as a *public benefit organization*, the founding document of the organization shall include:
- a) a description of the sort of public benefit activity defined in this Act the organization pursues, and a statement that the organization, if a membership organization, does not exclude non-members from public benefit services;
- b) a statement that the organization pursues business activity only in the interest of realizing its public benefit objectives, without jeopardizing them;
- c) a statement that the organization does not distribute profits, but spends them on the activity defined in its founding document;
- d) a statement that the organization does not pursue direct political activity, is independent of political parties and does not provide financial support to them.
- (2) In addition to the requirements set forth in paragraph (1), the founding document of a public benefit organization shall comply with further requirements prescribed in this Act (§ 7).²¹
- § 5. To be registered as a *prominently public benefit organization*, the founding document of the organization shall include, in addition to the requirements set out in § 4, a statement that the organization:

²¹ Regarding governance and management of the organization (see below)

²⁰ Article 20 of the Law on PBA and Volunteering, Poland



Apaczai Csere Janos u. 17, Hungary

www.ecnl.org



International Center for Not-for-Profit Law 1126 16th Street NW, Suite 400 Washington D.C. 20036, USA Tel: +1 202 452 8600 Fax: +1 202 452 8555 www.icnl.org

a) in the course of its public benefit activity fulfills a public duty which must be provided by state organs or local governments pursuant to an act or other law in accordance with the act's authorization, and

b) shall disclose through the local or national press the most important data regarding its activities as defined in the founding document and its management.

Section 11, Income Tax Act of Estonia

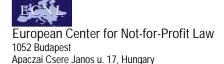
A non-profit association or foundation (hereinafter association) which meets the following requirements shall be entered in the list:

- 1) the association operates in the public interest;
- 2) it is a charitable association, that is, an association offering goods or services primarily free of charge or in another non-profit seeking manner to a target group which, arising from its articles of association, the association supports, or makes support payments to the persons belonging in the target group;
- 3) the association does not distribute its assets or income, grant material assistance or monetarily appraisable benefits to its founders, members, members of the management or controlling body (§ 9), persons who have made a donation to it or to the members of the management or controlling body of such person or to the persons associated with such persons within the meaning of clause 8 (1);
- 4) upon dissolution of the association, the assets remaining after satisfaction of the claims of the creditors shall be transferred to an association or legal person in public law entered in the list:
- 5) the administrative expenses of the association correspond to the character of its activity and the objectives set out in its articles of association;
- 6) the remuneration paid to the employees and members of the management or control body of the association does not exceed the amount of remuneration normally paid for similar work in the business sector.²²

It is important to note, however, that any such additional criteria should consider the local circumstances and the goals that the legislator aims to achieve through those requirements. Burdensome requirements can discourage organizations from applying for this status. For example, in Hungary it is rather easy for an average NGO to comply with the requirements for a regular public benefit status so around half of the CSOs are regular PBOs. In Poland, due to the difficult criteria and obligations, only around 10% of all CSOs have registered as PBOs. In regulating PBOs legislators should therefore consider whether they aim to increase the level of transparency and accountability and access to the benefits for the majority of the sector or if they

 $\underline{http://www.legaltext.ee/et/andmebaas/tekst.asp?loc=text\&dok=X40007K11\&keel=en\&pg=1\&ptyyp=RT\&tyyp=X\&query=tulumaksu$

²² Estonia Income Tax Act,



www.ecnl.org



International Center for Not-for-Profit Law 1126 16th Street NW, Suite 400 Washington D.C. 20036, USA Tel: +1 202 452 8600 Fax: +1 202 452 8555 www.icnl.org

<u>aim to create an "elite" group of organizations</u>, which, for example can partner with the government in delivery of social services (as it happens in Poland or in Hungary through the introduction of the second tier status of "prominent" PBOs).

V. DECISION-MAKING BODY

Who decides which organizations qualify for public benefit status? The question has critical implications for the regulation of public benefit organizations and the entire nonprofit sector. The decision-maker has the authority to grant public benefit status; often has the authority to revoke public benefit status; and in some countries is also responsible for supervising and supporting the work of public benefit organizations. By granting public benefit status, the decision-maker lays the foundation for distinct regulatory treatment – treatment that entails both state benefits (usually tax exemptions) and more stringent accountability requirements.

There is no single right answer to the question of who should make the public benefit determination. Instead, countries have adopted a variety of different approaches. In some countries, this authority is vested in the tax authorities (e.g., Germany). In other countries, the courts (e.g., Hungary) or a governmental entity, such as the Ministry of Justice, confers public benefit status (e.g., Bulgaria). Others have empowered independent commissions to decide the question (e.g., England, Moldova). In some countries a state body grants the status, based on a recommendation of an independent commission (e.g., Poland, Latvia). In Estonia, the status is approved by the Government of the Republic after obtaining a recommendation from a Committee of Experts. Each approach has distinct advantages and disadvantages.

Tax Authorities

In many countries, the public benefit determination is made by the tax authorities who decide which organizations are entitled to fiscal privileges based on their publicly beneficial purposes and activities. Countries adopting this approach for at least some categories of public benefit activity include Denmark, Finland, Germany, Greece, Ireland, the Netherlands, Portugal and Sweden. In Denmark, for example, the tax authorities grant public benefit status through an annually published list of qualified organizations. In Finland, the status is granted for a period of five years by the National Tax Board. In Germany, the local tax authorities are responsible for granting public benefit status and verifying that requirements for retaining this status are met every three years. In the Netherlands, official recognition as a public benefit organization is not required, but a CSO may request it. Such recognition helps organizations avoid potential disputes, which is particularly important when large donations are involved. Fiscal authorities in the Netherlands have adopted certain criteria for such requests, which seek to ensure that the CSO has appropriate standards of transparency and accountability.

Vesting the tax authorities with authority over the public benefit determination has the advantage of administrative convenience, in that one entity makes all such decisions. The degree of expertise which they can be expected to bring to the question of public benefit status may depend on whether or not there is a specialized department within the tax department to focus on this question. In addition, the tax authorities in some countries demand this authority, because the



European Center for Not-for-Profit Law 1052 Budapest Apaczai Csere Janos u. 17, Hungary

Tel: +361 318 6923 Fax: +361 266 1479 www.ecnl.org



International Center for Not-for-Profit Law 1126 16th Street NW, Suite 400 Washington D.C. 20036, USA Tel: +1 202 452 8600 Fax: +1 202 452 8555 www.icnl.org

determination affects the tax base. A potential disadvantage, however, arises out of the potential conflict of interest between the duty to maximize the tax base and the responsibility for granting a status that reduces the tax base.

Single Ministry

In Bulgaria, the Ministry of Justice – specifically, a Central Registry within the Ministry of Justice – is responsible for public benefit regulation (certification and supervision). Court-registered CSOs pursuing public benefit activities must submit applications and documentation to the Ministry. Should registration be denied, the applicant may file an appeal within 14 days in the Supreme Administrative Court.

The primary advantage of placing authority within a single ministry is the greater likelihood of consistent decision-making. The creation of a specialized department within the Ministry (as we see in Bulgaria) may also foster the development of specialized expertise relating to public benefit issues. At the same time, a single ministry with many duties may fail to allocate sufficient resources to public benefit issues, in which case expertise is less likely to develop. Perhaps the greatest danger in assigning authority to a single ministry is the danger of arbitrary, politically motivated decision-making. In certain countries, where ministries have decision-making authority on registration questions, there has often been a distinct chilling effect on CSOs pursuing registration.²³

Courts

Indeed, it is in order to avoid politicized decision-making that some countries have opted to vest **courts** with the power to certify or recognize public benefit organizations. Such is the case in Greece and Hungary. In France, the Conseil d'Etat – its highest administrative court – has authority to decide whether associations and foundations qualify for "public utility" status. Court-based registration can offer the additional advantage of accessibility, in cases where courts throughout the country hold the authority. Furthermore, courts can actually speed up the process of public benefit recognition, in countries where CSOs can apply simultaneously for both registration as a legal entity and recognition as a public benefit entity. Such is the case in both Greece and Hungary. On the other hand, because courts are usually overburdened, the registration process can be slow-moving. Also, courts must deal with a wide range of issues,

²³ Very few countries have placed decision-making authority within several line ministries. Romania is one exception. While this approach might seem useful in ensuring ministries with appropriate expertise are evaluating public benefit activities (e.g., the Ministry of Health would review the public benefit application of an CSO pursuing health-related activities), there are far more disadvantages. The danger of political decision-making remains; consider an environmental CSO seeking to engage in environmental advocacy and litigation having to apply to the Ministry of the Environment for certification / registration. The problem of inconsistent decision-making between ministries is acute. Moreover, there will inevitably be jurisdictional gaps, where the CSO-applicant will not know which ministry is competent to handle its application. Furthermore, in Romania, the law has left the formulation of qualifying criteria to each line ministry, creating uncertainty for those ministries that have issued no such criteria, and inviting inconsistency, as criteria may vary from ministry to ministry. This is why they now aim to reform this system.



www.ecnl.org



International Center for Not-for-Profit Law 1126 16th Street NW, Suite 400 Washington D.C. 20036, USA Tel: +1 202 452 8600 Fax: +1 202 452 8555 www.icnl.org

making it difficult for them to develop specialized expertise in public benefit issues. Decentralized decision-making, finally, is unlikely to produce wholly consistent decisions.

■ Independent Commissions²⁴

Perhaps the most innovative approach is the creation of independent commissions to decide on this status. For example, the Charity Commission for England and Wales is an independent regulator for charity activities. It is part of the government, yet it is independent of the political process. Its powers are conferred by an Act of Parliament and exercised under the oversight of Commissioners, each of whom is independent of the political process and voluntary sector. The Minister for the Third Sector appoints the Chair and Members of the Commission. The Commission is required to report on its performance to Parliament annually. The key benefits to the commission approach are its independence from political interference and the quality and consistency of decision-making made possible through the concentration of expertise in the Commission. The key disadvantages are the cost of creating and maintaining such a commission and the fact that it is a centralized organ.

Following the example of the Charity Commission, the Moldovan Law on Associations created a similar body, known as the Certification Commission. The Certification Commission consists of nine persons, three of whom are appointed by the President, three by Parliament, and three by the Government. At least one of each of the three sets of appointees must represent a public benefit organization (and not be a civil servant), a government official, or a Member of Parliament. The hope was that including civil society representatives on the Commission will protect against repressive or discriminatory decisions and increase public confidence. Developing the proper mechanism for selecting the civil society representatives, however, remains a critical challenge (see below).²⁵

• State bodies in cooperation with independent commissions

Estonia, Poland and Latvia are examples of countries where the decision on the public benefit status is granted by the Government, court or a Ministry. However, in addition to these ministries the laws set up the public benefit commissions with consultative, advisory status.

In Latvia, the Ministry of Finance grants the status, on the basis of an opinion of the Public Benefit Commission. The Commission is a collegial institution, with equal numbers of members

²⁴ For more detailed information on the work of the independent commissions granting public benefit status please review the publication "Public Benefit Commissions: A Comparative Overview - Armenia, England / Wales, Moldova", published by ICNL, 2005 (http://icnl.org/knowledge/pubs/PBCommissions.pdf)

²⁵ The new Latvian Law on Public Benefit Organizations contemplates the creation of a Public Benefit Commission. In the Latvian context however, the Commission simply acts as an advisory body for the Ministry of Finance, the decision-making body. The Latvian Public Benefit Commission consists of authorized governmental officials and representatives from associations and foundations, in equal numbers. The procedures for selecting representatives of associations and foundations to the Commission are not defined in the law, but instead shall be determined by the Cabinet.



European Center for Not-for-Profit Law 1052 Budapest Apaczai Csere Janos u. 17, Hungary

Tel: +361 318 6923 Fax: +361 266 1479 www.ecnl.org

International Center for Not-for-Profit Law 1126 16th Street NW, Suite 400 Washington D.C. 20036, USA

Tel: +1 202 452 8600 Fax: +1 202 452 8555

www.icnl.org

from the government officials and representatives of associations and foundations. The Commission provides the Ministry of Finance with an opinion on whether the associations. foundations or religious organisations comply with the activities for public benefit status and the requirements for use of property and financial means as prescribed by the Law. The Cabinet approves the by-laws of the Commission, the composition of the Commission and the procedures by which representatives of associations and foundations are nominated and selected.

In Poland, PBOs are registered in the Central Court Registry. The law also establishes a Council for Public Benefit Activities, which does not have a role in registration but which serves as an opinion, advising and supporting body for the Ministry of Social Security (which supervises the activities of the organizations). The Council is composed of 10 representatives of the public administration and local government, and 10 CSO representatives. The members of the Council are appointed and discharged by the Minister responsible for the issues of social security; however, the appointing of the members of the Council representing CSOs is limited to the candidates pre-selected by the CSOs. The Council has the following duties:

- advising on the issues relevant for the application of the Law;
- advising on the government's legal acts concerning public benefit activities and volunteering;
- providing assistance and expressing opinion concerning conflicts between public administration institutions and public benefit organizations;
- collecting and analyzing information about the performed inspections and their outcomes;
- participating in the process of inspection;
- advising in the field of public tasks, commissioning non-governmental organizations and entities mentioned in art. 3 par. 3 to perform such tasks, and recommending standards of performing public tasks;
- creating, in co-operation with CSOs, the mechanisms of informing them about the standards of performing public benefit activities and about the identified cases of violation of those standards.²⁶

Estonia, Income Tax Act, Section 11 (9)

"An application for entry of in the list shall be submitted to a regional structural unit of the Tax and Customs Board by 1 February or 1 August. After obtaining the recommendations of the Expert Committee, the regional structural unit of the Tax and Customs Board shall inform the association by 15 March or 15 September correspondingly of an initial decision to deny entry in the list or to delete the association from the list. Based on the proposal of the Minister if Finance, the Government of the Republic shall enter an association in the list or delete an association from the list as of 1 July or 1 January by an order."²⁷

²⁷ Estonia Income Tax Act.

http://www.legaltext.ee/et/andmebaas/tekst.asp?loc=text&dok=X40007K11&keel=en&pg=1&ptyyp=RT&t yyp=X&query=tulumaksu

²⁶ Article 35 of the law.





International Center for Not-for-Profit Law 1126 16th Street NW, Suite 400 Washington D.C. 20036, USA Tel: +1 202 452 8600 Fax: +1 202 452 8555 www.icnl.org

The Estonian Expert Committee was established in 2007, and it consists of 9 representatives of NGOs, mostly from umbrella organizations from different fields of activities. They are appointed by the Ministry of Finance after consultations with the CSOs.

o <u>Challenges of the model</u>

Apaczai Csere Janos u. 17, Hungary

www.ecnl.org

Tel: +361 318 6923 Fax: +361 266 1479

When considering the model of an independent commission as a sole regulator or in partnership with a state body, one should consider several issues before deciding on the approach.

Primarily, there is a notable difference in the approach to relations between government and the CSO sector in England and Wales and in Central and Eastern Europe (CEE). 'Charity' in England and Wales has a long history, and it is a deeply-rooted and well-supported part of society. Its role has developed to the stage where the cooperation between government and CSOs is generally constructive. The relationship is based on mutually acknowledged strengths, a degree of trust and an officially endorsed partnership approach²⁸. This environment enables the Charity Commission to operate at the same time as a regulatory/controlling body and as an enabler/supporting body of the sector: "Our aim is to provide the best possible regulation of charities in England and Wales, in order to increase charities' efficiency and effectiveness and public confidence and trust."²⁹

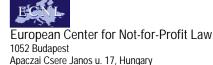
In most of the CEE countries (and especially countries of South East Europe) governments and CSOs are still struggling to define their relationships. CSOs do not have a "reserved seat on the table" when public policy issues are discussed or legislation is adopted. There is lack of trust about their role and CSO image in the society is low. Their own capacity to be a strong partner is also a challenge. On the other hand, the public administration has not yet clearly defined the role it can play beyond regulating CSOs. There is often a lack of vision and trust about how the government could support the development of the sector and thus strengthen their contribution to society.

Second, in considering the composition of the commission, countries of CEE often raise the issue of participation of the civil society experts. Such participation is beneficial as it could increase the capacity of the commission in considering the current needs and trends in the society when implementing the public benefit status. Indeed, almost all Commissioners in Charity Commission of England and Wales have been active in the voluntary sector. However, unlike in England and Wales, the participation of such experts remains a challenge in the countries of CEE mainly because of the difficulties in selecting such experts and regulating potential conflict of interests that might appear.

In England and Wales, the democratic culture, as well as well-developed and enforced regulations and low tolerance of corruption in public life have created an environment in which potential

²⁸ This approach was formally endorsed in 1998 with the launch of the "Compact on Relations between Government and the Voluntary and Community Sector in England". The Compact includes Codes of Good Practice - on black and minority ethnic groups, community groups, consultation and policy appraisal, funding and procurement and volunteering. http://www.thecompact.org.uk/

²⁹ http://www.charitycommission.gov.uk/spr/regstance.asp



www.ecnl.org



International Center for Not-for-Profit Law 1126 16th Street NW, Suite 400 Washington D.C. 20036, USA Tel: +1 202 452 8600 Fax: +1 202 452 8555 www.icnl.org

conflicts of interest are well managed. This would still be in contrast to much of the practice that can be found in countries of CEE, where avoiding conflict of interest is seen as a necessary burden rather than the natural way of doing business.

Thus although the model of a Charity Commission in England and Wales might sound attractive to countries of CEE, much of its success is due to the specific historical and cultural context of public benefit organizations in that country. CEE countries should consider the factors mentioned above (level of development of the public administration, and of the sector, the culture of partnership, relationship between governments and CSOs, position of the sector in the society, image of sector etc.) before deciding whether to follow it as a best regulatory approach for the particular local context.

"Principles

In common with other public bodies, the Commission has arrangements under which potential conflicts of interest can be recognized and managed.

Commissioners on appointment are normally asked to stand down from Chairmanship or other office in charities. It is normal, however, for them to retain existing trusteeships, and for those whose livelihood involves professional involvement with charities to continue with it, provided that it is transparent and is not inconsistent with the Commission's regulatory role.

Where a Commissioner's or other Board member's circumstances involve, or might appear to involve, clear potential for a material conflict of interest in his or her official role, he or she will declare them in this register, and, where appropriate, withdraw from related Commission business and discussions."³⁰

Finally, the model of independent commissions will have increased chances for success if its **independence from government interference is preserved and if the governments are seriously committed to ensure its proper functioning and integrating them in the system.** Indeed, of the big challenges that independent commissions in CEE are facing is the lack of cooperation with the other bodies or the lack of sufficient respect for their opinions and input. For example, in Estonia the challenge is that the Tax and Custom Board and Ministry of Finance are not receptive to the suggestions of this committee as these recommendations are not binding for them.³¹ The other challenge is the lack of serous commitment by the commissioners to attend the sessions (especially if their work is conducted without remuneration). Tailoring clear rules and allocating enough resources could ensure the smooth and full operation of the commission³², still this cannot guarantee a smooth and successful operation.

³⁰Charity Commission: Registering and Declaring Interests http://www.charitycommission.gov.uk/tcc/decint.asp

³¹ "Legal and Institutional Mechanisms for NGO-Government Cooperation in Croatia, Estonia and Hungary", by Katerina Hadzi-Miceva, © ECNL and Institute for Public Affairs (IPA), Poland. The paper was presented by Ms. Hadzi-Miceva at the conference on October 25-26 in Warsaw, under the project titled: KOMPAS II, financed by the European Union.

³² Article 39 of the Polish law provides that:





International Center for Not-for-Profit Law 1126 16th Street NW, Suite 400 Washington D.C. 20036, USA Tel: +1 202 452 8600 Fax: +1 202 452 8555 www.icnl.org

Moldova

www.ecnl.org

"...the truly independent performance of the Certification Commission has been frustrated by several problems. Government agencies have demonstrated an indifference and lack of understanding toward the role of the Commission. The President, Parliament and Government, as nominating bodies, have selected Commission representatives without sufficient thought and vision. To date, the Commission still has prepared no detailed procedural regulations, nor does it maintain a website. Even the register of public benefit organizations is not yet practically accessible to the public. Perhaps most importantly, however, lawmakers have not amended the legal framework to provide for sufficient privileges and incentives for public benefit organizations. Public benefit status is, fundamentally, an issue of fiscal regulation. Without corresponding state benefits, public benefit status is largely an empty concept." ³³

Government decree.

In stark contrast to the commission approach, a few countries grant public benefit status by governmental decree. In Belgium, for example, organizations engaged in cultural activities are granted public benefit status by royal decree. In Luxembourg, public benefit status is granted by Grand-Ducal decree after application to the Ministry of Justice. These practices reflect particular historical, cultural and legal contexts, and need not represent models for emulation.

VI. CERTIFICATION / REGISTRATION PROCEDURES

Whichever organ the state designates to rule on applications for public benefit status, the certification or registration process should be clear, quick and straightforward and specific rules about when public benefit status is denied should be prescribed.

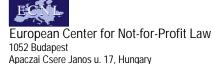
The specific procedures of course vary, depending on the country's regulatory scheme. Generally, however, CSOs applying for public benefit status must submit documentation indicating (1) the qualifying public benefit activities; (2) compliance with internal governance requirements, including safeguards against conflict of interest and self-dealing; and (3)

[&]quot;1. The costs of the Council that stem from services, conducting research, and preparing expert studies, as well as the participation in sessions by experts and individuals who are not members of the Council, are partly covered from the budget at the disposal of the minister responsible for social security.

^{2.} Participation in the works of the Council is remunerated with per diems and reimbursement of travel expenses defined in the regulations based upon art. 77(5), point 2 of the Labor Code."

^{3.} An employer should grant an employee who is a member of the Council a leave in order to allow him or her to participate in the sessions of the Council. For the period of the leave the employee is entitled to remuneration calculated to be the financial equivalent of holiday leave. This is covered by the budget at the disposal of the minister responsible for social security."

³³ "Public Benefit Commissions: A Comparative Overview - Armenia, England/Wales, Moldova", published by ICNL, 2005 (http://icnl.org/knowledge/pubs/PBCommissions.pdf)



www.ecnl.org



International Center for Not-for-Profit Law 1126 16th Street NW, Suite 400 Washington D.C. 20036, USA Tel: +1 202 452 8600 Fax: +1 202 452 8555 www.icnl.org

compliance with activity requirements (extent of public benefit activity) and limitations on activity (for-profit, political, etc.).

Detailed procedures for public benefit registration are contained in separate public benefit legislation, such as we find in Hungary or Poland. The goal of these requirements is to ensure that the organization is focusing predominantly on public benefit activities, that it is not engaged in other activities to the detriment of its public benefit mission, and that it maintains appropriate standards of transparency.

<u>Section 4, of the Public Benefit Act, in Hungary</u> lists the specific provisions that must be included in the organization's founding instrument, including the following:

- (1) the list of public benefit activities;
- (2) a clause stating that the organization conducts entrepreneurial activities solely in the interest of and without jeopardizing its public benefit activities;
- (3) a clause stating that the organization does not distribute business profits, but devotes them to its statutory activities;
- (4) a clause stating that the organization is not involved in direct political activities and does not provide financial aid to political parties; and
- (5) clauses relating to internal governance, conflict of interest and reporting requirements.

Procedural safeguards to protect applicants are the norm. These include time limits for the registration decision, a requirement for the decision-making body to provide, in writing, the reasons for denying registration, and the right to appeal an adverse decision to an independent arbiter. Hungarian courts must decide on public benefit applications within 30 days – or 45 days, if additional information is required; an adverse decision can be appealed to the superior courts within 15 days. Polish courts must rule on applications within three months, but in practice take about six weeks. Bulgaria imposes even stricter limits for government action; the Ministry of Justice must decide on public benefit applications "immediately". The failure to grant registration within 14 days is considered a tacit denial of registration. In the case of denial, the applicant may appeal to the Supreme Administrative Court within 14 days. The Charities Act of 2006 introduced the Charities Tribunal, an appeal body, which will deal with appeals against and reviews of Commission decisions and referrals from the Commission or Attorney General involving the operation or application of charity law. The purpose for setting up this Tribunal was to ensure that it would be easier and less expensive for charities to challenge the Commission's decisions.³⁴ Laws should also contain **grounds for refusal** to grant the organization a public benefit status.

Section 8, PBO Law, Latvia

(1) The Ministry of Finance shall take a decision, based upon an opinion of the Commission, to <u>refuse</u> the granting of public benefit organisation status if:

³⁴ http://www.charitycommission.gov.uk/spr/briefing.asp



www.ecnl.org



International Center for Not-for-Profit Law 1126 16th Street NW, Suite 400 Washington D.C. 20036, USA Tel: +1 202 452 8600 Fax: +1 202 452 8555 www.icnl.org

(i) the indicated aims in the articles of association, by-laws or constitution of the association or foundation or the activities of the association, foundation or religious organisation do not conform to the essentials of public benefit activities; (ii) the State Revenue Service territorial office, the Office of the Prosecutor, another institution or court has determined significant violations of regulatory enactments in the activities of the association, foundation or religious organisation;

- (iii) the association, foundation or religious organisation has a tax debt; or (iv) the association, foundation or religious organisation has not submitted all of the information and documents referred to in Section 7, Paragraphs two and four of this Law.
- (2) An applicant has the right to appeal a refusal to grant public benefit organisation status to a court according to the procedures specified in Administrative Procedure Law.

As a procedural shortcut, countries granting public benefit status often allow an organization to **register simultaneously** as a CSO (association or foundation or other organizational form) and as a public benefit organization. Such is the case in Greece and Hungary, as well as Kosovo. Bulgaria is an exception; there, courts are responsible for CSO registration and, subsequently, the Ministry of Justice processes applicants for public benefit status.

Some countries also regulate the issue of **registration of an organization after it has obtained and lost the PBO status**. For example, in Bulgaria, such an organization may apply for PBO status one year after it has lost its status. This right can be exercised only once. Latvian law contains the same rule.

A final issue which should be considered in the registration process is if the PBO status is granted upon a formal check up if the organization is complying with the legal requirements or upon a substantive check up of the actual activities of the organization. For example, in Hungary the process of granting the status is similar to the registration as an association or foundation. The procedure is formal and implies only the submission of the documents required by law to the court. There is not much space for a merit judgment. In England and Wales, the primary purpose of registration is to ensure that the charity has exclusively charitable purposes and its activities in practice will all be charitable. Therefore, the Commission performs a substantive review of the proposed activities listed in the governing documents. If it finds that those proposed activities are not charitable, first it will provide advice on the necessary alteration and if the charity does not comply; the Commission will refuse to register the charity. The secondary purpose of registration is to ensure best practice in the organization. Hence, the Commission recommends the use of model governing documents and will review governing documents submitted and make a best practice recommendation. However, a poorly drafted document is not a reason for rejection of registration.

Facilitating the recognition of public benefit organizations is in the state's interest. Registration requirements that delay such recognition or impose unnecessary requirements will only interfere with the work of public benefit organizations. Whether contained in the law or in accompanying



www.ecnl.org



International Center for Not-for-Profit Law 1126 16th Street NW, Suite 400 Washington D.C. 20036, USA Tel: +1 202 452 8600 Fax: +1 202 452 8555 www.icnl.org

regulations, the legal framework must set forth clear procedural requirements that facilitate registration while imposing appropriate standards of accountability and transparency.

VII. BENEFITS FOR PUBLIC BENEFIT ORGANIZATIONS

Public benefit recognition would have no real meaning if there were no state benefits provided to facilitate the work and sustainability of PBOs. State benefits typically come in the forms of tax exemptions on organizational income, tax incentives for the organization's donors, and VAT relief. PBOs may also receive state subsidies or grants, and preferential treatment in procuring certain government contracts.

Most commonly, the state extends tax benefits to PBOs. **Tax exemptions** may take a variety of forms and are usually available only if the income is used to support the public benefit purpose. The following categories of income may be exempt from taxation:

- Income from grants, donations, and membership dues;
- Income from economic activities;
- Investment income;
- Real property;
- Gifts and inheritance.

In addition, many countries extend exemptions or preferential rates on value added tax (VAT) to PBOs or to organizations engaged in transactions of certain goods and services related to the public benefit.

Crucial to encouraging private philanthropy to support public benefit activity are tax incentives to individuals and corporations donating to PBOs. Such tax incentives may take the form of tax credits, or more typically, tax deductions. Almost invariably, **donor incentives** are linked to either the public benefit status of the recipient or to enumerated public benefit activities in which the recipient is engaged. For example, Hungary, France and Germany allow only public benefit organizations to receive tax-deductible donations.³⁵

The state may also provide **other forms of support** to public benefit organizations, including the following:

- Many sources of grants, including the National Lottery, are available more easily, or exclusively, to charities (UK);
- A PBO may purchase "the right of perpetual usufruct of estates that are owned by the State Treasury or local self-government units" (Poland);

³⁵ In France, only general interest associations, public utility associations, and public utility foundations (all categories of PBOs) are entitled to receive tax-deductible donations. In Germany, only certain public benefit organizations (those pursuing general public benefit purposes, benevolent or church-related purposes, or especially support-worthy general purposes) may receive tax-deductible contributions.



www.ecnl.org



International Center for Not-for-Profit Law 1126 16th Street NW, Suite 400 Washington D.C. 20036, USA Tel: +1 202 452 8600 Fax: +1 202 452 8555 www.icnl.org

- A taxpayer may allocate 1% of his/her tax payment for the sake of public benefit organizations chosen by him or her (Poland);
- Users of PBO services are entitled to a personal tax exemption for the value of the service received (Hungary); and
- PBOs are eligible for a range of tax benefits related to hosting volunteers e.g. tax free reimbursement of expenses related to the volunteer work (Hungary).

VIII. OBLIGATIONS OF PUBLIC BENEFIT ORGANIZATIONS

The right of PBOs to greater state benefits brings with it more stringent obligations and reporting requirements. Since, PBOs are recipients of direct and/or indirect subsidies from the government they are naturally subject to greater government scrutiny. The purposes of this scrutiny are to protect the public from possible fraud and abuse by CSOs and to ensure that public support is linked to public benefit. In positive terms, the goals of supervision are to promote the effective operations of PBOs, by supporting good management, appropriate to the size of the organization, and to ensure that public benefit organizations are accountable to their members, beneficiaries, users and the public. The degree of supervision should be proportionate to the benefits provided, and not so intrusive as to compromise the organization's independence.

1. Rules regarding use of property, transformation and liquidation

When PBOs are exempt of relevant taxes, they often face greater **restrictions on the use of their property** than organizations which have not obtained this status, in order to ensure that public money is not used for the private purposes of members closely linked to the organization.

Section 12, Latvian Law on PBO

- (1) It is prohibited for a public benefit organisation to divide its property or financial means between founders, members of boards of directors and other administrative institutions (if such are established), as well as to utilize it so that directly or indirectly a benefit is obtained (guarantees, loans, promissory notes, as well as other material benefits.
- (2) The provisions of Paragraph one of this Section shall apply also to the founders, members of boards of directors and other administrative institutions (if such are established) of the public benefit organisation, spouses, kin and affine, counting kin up to the second degree and affine up to the first degree.
- (3) If a person receives remuneration for work in a public benefit organisation, such remuneration shall be reasonable and justified by the work performed and the financial circumstances of the public benefit organisation.

The Hungarian law prescribes that PBOs cannot provide "targeted grants to responsible persons, supporters and their relatives, with the exception of services available to anyone without

Copyright © 2007 by the European Center for Not-for-Profit Law, International Center for Not-for- 26 Profit Law and the Macedonian Center for International Cooperation. All rights reserved."



www.ecnl.org



International Center for Not-for-Profit Law 1126 16th Street NW, Suite 400 Washington D.C. 20036, USA Tel: +1 202 452 8600 Fax: +1 202 452 8555 www.icnl.org

limitation and grants corresponding to the founding document and provided on the basis of the legal relationship between civil society organizations and their members."³⁶

An important constraint that can be found in many laws is the **prohibition of transformation** of the public benefit organization into an organization pursing private benefits (e.g., Bulgaria). Section 16 of the Latvian law provides that in the case of the reorganization of an association or foundation, the public benefit status shall not pass on to the acquiring association or foundation, except in the case when the reorganization is performed by way of merger and the association or foundation to be merged is a public benefit organisation at the moment of reorganization. In the case of the division of an association or foundation, the divided organization retains the public benefit organisation status.

Liquidation rules are also specifically prescribed in most of the laws regulating the public benefit status. In Latvia, in case of liquidation or withdrawal of the status, the undivided property of the PBO will may be transferred to a PBO specified in a decision of the Commission which has similar aims of activities; and if this cannot be performed than the undivided property will pass to the State, "which shall utilise it as far as possible in accordance with the aims indicated in the articles of association of the public benefit organisation."³⁷ In Bulgaria, the property after liquidation can be transferred to another PBO by decision of the court; and, in case this it not possible, to the municipality by domicile of the dissolved non-profit legal entity.

Article 43 (2), of the Bulgarian Law:

The property may not be assigned in any way whatsoever to:

- 1. the founders and present and former members;
- 2. persons who have been members of the bodies, and employees of the legal entity;
- 3. the liquidators, except for their due valuable consideration;
- 4. spouses of the persons under sub-paragraphs 1 3;
- 5. relatives of the persons under sub-paragraphs 1 3 of direct descent without limit, collateral relatives to the fourth branch, or in-laws to the second branch, inclusive;
- 6. legal entities in which the persons under sub-paragraphs 1 5 are managers or may impose decisions or hinder decision making.

According to the Polish law, if the organization is removed form the Register, it is obliged, within 6 months, to spend, on its own activities, the means gained through public fund-raising, which were gathered in the period when the organization possessed the status of a public benefit organization. The means that have not been used in the manner and during the will be transferred to an organization that runs statutory activities in the same or similar scope, and which is chosen by the Minister responsible for social security.

_

³⁶ Article 14 of the Law.

³⁷ Article 17, Latvian Law on PBO.



www.ecnl.org



International Center for Not-for-Profit Law 1126 16th Street NW, Suite 400 Washington D.C. 20036, USA Tel: +1 202 452 8600 Fax: +1 202 452 8555 www.icnl.org

2. Supervision and Accountability

Supervisory Authorities

The governmental body authorized to regulate PBO activity varies widely from country to country. In nearly every country, **the tax authorities** play a prominent supervisory role, through their control over the tax treatment of PBOs. Indeed, in countries like Germany and the Netherlands, where public benefit regulation is primarily an issue of tax regulation, it is the tax authorities that play the central supervisory role. In other countries, **a ministry** may be vested with primary authority over PBO supervision, such as the Ministry of Justice in Bulgaria or the Ministry of Social Security in Poland. In France, the Ministry of Interior and the *Prefet du Departement* exercise supervision over public utility foundations. In Hungary the **public prosecutors** are the main supervisory body for PBOs (as well as all registered NGOs).

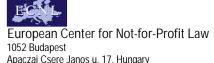
Other specialized government organs may be involved with specific aspects of PBO supervision, including the spending of state budgetary funds and general legal compliance. In Hungary, for example, when a PBO has received funding from the state budget, the State Audit agency may monitor the use of these funds; the public prosecutor has authority to investigate potential legal violations. In Bulgaria, the Ministry of Justice can notify the public prosecutor and bodies of State Financial Control, in the event of a violation of law. Similarly, in Germany, the Ministry of Interior Affairs has supervisory authority over non-fiscal infringements, and civic organizations are subject to state control according to the respective laws of the *Bundeslander*, meaning that each state has its own supervisory system.

As highlighted above, the Charity Commission of England and Wales represents a unique approach to the regulation of public benefit organizations (or charities). The Commission has five broad functions, which include registration, accountability, monitoring, support and enforcement. Underscoring all of these functions is the Commission's general duty to enhance charitable endeavor.

Reporting.

To ensure that PBOs are transparent and accountable, the state has legitimate interests in receiving information. Relevant information includes (1) **financial information** (e.g., annual financial statements, an accounting of the use of assets obtained from public sources and claimed to be used for public benefit) and (2) **programmatic information** (e.g., a report on activities made in the public interest).

Most commonly, a PBO files reports with the tax authorities, including annual tax returns (even if the organization is exempt) and/or tax benefit application forms (submitted voluntarily), as well as annual activity reports to the supervisory ministry or agency. In France, public utility foundations submit an annual report and financial statement to the competent *Prefet* and the Ministry of Interior. In Germany, civic organizations must present annual reports to the relevant state authorities (according to the laws of the *Bundeslander*) and, to receive tax privileges, to the



www.ecnl.org



International Center for Not-for-Profit Law 1126 16th Street NW, Suite 400 Washington D.C. 20036, USA Tel: +1 202 452 8600 Fax: +1 202 452 8555 www.icnl.org

financial authorities (the tax exempt status is reviewed every three years). In Poland, PBOs must prepare and submit an annual activity report and annual financial statement to the Ministry of Social Security. The law states that these organizations "prepare and announce annual financial statements even when other accounting regulations do not require it." In Hungary, a PBO must prepare and make available on its website a public benefit report (containing an accounting report, a summary of public benefit activity, and information regarding the use of public support, the use of own assets, amounts of budgetary subsidies received, and amount of remuneration extended to senior officers). Interestingly, however, Hungary does not require the submission and filing of a public benefit report with a ministry or regulatory authority, but only that the report be made available for review (if the organization does not have a website, making "publicly accessible" will suffice).

In England and Wales, the accountability framework is graduated according to the size of the charity, with simple reporting of activities and receipts and payment accounts for small charities, and sophisticated reporting and accounting for large charities. The threshold is set at the annual income level of 10,000 British pounds. Those below the threshold need only make reports available for inspection, but do not have to file reports; those above the threshold must complete a more detailed return and send the report to the Commission. Those above 250,000 pounds a year must have a full audit undertaken by a qualified auditor.

Appropriate disclosure of information enables the public to exercise oversight responsibilities.³⁹ Recognizing this valuable role, many countries expressly require public disclosure. In Bulgaria, "The report of the [PBO] shall be public. The notification for availability of the elaborated report, as well as for the place, time and procedure for access thereto, shall be published in the bulletin of the central register." ⁴⁰ In Poland, a PBO makes its annual report "public in a manner that is accessible to anyone interested." In Hungary, "Reports on public welfare activities ... shall be available for review by the public, and anyone may make copies of such at his own expense." ⁴²

Audits and Inspections.

In addition to reporting obligations, authorities often employ other monitoring tools, such as government audits and inspections. In Germany, for example, tax authorities may conduct **regular tax inspections**, following notice and an adequate time for the CSO to prepare; VAT inspections may, however, be conducted without prior notice. Hungarian PBOs are subject to supervision by the State Audit Office for the use of budgetary subsidies. In Bulgaria, PBOs are subject to **financial audits for the use of state or municipal subsidies or grants** under

_

³⁸ Article 23 of the law.

³⁹ Preferred methods of disclosure include publication in the newspapers (Czech Republic), publication on the website (Hungary) or making the information available to the public at the organizational premises (Hungary).

⁴⁰ Bulgarian Law on Nonprofit Legal Entities, Article 40(3).

⁴¹ Polish Law on Public Benefit Activities, Article 23(1).

⁴² Hungarian Law on Public Benefit Organizations, Article 19 (5).



To52 Budapest
Apaczai Csere Janos u. 17, Hungary
Tel: +361 318 6923 Fax: +361 266 1479
www.ecnl.org

ernational Center for Not-for-Profit Law 1126 16th Street NW, Suite 400 Washington D.C. 20036, USA Tel: +1 202 452 8600 Fax: +1 202 452 8555 www.icnl.org

European programs. The responsible auditing body must have cause to justify the audit, but there is no requirement of prior notification.

<u>Articles 28-33 of the Polish Law</u>, spell out the procedures for carrying out inspections of PBOs in detail.

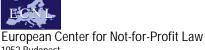
The Ministry of Social Security is authorized to conduct inspections or to commission a provincial governor to perform the inspection. The Ministry has the right to access an organization's property, documents and other carriers of information, as well as to demand written and oral explanations. Such an inspection must be performed in the presence of a representative of the PBO or other witness. The inspecting officials must prepare a written report; the head of the PBO then has the opportunity to submit a written explanation or objections to the content of the report, within 14 days. Once filed, the inspection report describes the facts found during the inspection, including any deficiencies, and provides not fewer than 30 days to correct them. The PBO Council may accompany the inspection visits conducted by the Ministry responsible for issues of social security.

In England, the government has no powers to investigate charities as such. The authorities do, of course, have a range of powers – related to terrorism and criminality (police), financial malpractice by companies or banking agencies, childcare (Social Services Inspectorate) – but these are generic and not specific to the charitable sector. Independent of government, the Charity Commission is vested with **supervisory and investigative** power, through which it seeks both to encourage good practices (as a support and advisory body) and to tackle abuse (as an investigative body).

The Commission's Support Division is responsible for giving advice and guidance to organizations on a range of legal, governance, management and financial issues. To make these services more widely available, the Support Division engages in outreach, including visits to individual charities, road shows open to charities, and conferences. The Commission's Investigation Division is responsible for combating abuse; it can suspend trustees, freeze bank accounts and appoint a receiver and manager to act in place of the trustees. Although the Commission does not have the power to de-register a charity, it can act to dissolve a charity by transferring all of its resources to a comparable charity. These two Divisions, along with the Registration Division, are supported by a team of lawyers and accountants who provide professional expertise.

The key to Commission action is proportionality. Smaller charities (with an annual income of less than 10,000 British pounds) are handled deferentially. "Audit" is not a term the Commission uses; instead it has developed the practice of pre-announced visits to examine a charity's administration. The Commission focuses on larger charities (based on cause) with the aim of promoting good practice. Initiating an investigation without cause runs against the ethos of the Commission.

State Enforcement, Sanctions and Withdrawal/Termination.





European Center for Not-for-Profit La 1052 Budapest Apaczai Csere Janos u. 17, Hungary Tel: +361 318 6923 Fax: +361 266 1479 www.ecnl.org International Center for Not-for-Profit Law 1126 16th Street NW, Suite 400 Washington D.C. 20036, USA Tel: +1 202 452 8600 Fax: +1 202 452 8555 www.icnl.org

State sanctions against CSOs often include the **imposition of fines**, for violations such as the failure to file reports. The continued failure to file reports can lead to termination and dissolution in most countries. Termination, however, should occur only after the organization is given notice and an opportunity to remedy the deficiency. With both fines and termination orders, the CSO usually has the opportunity to file an appeal.

Additional sanctions may be available against public benefit organizations; these typically include the **loss of tax benefits** or **the termination of PBO status**. In Bulgaria, for example, no fines can be levied against PBOs; instead, systematic non-compliance with reporting requirements can lead to the PBO's termination. In Germany, Kosovo and Romania, PBOs that fail to file reports may also lose their public benefit status. Somewhat similarly, public benefit companies in the Czech Republic may lose comprehensive tax benefits in the year of breach and other more limited tax benefits in the following year.

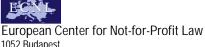
Revocation of public benefit status should only be available as a sanction under exceptional circumstances. If an organization in Hungary violates the law or its founding charter, for example, the court can revoke its public benefit status at the request of the public prosecutor, but only after notifying the organization and giving it the opportunity to remedy the situation. In Poland, if the PBO fails to eradicate problems identified during the inspection process within a given time period, the Minister of Social Security can file to have the organization removed from the State Court Register. Note that in both cases the government must first notify the organization of the violation and give it an opportunity to eliminate the problem, and the decision on revocation is made by the court. In Latvia, the Ministry of Finance, prior to taking a decision regarding the withdrawal of public benefit organisation status, has the right to request an opinion from the Public Benefit Commission regarding the violations. The status may be withdrawn only if the organization has not rectified the problem within the set deadline specified in the written warning by the Ministry.

IX. CONCLUSION

The regulatory approach to public benefit status differs in countries throughout Europe. The main aims in introducing this status are to promote public benefit activities and to ensure that tax benefits granted to PBOs are related to purposes and activities which are of benefit for the public and the society. However, public benefit status can be also introduced in order to extend other types of state benefits to organizations engaged in activities for the benefit of the society or to support cooperation between the governments and CSOs, or to enhance the image and accountability of the sector. The goals that legislators aim to achieve in introducing this status

_

⁴³ Such is the case in Bulgaria, where the state may penalize CSOs from 50-500 EUR. In Poland, an association that does not comply with requests for documentation is subject to a one-time fine not to exceed 50,000 zlotys (approximately 11,300 EUR), which may be waived if the association complies immediately after the fine is imposed. In Slovakia, a foundation failing to file a report may be fined from SKK 10,000 to 100,000 (approximately 250-2500 EUR). In many countries (Bosnia, Croatia, Serbia and Montenegro), fines may be levied against both the organization and against the responsible representative of the organization.





1052 Budapest Apaczai Csere Janos u. 17, Hungary Tel: +361 318 6923 Fax: +361 266 1479 www.ecnl.org International Center for Not-for-Profit Law 1126 16th Street NW, Suite 400 Washington D.C. 20036, USA Tel: +1 202 452 8600 Fax: +1 202 452 8555 www.icnl.org

should drive the general policy in regulating public benefit. Consideration should also be given to numerous local factors (existing legal framework, local culture and traditions, existing benefits, the level of development of the third sector, the relationship with the government) that will influence the implementation of the regulation, in order to ensure that it achieves the desired result.

This paper aimed to raise, the most common issues and best practices discussed in countries throughout CEE when launching a process to introduce public benefit status. Those include:

- What are the regulatory approaches in Europe? Should the state regulate in the framework law, tax laws, or enact a separate law on public benefit status?
- What are the criteria for granting public benefit status? Which are the eligible entities that can apply for this status? To what extent should the activities of the organizations be of public benefit in order to receive this status, and who should they target?
- Who grants the public benefit status? A tax authority, court, independent commission, a line Ministry?
- What is the procedure for granting public benefit status?
- What are the benefits and obligations for public benefit organizations?

Where appropriate, the paper also describes the difference in regulating public benefit in England and Wales (as common law countries) and countries in continental Europe. The paper does not aim to answer all questions, as the specific approach depends on the local circumstances and overall environment. Policymakers and legislators throughout Europe have been creative in adopting various solutions, described in this paper, hoping to achieve the goals of the legislation. We hope that those solutions can serve as an inspiration, while the lessons learnt as guidance to the countries which are yet to define and introduce the concept in their societies.