

CHALLENGES TO EXPANDING A NON-PROFIT INTO RUSSIA

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I. Introduction

In the past 20 years since the fall of the Soviet Union there has been a steady growth of private business opportunities in the Russian Federation. Russia is attractive to foreign businesses because of its emerging market economy and its need for foreign capital to fund it. Foreign direct investment (“FDI”) has been encouraged by Russian politicians, who have emphasized throughout the last decade that foreign investment is a priority of Russia’s foreign policy.¹ The largest FDI was documented in the manufacturing, wholesale/retail, mining, real estate, as well as professional and administrative service sectors.² What is overlooked by the Russian government, however, are important issues such as subpar social programs, anti-Semitism and violence against ethnic groups, and low environmental standards.

In regard to these frequently overlooked issues, Russia citizens often rely on non-profit organizations—internationally referred to as Non-governmental Organizations (“NGOs”), i.e., they are not part of government and are not conventional for-profit businesses.³ In Russia, NGOs are formed either as Public Associations (including foundations and partnerships) or Non-Commercial Organizations (“NCOs”) with Public Associations comprising 70% of the existing NGOs in Russia.⁴ NGOs in Russia have the opportunity to provide “vital services in such areas as human rights, social support, education, and environmental activism.”⁵ Some of the major NGOs that have affiliate offices in Russia include the International Youth Foundation, Adventist Development and

Relief Agency, the MacArthur Foundation, Partners in Health, and the Moscow Helsinki Group.

Unfortunately, the Russian government does not view NGOs in a positive light and this is especially true when they are foreign-owned or funded. The Russian government has publically discredited and raised suspicions of NGOs, stating that they are mechanisms for foreign governments to interfere in Russia's internal affairs and carry out their policies.⁶ International and foreign-funded NGOs that promote human rights protection, environmental monitoring, and law enforcement are often perceived as enemies.⁷ Coincidentally, NGOs that receive foreign support are not treated on equal basis with purely domestic NGOs—they face burdensome registration procedures and/or heightened standards on reporting and activity control. Because of these restrictive procedures, it is not surprising that out of the USD \$233.8 billion FDI poured into Russia in 2011, less than USD \$1 billion total was invested in sectors such as human health, social work, and education.⁸ This article addresses the most common challenges encountered for non-profits who seek to expand in to Russia. First, we will discuss the formation concerns for NGOs in Russia, and second, operating uncertainties facing foreign-owned or funded NGOs.

II. Foreign entities seeking to expand NGO activities into Russia face formation restrictions and other bureaucratic barriers.

If you are a foreign (non-Russian) entity, forming and supporting a domestic NGO in Russia is confined to a specific class of persons. Only those foreign nationals who are legally domiciled in the Russian Federation may be founders, members, or participants in Public Associations or any other NCOs.⁹ Moreover, persons deemed “undesirable” may not become founders, members, or participants in the Russian NGO. An

undesirable person may be anyone who subjectively “shows signs of extremist activity.”¹⁰ This stems from the Russian Government wanting to have the ability to restrict participation of anyone who it projects to be critical of the current regime.

So if you want to register as a domestic Russian NGO, not only do you have to find capable individuals residing in Russia, but you must also think about how the registration office will scrutinize the desirability of such persons. If your NGO is already established and operating in other countries, you cannot register as a domestic Russian entity. Rather, you can create a new affiliate company and register as a foreign company with programs supportive of your mission.

If your organization is a foreign NGO in Russia; however, such registration is also made difficult. International non-profit organizations must, within three months of establishing an affiliate office in Russia, notify the government and provide information for legal registration.¹¹ There is an overwhelming amount of paperwork that the registrant must complete—“detailed audits of financial records and sources of funding, down-to-the-penny accounting of how that funding will be spent, profiles of all the founders of an NGO, even those no longer affiliated.”¹² Among the various documents, the notification must include the goals and tasks of establishing the affiliate office in Russia.¹³

As of 2009, foreign NGOs may no longer be refused registration based on criteria such as “threats to unique character, cultural heritage, or national interests” of the Russian Federation.¹⁴ However, a foreign organization may still be denied registration for vague reasons, such as posing a threat to Russia’s sovereignty, political independence, or territorial integrity.¹⁵ The activities of a foreign organization expanding into Russia can thus be limited and controlled by the registration office, which can choose to enforce the vague terms or not. One example is Rainbow House, which advocates lesbian, gay, bisexual and transgender rights; it was denied registration

because it was found to “undermine sovereignty and territorial integrity” of the Russian Federation.¹⁶

The actual registration procedures for establishing a Public Association or an NCO in Russia are ambiguous and bureaucratic. The various requirements have proven to be especially confusing to foreign organizations. After the 2006 NGO law overhaul, the ambiguities were evidenced by forty consecutive foreign applicants being turned down, presumably for incorrectly completing paperwork.¹⁷ Grounds for refusal are neither clear nor finite, and are subject to broad interpretation.¹⁸ The bureaucrats can essentially choose new grounds for refusing registration. The laws fail to define terms and concepts that could help in the registration process. For example, terms such as enlightening activity, location of a permanently functioning body, and territory of the activity of the NGO – to name a few.¹⁹

In addition, there are no criteria for determining what constitutes activity in accordance with or outside of the goals of an organization’s charter.²⁰ If the Registration Office deems any application section unacceptable it may give the applicant an opportunity to amend, but it also has the power to deny registration. And if you are denied, you must start the registration process from anew. Therefore, it is suggested to obtain assistance from local Russian resources prior to the registration. For example, Vista Foreign Business Support (VFBS) offers incorporation services for both commercial and non-commercial organizations, as well as official recognition assistance for representative offices of foreign companies expanding into Russia.²¹ The NGO-Corporate Partnership Committee, created by the American Chamber of Commerce in Russia, helps member NGOs overcome barriers and address common problems. They can connect companies with others who have previously been through the process and know how to approach specific issues. Such resources can help foreign NGOs save time and funds needed to meet Russian registration requirements.

III. NGOs who expand activities into Russia face operating uncertainties and impediments

The programs of foreign NGO's operating in Russia frequently face intense scrutiny. The Russian government can ban the existing programs of a foreign NGO and there is no way to predict these prohibitions.²² Officials can also ban transfers of funds and resources from a foreign affiliate to an NGO office in Russia. Possible reasons include: protection of morality, health, legal rights and interests of others.²³ Current regulations allow authorities to dissolve and liquidate an NGO that may have had just minor compliance issues. For example, a violation that can lead to an involuntary liquidation is failure to convene a general meeting within the required period.²⁴ In 2006, the Russian-Chechen Friendship Society, which promoted regional tolerance and distributed information about human rights violations was closed and liquidated by court order.²⁵ The reasons for why it was shut down were that it was presumably headed by a person involved in "extremist" activity and the NGO did not oblige with an order to remove the word "Russian" from its name.²⁶ Political conflicts in the North Caucasus region of Russia still exist. And the Russian Government takes notice of anyone who is a dissenting voice to its efforts in those territories.

Next, NGOs that are registered as international organizations in Russia or receive foreign funding face oppressive reporting requirements. Government bodies can make broad document demands, such as obliging those entities to provide all financial documents, without limitation, for a given tax year.²⁷ Foreign NGOs operating in Russia, unlike their domestic counterparts, cannot benefit from the simplified tax reporting procedure.²⁸ And domestic NGOs making under \$100,000 annually are not required to formally report their income; however, similar NGOs that have foreign founders or funding must

report.²⁹ To lessen the reporting duties, domestic NGOs seem to be the preferred choice to organize in Russia (assuming one meets restriction criteria).

However, domestic NGOs must report the funds and assets received from foreign or international sources and how they are intended to be used.³⁰ The Russian government and the for-profit sector provides very little support to NGOs, which often they have no choice but to rely on international funding.

Furthermore, there are no limitations on "unplanned" audits that the government bodies can initiate, in addition to the required annual audit.³¹ Surprise audit of foreign-owned or funded NGOs is a method Russian officials utilize to "bring foreign agents to heel."³² The auditing procedure itself is enough to shut down an NGO for several weeks, as the entire staff is redirected to the collection of necessary information.³³ Several NGOs have been shut down for arbitrary reasons, such as improperly binding their audit papers.³⁴ Thus, if you plan to establish an affiliate NGO in Russia, you should carefully plan out the staffing requirements as well as the funding and record-keeping policies.

A new law proposed on June 29, 2012 will require domestic NGOs who receive foreign funding and intend to participate in "political activities" to register with the Ministry of Justice as a "foreign agent," which is akin to a spy, prior to receiving any foreign funds.³⁵ The bill interprets political activities broadly, including any acts that influence public opinion on public policies.³⁶ The Russian Parliament passed the bill on July 18th and it will go in to effect within 90 days after its passage.³⁷

Numerous NGOs worry that the "foreign agent" label could harm their image, dissuade the population from trusting in their work and acting on their advice.³⁸ They have also expressed concerns that such designation is meant to red flag the company for heightened scrutiny. Failure to comply with registration requirements is punishable by a six-month suspension of activities, up to 1,000,000 Rubles (about US\$30,000) in penalties, and a 2

year prison term.³⁹ It is not yet clear how burdensome the registration procedures will be under the new bill. What is known is that the subject NGOs will have to maintain separate accounting of foreign and domestic assets and submit quarterly reports.⁴⁰

Compliance with the bill is mandatory. A Russian deputy recently stated that the law will only negatively impact those NGOs that try to effectuate a change in the political power structure, and not those who advocate for general changes in laws.⁴¹ It is unclear whether this will be the actual result. The Russian government has historically been concerned with the image of its regime. And that has certainly been the case with its current political leaders.

IV. Conclusion

NGOs who wish to operate in Russia can pursue the much needed missions in civil rights, social support, education, modern medicine, and environmental activism. Foreign-owned or funded NGOs can continue to further human rights and social programs in Russia, they just need to forego open criticism of the government authorities. The same limitations apply to lobbying programs in opposition to Russia's military, international, or other major policies.

Entities should seek out early guidance from the available resources that can streamline the burdensome registration procedures and help implement efficient accounting systems. While the accounting procedures will be more demanding under the new law, lesser known NGOs might actually benefit by from the exposure. Despite, some clear challenges to NGOs that want to expand into Russia, it can be done and there is support for the process.

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¹ Kashin, Konstantin, *Welfare Impact of Foreign Direct Investment in Russia: Do the Poor Benefit?* 4 (April 2010), available at

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² Kashin, *Id.* at 68 (based on 2008 statistics); *See also* <http://www.amcham.ru/regions/regionalinvproj> (mentioning current opportunities in the energy, communications, oil & gas, manufacturing, and food and beverage sectors.)

³ Wikipedia, *Non-Governmental Organization*, http://en.wikipedia.org/wiki/Non-governmental_organization (last visited July 9, 2012)

⁴ The Int'l Center for Non-profit Law (hereafter "ICNL"), *Int'l Law Monitor: Russia*, available at <http://www.icnl.org/research/monitor/russia.pdf> (last updated July 30, 2012)

⁵ Sharon Singh, *Press Release: Russia Must End Smear Campaign Against NGOs* (July 13, 2012), available at <http://www.amnestyusa.org/news/news-item/russia-end-%E2%80%98smear-campaign-against-ngos>

⁶ Human Rights Watch, *Choking on Bureaucracy, Efforts to Discredit Human Rights and Foreign-Funded NGOs 4* (February 20, 2008), available at <http://www.hrw.org/node/62400/section/4>

⁷ Aleksej Bogoroditskii, *The Int'l Journal of Non-Profit Law* (Vol. 10, Issue 3, May 2010), available at http://www.icnl.org/research/journal/vol12iss3/special_4.htm

⁸ Central Bank of the Russian Federation, *Foreign Direct Investment in Russia by Industry, 2010 - Q1 2012*, http://www.cbr.ru/eng/statistics/print.aspx?file=credit_statistics/inv_in_rus_e.htm&pid=svs&sid=ITM_48993&pid=svs&sid=ITM_5584_1 (last accessed July 20, 2012)

⁹ Federal'nyi Zakon RF o Obshesvinnih Objedenenijah [Federal Law on Public Associations], *Sobranie Zakonodatel'stva Rossiskoi Federatzii [SZ RF] [Russian Federation Collection of Legislation] 1995*, No. Item 19 (hereafter "82-FZ"); Federal'nyi Zakon RF o Nekommerchiskih Organizatzei; [Federal Law on Non-Commercial Organizations], *SZ RF, 1996*, No. 7, Item 15 § 1.1 (hereafter "7-FZ").

¹⁰ 7-FZ, Item 15 § 1.2

¹¹ 7-FZ, Item 13.2 § 1.

¹² Charles Digges & Vera Ponomareva, *Russian-based Foreign NGOs in a Paper Chase to Beat Oct. 18th Registration Deadline, or Face Closure* (2006), available at http://www.bellona.org/articles/articles_2006/NGOlaw_preview

¹³ 7-FZ, Item 13.2 § 5.

¹⁴ Bogoroditskii, *supra* Note 7

¹⁵ 7-FZ, Item 23.1 § 2(2)

¹⁶ Human Rights Watch, *Russia: Revise NGO Law to Protect Rights*, <http://www.hrw.org/news/2009/05/13/russia-revise-ngo-law-protect-rights> (last accessed July 9, 2012)

¹⁷ Anastasia Korniya, *Non-Governmental Organizations Fail the Test*, NCSJ Weekly News Brief No. 7 (2006), accessible at <http://www.ncsj.org/AuxPages/Wkly060630.pdf>

¹⁸ Human Rights Watch, *Proposals on Changes to the Russian Federal Laws on Regulating NGOs* (2009), available at <http://www.hrw.org/news/2009/05/13/proposals-changes-russian-federal-laws-regulating-ngos>.

¹⁹ *Id.*

²⁰ *Id.*

²¹ Vista Foreign Business Support, <http://www.vfbs.ru/index.htm> (last accessed July 22, 2012)

²² ICNL, *International Law Monitor: Russia*, *supra* Note #4

²³ *Id.*

²⁴ Human Rights Watch, *supra* Note #18

²⁵ Statement from the Russian-Chechen Friendship Society following its forced closure, <http://www.frontlinedefenders.org/node/144> (last accessed July 9, 2012)

²⁶ *Id.*

²⁷ Human Rights Watch, *supra* Note #18

²⁸ Bogoroditskii, *supra* Note 7 (citing Item 346.12 § 3.18 of the Tax Code of the Russian Federation).

²⁹ Bogoroditskii, *supra* Note 7

³⁰ See 82-FZ, Item 29; See also 7-FZ Item 32 § 4.

³¹ Human Rights Watch, *supra* Note #18

³² Bellona, translated by Charles Digges, *Russian NGOs Face Surprise Audits Under New Amendments to Legislation*, http://www.bellona.org/articles/articles_2012/NGO_amendments (last accessed July 9, 2012)

³³ Charles Digges, *Medvedev Suggests Amendments to Russia's NGO Law – Human Rights Activists Suggest More*, http://www.bellona.org/articles/articles_2009/medvedev_ngo_amendments (last accessed July 9, 2012)

³⁴ *Id.*

³⁵ ICNL, *International Law Monitor: Russia*, *supra* Note #4 at *Pending NGO Legislative / Regulatory Initiatives*

³⁶ *Id.*

³⁷ Russian Parliament Passes NGO (“Foreign Agents”) Law, <http://www.trust.org/trustlaw/news/russian-parliament-passes-ngo-foreign-agents-law/> (last accessed July 22, 2012)

³⁸ The Observatory, Press Release, *Russian Federation: Utmost concern over new bill on Non-Commercial Organizations (NCOs)* (July 6, 2012), available at <http://www.omct.org/human-rights-defenders/urgent-interventions/russia/2012/07/d21857/>

³⁹ *Id.*

⁴⁰ *Id.*

⁴¹ Nickolaus Von Twickel, *Deputy Says NGO Bill Has Strict Limits* (July 19, 2012), available at <http://www.themoscowtimes.com/news/article/deputy-says-ngo-bill-has-strict-limits/462318.html>