



## INTERNATIONAL KNOWLEDGE AND EXPERIENCE EXCHANGE ON THE DEVELOPMENT OF NON-GOVERNMENT ORGANIZATIONS

*Ho Chi Minh, 31.07-01.08.2014*

### **Internal Governance of NPOs / Central and Eastern Europe**

The laws in Central and Eastern Europe vary greatly in the amount of detail with which they address NPO internal governance issues. Some simply require that the organization's statute outline the structure of the organization. Others spend pages of legislative text laying out voting procedures and quorum requirements, providing for management failures of various kinds, etc. In some cases, these detailed rules can be modified by an organization's statute or bylaws; in others, not.

#### *A. Internal Structure*

*1. Associations.* An association's highest governing body is the general assembly of its members. Several countries envision a management body in addition to the general assembly to deal with the day-to-day affairs of the association. In addition, many countries require the association to designate a person to have the general power to represent the organization in dealing with third parties. Most countries guarantee the right to withdraw from an association, and several allow members to contest association decisions contrary to law or statute. Countries may also specify (or require the organization's statute to specify) a variety of other features of associations, such as the criteria for accepting/expelling members, members' rights and duties, authority to represent the NPO, and other issues of internal governance.

It is common for legislation in the region to reserve decisions of particular importance to the general assembly. Acts commonly reserved to the general assembly include termination of the association; its transformation, division, or merger with another association; amendments to the association's statutory purpose; the election or recall of officers; and setting the amount of membership dues. Often the decisions to do these things require more than a standard majority vote.

Countries differ on the procedure to call a meeting of the general assembly of members. Many allow the procedure to be governed by the organization's statutes. Some also regulate additional issues, for example, the fraction of the members required to call a special meeting of the general assembly. A few also require that notice be given about what will be decided at the meeting. Laws that address the procedure to convene the general assembly usually also determine how many members must be present to constitute a quorum. Some also determine a procedure by which members can obtain redress if the association operates improperly. In Albania, Hungary, Romania, Bulgaria, and Estonia, laws give members the explicit right to go before a court to contest decisions they take to be contrary to law or to an association's statute. Such an objection must be filed within a fixed time period (typically, 10 days to three months).

*2. Foundations and Other Non-Membership Organizations.* In general, non-membership organizations are governed by a board of directors. They may also have separate management to conduct routine business of the organization and a separate supervisory board (or at least an auditor) to oversee the operation of the organization (making sure it does not act illegally or misuse its funds, etc.). A few organizations do allow founders to play a continuing role in the governance of the organization.



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## *B. Accountability: Duties and Responsibilities of Governing Bodies*

As a general rule, the highest governing body has the authority and duty to review and approve the annual budget, the annual financial report, and the annual activity report (if applicable). In addition, the highest governing body is empowered to set policy; to elect or appoint officers; to decide on transformation, termination and dissolution; and to decide on changes to the organization's governing documents. While the highest governing body may delegate certain powers to management—including, for example, signing powers – there are usually limitations on what powers may be delegated, such as the power to amend the statute or approve the budget.

Members of governing bodies may be personally liable for harm to the NPO or to third parties incurred as a result of the board member's breach of duties. In some countries, the liability to third parties lies with the organization and not with the individual members of the board, but the organization may recover damages from a responsible member of the board before a civil court. In other countries, the responsible board members may be held directly responsible for injuries to third parties where the responsible member acted in the exercise of duty, willfully, or with serious negligence.

## *C. Conflict of Interest*

Legal rules designed to prevent conflict of interest and self-dealing are increasingly common. Conflicts of interest may be addressed through (1) required disclosure of the conflict of interest between the individual and organization, (2) recusal of that individual from the decision-making process, (3) mandatory approval of any associated transaction by the highest decision-making body of the organization, and (4) a requirement that the transaction be at fair market value or on terms more favorable to the organization. Enforcement of conflict of interest rules may be based on a declaration of compliance with these rules submitted by the organization at the time of registration and subsequent changes in membership of the governing body. If a member of an association violates the conflict of interest rule—and the required majority approval could not have been obtained without the member's vote—he or she is responsible for the damages caused to the association.

In practice, few countries evidence a history of governing body members being held liable for violations of duties, such as the duty of care, duty of loyalty, the duty of good faith, etc. For those found liable of improper conduct, there is generally a right to appeal, according to general civil procedure rules.

## *D. Non-Distribution Constraint.*

Both associations and foundations are implicitly or explicitly bound by the “non-distribution constraint.” In some jurisdictions, a “positive formulation” is used: in Albania, for example, the law states that NPOs must use their income and property for the purposes specified in the organization's charter. In others, a “negative formulation” is employed: in Kosovo, an NPO “shall not distribute any net earnings or profits as such to any person.” Regardless of the precise formulation, the non-distribution constraint is the common attribute that distinguishes NPOs from commercial companies.