



Nonprofit
Enterprise and
Self-sustainability
Team (NESST)



The Legal and Regulatory Framework for CSO Self-financing in Argentina

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This guide examines the legal and regulatory framework governing the self-financing activities of civil society organizations (CSOs) in Argentina and provides an assessment of the relevant laws and their practical effects in order to identify areas where the law might be improved. Chapter 1 explains the regulatory environment as it relates to self-financing, defines the concept of CSO self-financing, and explains the methodology NESST used in researching and assessing the current legal framework in Argentina. Chapter 2 outlines a typology initially developed by the International Center for Not-for-Profit Law (ICNL). Chapter 3 describes the current regulatory framework in detail and its application in Argentina. Although CSO self-financing activities are permitted in Argentina, this chapter illustrates that tax laws vary, especially in regard to income tax, depending on the type of organization and its social purpose. This chapter also explains the procedures for CSOs to follow. Finally, Chapter 4 discusses the Argentine legal framework for CSOs carrying out commercial activities, including an analysis of two case studies, and makes recommendations for improvement.

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Guillermo Canova, lawyer, co-founder and legal director of the legal and fiscal framework commission (Comisión Marco Legal y Fiscal) of the social sector forum (Foro del Sector Social), and a specialist in nonprofit organizations. He has conducted research on the Third Sector and corporate social responsibility and has presented at a variety of national and international events and conferences related to the Argentine legal tax framework specifically relating to nonprofit entities.

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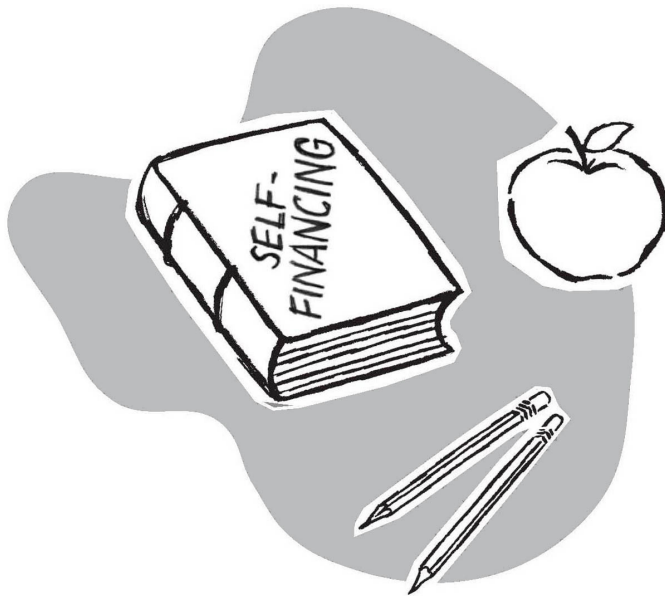
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Setting the Stage: Purpose and Methodology



The term "*civil society organization*" (CSO)¹ encompasses nonprofit, non-state organizations as well as community-based associations and groups that fall outside the realm of the government and business sectors. Given limited philanthropic and government assistance, many CSOs undertake self-financing activities² to generate revenues in support of their mission and programs.

NESST has documented over a hundred cases of CSOs in Latin America and Central Europe that engage in these types of activities, and has analyzed the impact of these strategies on the organizations' performance and sustainability. An important factor that emerged from this research is the need for a clear and supportive legal and regulatory framework to encourage the adoption of self-financing strategies among CSOs.

1 NESST uses the term *civil society organization* (CSO) to refer to a wide range of formally registered nonprofit, non-state organizations or community-based associations and groups that fall outside the realm of the government and business sectors. In Argentina, this definition includes the legal entities association and foundation.

2 NESST uses the term *self-financing* to refer to diverse strategies used by civil society organizations to generate their own revenues, including service fees, sale of products, use of hard or soft assets, membership dues, and investment dividends. NESST uses the term *social enterprise* to refer to self-financing activities that are designed by a CSO to significantly strengthen its financial sustainability and further its mission.



This framework defines whether or not CSOs may engage in self-financing activities and influences the way in which they do so. The tax structure, the level of bureaucracy, and the clarity of existing laws are also factors that have a direct bearing on the development of self-financing activities. Many organizations do not know these rules and believe that they cannot practice self-financing activities or income-generating business activities; others feel that if they do, their reputation or relationship with donors will be adversely affected.

Even when CSOs are aware of the respective legislation, they often do not understand what taxes they need to pay, what forms to file, or what administrative procedures to follow.

The purpose of this guide is to clarify the legal framework for CSOs in Argentina and to assess the degree to which this framework provides an enabling environment for them to pursue self-financing strategies.

1.1 What Is self-financing and why is it important?

Self-financing strategies are used by CSOs to generate revenues in support of their missions. The use of these strategies is a response to the current funding paradigm in which CSOs compete for a limited pie of existing government and philanthropic funding from both national and international sources. This reality makes many CSOs heavily dependent on short-term, project-based funding and prevents them from focusing their attention on long-term, strategic development. Through self-financing, CSOs may be able to increase their long-term viability and independence by generating some of their own resources to supplement support from public and private donors.

Self-financing does not necessarily lead to the commercialization of CSOs. Rather, it can provide these organizations with a greater level of independence and sustainability without compromising their mission purpose or values. Income from self-financing can be one alternative for CSOs to support work that is often more difficult to finance

through traditional sources of funding, such as core operating expenses, new programs, promotional work and others.

NESsT does not believe that self-financing should entirely replace traditional sources of financing, but instead proposes that self-financing can provide a powerful complement to government and philanthropic support. Through self-financing, many CSOs are not only financially strengthened, but also institutionally empowered by their own ability to generate new revenues and to determine the course of their work with fewer constraints from donors.

Furthermore, when pursued in a socially and environmentally responsible manner, the enterprise activities of CSOs can help create an alternative economy more responsive to the needs of local communities, small producers, and low-income people. By purchasing products and services sold by CSOs, consumers are simultaneously promoting their missions and contributing to a more equitable and sustainable world.

Types of self-financing activities include the following:

- **Membership dues:** raising income through dues from members or constituents in exchange for some kind of product, service, or other benefit (for example: a newsletter or magazine for its members or discounts on products or services). If the fee is not paid in exchange for a product or service, it is considered a donation.
- **Fees for services:** capitalizing on some existing skill or expertise of the organization by contracting work to paying clients in the public or private sector (for example, a CSO provides consulting services to businesses or local government agencies).
- **Product sales:** selling, rather than giving away, the products of projects (for example, books or other publications); reselling products (for example, in-kind donations) with a markup; or producing and selling new products (such as T-shirts or mugs).



- **Use of *hard assets*:** renting out real estate, space/facilities, equipment and other assets, when not in use for mission-related activities.
- **Use of *soft assets*:** generating income from patent licenses or other intellectual property, or by endorsing products with the CSO's name or reputation.
- **Investment dividends:** passive investments such as share accounts, savings accounts and mutual funds, or other more active and sophisticated financial transactions: active trading on the stock market or engaging in debt swaps, etc.

As previously mentioned, CSOs engage in self-financing activities primarily to strengthen their financial resources or to advance their social purpose. Some of these may be solely interested in generating profits that they can use to fund core mission programs. In these instances, the organization is not concerned with advancing its social mission directly through self-financing, but rather indirectly by applying the profits earned through this activity to further its social mission. An example of this is a health education organization that starts a printing business and uses the revenues to fund research projects. In this case, the activity would be considered non-mission-related.

Other CSOs may be primarily interested in using a self-financing strategy to advance their social mission. For example, a CSO, whose social mission is to offer carpentry training and job placement to recovering substance abusers, sells the furniture that the trainees produce in order to pay for the costs of the materials and the salaries of the trainees. This activity would be considered mission-related.

These two examples are not mutually exclusive, and neither are the financial and social goals that motivate CSOs engaging in self-financing activities. Many times, CSOs aim to achieve financial and social goals simultaneously through self-financing. A health organization may be better positioned to disseminate the findings from its research by publishing its own materials. Meantime a job training organization may be able

to apply surplus from its furniture sales to fund other programs of the organization or its core operating expenses. In each of these scenarios, the objectives of CSO self-financing activities and the relationship between these activities and the organization's primary mission are fundamental in determining the legal treatment of these activities, as this guide will illustrate.

1.2 Purpose and contents of this guide

In an attempt to diversify their funding base, many Argentine CSOs have already initiated self-financing strategies. For the most part, however, most of these have done so with little expertise, capital, or other forms of support. NESST research on the use of self-financing among CSOs in Latin America in general and in Argentina in particular, demonstrates that many do not have the internal capacity (skills, human resources, adequate financial systems, stakeholder support, business plans) or the external support (financing, consulting support, favorable legal and regulatory environment) to engage in self-financing activities. When such organizations attempt to pursue self-financing strategies, a great deal of stress is put on their staff and indirectly on their other programs and the underlying mission. When a CSO decides to pursue self-financing activities, it is important that it do so with the appropriate levels of technical and financial support and with external conditions that make such activities possible.

The pressures and demands faced by CSOs engaging in self-financing activities in Argentina highlight the need to understand the legal framework affecting them.

In this context, the purpose of this guide is to address the following areas:

1. Outline the key laws, regulations and procedures governing the use of self-financing by CSOs in Argentina. Chapter 3 explains what Argentine law, specifically the National Constitution, the Civil Code and tax law, says about the use of self-financing or *commercial activities* (the most frequently used term in Argentina). It provides



an analysis of the administrative registries and procedures and tax regulations that apply to CSOs engaging in such commercial activities. Chapter 3 also offers a general overview of these laws and regulations, so that Argentine CSOs have a clear idea of where they fit within the legal system and the tax implications of the commercial or social enterprises they operate for self-financing.

2. Assess the relevant laws governing CSO self-financing activities in Argentina, evaluate their practical effects, and identify areas where the law might be improved. The guide identifies the strengths and weaknesses of Argentine legislation: whether they are a help or a hindrance to self-financing, whether they allow for transparent use of self-financing, and whether they foster or hinder the development of the sector as a whole. The legislation is analyzed within a tax treatment typology that makes it easy to understand and assess.

This typology was first developed by the International Center for Not-for-Profit Law (ICNL) to examine the legal treatment of CSO economic and commercial activities in Central and Eastern European countries.³ It has now become a widely accepted typology for understanding and assessing the tax treatments of such activities.

The ICNL typology is presented in Chapter 2; Argentine legislation is analyzed in the context of this typology in Chapter 3; and the criteria presented are used as a basis for the assessments and recommendations offered in Chapter 4.

1.3 Background and methodology

This guide is a component of NESsT's efforts to foster self-financing among CSOs in Central Europe and Latin America. Since 1997, NESsT has conducted applied research on CSO self-financing

in order to identify common challenges and needs. The objectives of the applied research were as follows:

- Assess the current use of self-financing activities among CSOs. NESsT has developed national assessments of CSO self-financing in 9 countries to determine CSO needs and to prepare the capacity-building tools and support for nonprofit organizations seeking to implement or expand their self-financing activities.
- Document success stories and obstacles in self-financing activities among CSOs. NESsT has documented over 100 case studies of CSO self-financing activities to gain insights into their development.
- Examine the legal environment for CSO self-financing in 12 countries,⁴ including the regulatory and tax framework in place at local and national levels that affects these activities.
- Disseminate lessons from the research – by organizing conferences, seminars, and workshops – to stakeholders from all sectors in an effort to develop strategies for assisting CSOs in the use of self-financing.

The research methodology for this guide was developed by NESsT to assess the legal framework for CSO self-financing activities in a given country. This methodology strives to help answer the following core concerns and questions:

1. *What the law states.* What is the current legal treatment of CSO self-financing activities, including current legislation, legal provisions, history of the law, revisions of the law, regulatory approach, tax rates, reporting requirements, other laws or regulations, legal cases, and organizations or lawyers providing advice or assistance?

³ ICNL is an international organization whose mission is to facilitate and support the development of civil society and the freedom of association on a global basis. ICNL, in cooperation with other international, national, and local organizations, provides technical assistance for the creation and improvement of laws and regulatory systems that permit, encourage, and regulate the not-for-profit, non-governmental sector in several countries around the world. ICNL maintains a documentation center for laws, regulations,

self-regulatory materials, and other relevant documents; provides training and education; and conducts research relevant to strengthening and improving laws affecting the NGO sector. For more information on ICNL, see www.icnl.org.

⁴ The countries in Latin America and Central Europe where NESsT has analyzed the legal and regulatory framework for CSOs are: Argentina, Chile, Colombia, Croatia, Czech Republic, Ecuador, Hungary, Peru, Romania, Slovakia, Slovenia, and the Ukraine.



2. *How is the law understood?* Are the regulations of CSO self-financing activities understood by CSOs?

3. *Effects of the law.* What is the effect of current regulations on CSO self-financing activities?

4. *Recommendations for the law.* What are the most important recommendations for addressing current regulatory problems?

Research was carried out with the help of Isabel Friz, an accountant specializing in nonprofit organizations and highly experienced in the analysis of the legal tax framework of CSOs, who collaborated with NESST through a questionnaire surveying the legal tax framework; and Dr. Guillermo Canova, attorney and professor, who shared his knowledge of the legal tax framework for CSOs, including that concerning commercial activities. Dr. Canova also provided feedback on the Spanish version of this guide.

Isabel Friz provided survey responses based on her own knowledge of tax legislation in Argentina and her firsthand experience of tax advisory and consulting services to organizations. She also took into account research and papers she has developed on the issue, including *“The Regulatory Framework for Civil Society Organizations in South America”* (*Marco Regulatorio de las Organizaciones de la Sociedad Civil en Sudamérica*) compiled and edited by ICNL in 1997.

To illustrate the legal framework developed in chapters 3 and 4, two case studies are included in chapter 4 to provide an in-depth understanding of the experience of CSOs in this area. The organizations selected were El Ceibal Asociación Civil and AEDROS, la Asociación de Ejecutivos en Desarrollo de Recursos para Organizaciones Sociales de Argentina.





A Typology for Assessing the Legal and Regulatory Framework



This chapter presents a typology for analyzing the regulations that govern CSO self-financing activities. The typology was developed by ICNL,⁵ and NESsT has expanded and modified it to make it more applicable to the Argentine legal system. The following section presents four key areas that are vital for understanding the legal structure for CSO self-financing before assessing the specifics of Argentina: 1) legal characteristics of CSOs; 2) the legal definition of self-financing; 3) criteria for permitting self-financing; and 4) taxation of self-financing activities.

In its texts, ICNL uses the term *nonprofit organizations* (NPOs) or *NGOs* which refers to a subgroup of the broader classification of *CSOs*, the term used by NESsT. This guide uses the term *CSO*, except in parts that specifically draw upon the ICNL typology, where it maintains the original ICNL terminology.

The broad scope of organizations encompassed by the term *CSO* is consistent with existing Argentine law in the Civil Code for nonprofit legal entities: association and foundation.

5 The overall typology presented in this chapter was adapted, with permission, from the paper *Regulating Economic Activities of Not-for-Profit Organizations that was first prepared by ICNL for the Regulating Civil Society* Conference in Budapest, Hungary,

in May 1996 (copyright ICNL, 1997) and from the Handbook on Good Practices Relating to Non-Governmental Organizations, Appendix I: Economic Activities and Taxation (copyright ICNL, 2000).



2.1 Legal characteristics of nonprofit organizations

The characteristics listed below illustrate the key differences between nonprofit and for-profit organizations and provide a context for understanding how nonprofit organizations (NPOs) engage in self-financing activities. The discussion that evolves in this chapter and the rest of the guide addresses a subgroup of all NPOs: those whose philanthropic purposes are intended to promote public benefit. There is no agreed-upon definition of what constitutes public benefit, which is why most of Chapters 3 and 4 address this issue in terms of Argentine law.

It is important to recognize that some NPOs such as cooperatives, mutual benefit societies, social work organizations and labor unions are also considered to be NPOs and in general the regulatory norms for associations and foundations apply to them, although they are usually governed by a separate set of laws and regulatory bodies. Therefore, they are not included in this study.

Organizations are considered NPOs as long as their objective is to provide a public benefit and uphold the principle of non-distribution.

ICNL, however, does make this distinction between NPOs, and its typology accordingly identifies two basic legal assumptions that distinguish public benefit NPOs from for-profit entities:

1. Non-distribution constraint. Although NPOs are not prohibited from generating profits, these profits may not be distributed to private parties who might be in a position to control them for personal gain: such as founders, members, officers, directors, agents, employees, or any related party.

2. Public benefit as objective. By definition, this class of NPO is organized and operated primarily to provide a public benefit. These characteristics are not dependent on the particular legal form of the NPO. Accordingly, this discussion addresses

NPOs of various legal forms as long as they provide a public benefit and uphold the principle of non-distribution (nonprofit purpose).

From a legal perspective, the main terms established by Argentina's Civil Code for private, nonprofit legal entities are civil association and foundation. However, the provisions and concepts included in the Civil Code are quite general and have proven to be inadequate in the face of the complex reality and multifaceted dynamics of civil associations. As a result, a wide-ranging set of rules has been generated by jurisprudence from both judicial and administrative authorities, together with a series of resolutions, criteria and background information from official regulatory authorities. Thus, there are non profit organizations that while considered to be civil associations in the broad sense, are referred to in a legal sense using special terms and are subject to their own regulations and regulatory authorities (this includes mutual benefit societies, cooperatives, labor unions and social work organizations) or are subject to dual regulation: by the Inspección General de Justicia as well as their own regulatory body (cooperatives, development organizations, national academies and non-Catholic religious groups). Such organizations are excluded from this report; due to their operations and legislation, they are considered hybrid cases.

2.2 Legal definition of self-financing

There are many terms and definitions, both legal and non-legal, currently in use to describe activities that generate revenues for CSOs (e.g., commercial activity, economic activity, philanthropic enterprise, social enterprise, social-purpose business, earned income, income-generating activity). ICNL uses the term *economic activity* to refer to self-financing activities. ICNL defines economic activities as *regularly pursued trade or business activities*, with the exception of those that have traditionally been excluded (such as ticket sales for cultural events, tuition fees at educational institutions, and patient fees at nonprofit hospitals). NESST, on the other hand, uses the term *self-financing* to



refer to activities that generate revenues for CSOs, including the six types of activities described in the previous chapter.

Argentine civil legislation does not differentiate between commercial activities and other types of income-generating activities for CSOs, as long as these are considered within the objectives defined in their bylaws.

By contrast, within the legal tax framework, distinctions do exist, as will be discussed in greater detail later. Specifically, the Ley de Impuesto a las Ganancias (income tax law) established that foundations that carry out commercial activities are not exempt from income tax.

Note: This guide uses the terms self-financing and commercial/economic activities interchangeably when presenting the ICNL typology.

2.3 Criteria for allowing self-financing

According to ICNL, *a threshold issue is the extent to which NPOs should be permitted to engage in economic or commercial activities without losing their philanthropic status*. When viewed from this standpoint, the question is not whether such activities should be tax-exempt, but under what circumstances they will be permitted at all.

When viewed from this standpoint, the question is not whether such activities should be tax-exempt, but under what circumstances they will be permitted at all.

There is a global debate about whether or not an NPO that engages in commercial activities retains its essential characteristics. The answer is simple: provided the activity is not interpreted as or related to the generation of profit, and this difference remains clearly established, we can assert that NPOs that carry out commercial activities do not lose their quality as NPOs.

There are two typical tests used by governments around the world for determining whether economic activities are *for-profit* or *nonprofit*:

1. Principal-purpose test. The *principal-purpose* test provides one legal model for regulating NPO self-financing. It does not prohibit the use of self-financing activities, but rather emphasizes that the NPO is established and operated primarily for nonprofit purposes and not for private gain. This test implies that self-financing would be for mission-related purposes and would not be the principal activity of the organization. Common examples of principal-purpose tests found in regulatory frameworks of many countries are: that economic activities are not the principal purpose (i.e., the principal activity) of the NPO; that economic activities are complementary (or additional) to the NPOs programs; or that economic activities are related to institutional objectives.

2. Destination-of-income test. Contrary to the principal-purpose test, the destination-of-income test, in its pure form, ignores the economic or commercial nature of the activity in question and focuses exclusively on the purposes for which profits from the activity are used. Under this test, an organization must devote all of its income to its not-for-profit purposes in order to qualify as an NPO. Accordingly, an organization that spends 99% of its time pursuing commercial endeavors, spends 1% of its time undertaking public-benefit activities, and devotes all of its profits to these public-benefit activities could still qualify as an NPO. An example of a destination-of-income test is when the profits from economic activities are used to support the organization's mission purpose and not distributed as earnings.

Under either test, an NPO is permitted to engage in economic activities that further the mission (nonprofit purposes) for which it is organized. It should be noted that governments can — and in some cases do — use a combination of conditions under the principal-purpose test and destination-of-income test to determine whether the economic activities of an NPO are permitted. For example, a government can authorize only those commercial activities that are related to the mission of an



NPO (principal-purpose test) and require that the revenues from these be used exclusively for mission-related activities (destination-of-income test).

But what justification is there for governments to permit NPOs to conduct self-financing activities? There are two main public policy rationales for permitting NPOs to engage in such activities:

1. Self-financing applies non-public resources to the public benefit. Income from economic activities is a primary source of funds for NPOs (particularly in emerging market countries, where there is an absence of private capital and philanthropic tradition) and enables them to do their public-benefit work with less dependence on governmental support and charitable donations.

Governments have typically employed four approaches, alone or in combination, to determine the tax treatment for CSO self-financing activities.

2. Self-financing meets public benefit objectives. Certain economic and commercial activities directly accomplish public-benefit purposes. For example, even though the sale of a book on teaching techniques by an educational organization is an economic activity, the distribution of the book directly serves the public-benefit purpose of promoting education. Preventing NPOs from using such commercial and economic means to attain their goals could directly impair their ability to serve public-benefit purposes.

2.4 Taxation of self-financing activities

Although the legal treatment of CSO self-financing varies on a practical level from country to country, most have avoided going to extremes (i.e., a complete prohibition on economic activities or, conversely, allowing economic activities to be the

principal activity of the organization). However, the important issue is the tax treatment of such activities. Governments have typically employed four approaches, alone or in combination, to determine the tax treatment for CSO self-financing activities.

1. Blanket tax. A *blanket tax* policy is applied to income from all economic activities, regardless of the source or destination of the income. Under this approach, the organization is not limited by the level or type of activity, but is taxed on all revenues generated by these activities regardless of how the revenues are used.

2. Destination-of-income tax. A *destination-of-income tax* policy exempts income from economic activities that is used for public-benefit purposes. Under this approach, the organization is not limited by the level or type of economic activity, but is taxed on all income that is not used to further its public-benefit purposes.⁶

3. Source-of-income tax. A *source-of-income tax* policy focuses on the source of the income, granting a tax exemption only when the income is generated by activities that are related to the public-benefit purposes of the organization. Under this approach, the organization is taxed for all income generated from non-mission-related activity even if the income is used to support mission-related programs.

4. Mechanical tax. A *mechanical tax* policy is applied to determine the difference between economic activities that are taxed and those that are not; or it may establish an exemption ceiling (a maximum profit level). Income levels are determined whereby levels below the ceiling are tax-exempt and above it are taxable.

Some governments have created hybrid tax policies that are based on one, two or more of these approaches. For example, it is possible to allow net income from economic activity to be

⁶ The destination-of-income tax should not be confused with the destination-of-income test. The test is used to establish that CSOs may conduct economic activities without compromising their nonprofit legal status as long as any revenues are destined

to the organization's mission. The destination-of-income tax, on the other hand, focused purely on the tax treatment of nonprofit organizations.



tax-exempt below a specified threshold and to apply a mission-relatedness mechanical test to determine whether net income above that threshold should be taxed.

The following chapter analyzes the legal framework in Argentina and the criteria that apply to taxes for NPOs. These criteria indicate that in order to qualify as NPOs, CSOs must put all their profits toward nonprofit purposes. With regard to income tax, all associations and foundations may request exemption from this tax if they are constituted as legal entities. This makes them exempt from paying value added tax (VAT). Exemption is limited for foundations with commercial activities but not for associations, which may carry out such activities without risking their exempt status but must declare the VAT when the commercial activity is something other than selling a service or product which is exempt from VAT.

There is no consensus on which of these tax approaches is best, since each entails certain benefits and costs and defines a different public policy objective. NESST uses four of the ICNL criteria to shed light on the practical implications of each approach.

1. Simplicity or complexity of administration.

Blanket taxation of all economic activity is the simplest approach to administer. Once economic activities are defined, NPOs are treated the same way as for-profit organizations. The *destination-of-income* rule is slightly more complex to administer. The main difficulty is establishing and enforcing criteria for what constitutes expenditure to support public-benefit purposes. This requires monitoring of the CSOs and how they use their income. This political function can be difficult to administer. Moreover, this approach creates a greater potential for abuse by unscrupulous individuals seeking to use NPOs as vehicles for tax evasion.

A *mission-relatedness* test is the most complicated to apply because it is difficult to specify the necessary connection between the economic activity and the public-benefit purpose. However, this test tends to work best when developed over time through administrative practice. This *mission-relatedness* approach is also the most likely to keep NPOs focused on economic activities that also provide public benefit.

2. Effects on revenue collection. Assuming the tax rates under the various treatments are equal, the greatest tax revenue is generated under the blanket taxation approach, since it subjects the largest number of NPO self-financing activities to

taxation. However, it is empirically unclear how much tax would in fact be collected, because, all things being equal, the level of commercial activities by NPOs will presumably be lower under this rule than under the others (because taxation provides a disincentive for CSOs to initiate commercial activities).



In its purest form, the *destination-of-income* rule has the lowest potential to produce tax revenue because all income, regardless of the source, is free from taxation if it is applied toward public-benefit purposes. In practice, many countries impose limits on the amount of income that is exempt under the *destination-of-income* rule, thereby limiting potential losses to the state's revenue base. The *mission-relatedness* test also potentially reduces the size of the tax base, but probably less so than the "destination-of-income" test, because it only provides tax benefits for mission-related activities. However the mission criteria brings an additional benefit: it channels NPO economic activity into specific areas that produce public benefit.



3. Effects on the commercial sector. The *blanket taxation* approach to NPO income from economic activities is most favorable for the commercial sector, since there is no possibility of *unfair* or prejudicial competition (i.e., NPOs do not receive preferential tax treatment when compared to for-profit entities). The *destination-of-income* rule does not create any mechanism to prevent complaints about unfair competition. The use NPOs make of their income could give them an advantage over their for-profit competitors. However, a limit on this benefit reduces the comparative advantage for NPOs. The *mission-relatedness* test minimizes unfair competition by encouraging NPOs to focus on activities that produce a public benefit and by applying the standard tax treatment used for for-profit enterprises when NPO activities are conducted purely for profit. The difficulty in implementing this *mission-relatedness* rule lies in establishing which economic activities advance the public benefit and which do not (or which do not advance it enough).

channels NPO economic activities into more socially beneficial directions than the *destination-of-income* test, which encourages NPOs to engage in economic activities that can earn the greatest potential financial return but not necessarily the greatest social return.

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4. Effects on the development of the NPO sector. The *blanket taxation* approach reduces resources for the nonprofit sector, essentially transferring money from NPOs to the public sector. It is generally accepted that NPOs devoted to public-benefit purposes, if not eligible for state subsidies, should at the very least not be required to transfer resources to the state (in the same fashion as for-profit enterprises). Blanket taxation of all NPO income from economic activities eliminates the incentive to engage in income-generating, public-benefit activities and is the least favorable to the nonprofit sector. NPO proponents claim that such taxes should be at a lower, more preferential rate than taxes for for-profit enterprises.

The *destination-of-income* rule provides the greatest potential revenue to NPOs, since virtually any income can be made tax-exempt if channeled into public-benefit activities. The *mission-relatedness* test is less favorable to NPOs because activities that are undertaken purely to obtain revenue enjoy no tax exemption. However, the *mission-relatedness* test still provides significant tax benefits for NPOs, particularly when they focus on activities associated with public-benefit purposes. Moreover, this approach



The Legal and Regulatory Framework of Argentina



This chapter analyzes the legal framework that governs CSO commercial activities in Argentina. No specific legislation exists for CSOs; rather, they are primarily governed by the Civil Code. The legislation does not favor the implementation of social enterprises or self-financing activities in general; on the contrary, it restricts them, defining the conditions under which an organization can lose its income tax exemption.

Generally speaking, the Civil Code is flexible as far as regulation of CSOs is concerned: in practice, the provisions are interpreted on a case-by-case basis by administrative and judicial judges. A certain logic is applied whereby it is not the means by which the CSOs obtain resources that determines their for-profit or not-for-profit status, but rather the end use or social purpose to which these resources are applicable.

Currently, there are no bills that seek to revoke the restrictions or to promote rules aimed at granting greater tax exemptions to this type of entity or acknowledging this benefit in practice.



For CSOs to fulfill their role as a voice for marginalized communities and to contribute to resolving the country's most pressing problems, it is important that they be strengthened and self-sustaining over time. A sustainability strategy consists of finding mechanisms for an organization to generate its own resources through self-financing activities, lessening their dependence on donations, while at the same time strengthening their social mission.

Below is a guide to the formal process these organizations must follow to carry out self-financing activities.

3.1 General regulatory framework governing CSOs

Argentina is a country with a federal state; its legal system is based on the National Constitution, which represents the highest authority on national laws and regulations on different subjects. These laws can be organized in different codes that are enacted at national level, for example, the Penal Code, Commercial Code, Civil Code, among others. Moreover, provinces also have their own constitutions, always respecting the principles, rights and guarantees established in the National Constitution, but also dictating laws that are specific to their own jurisdictions.

Within this legal system, first there are general rules and regulations from the National Constitution (constitutional regulations) and the Civil Code (civil legislation). Then there are laws that regulate different types of organizations at a national level, which can be inserted into the Civil Code as complementary laws – such as the case of the Law on Foundations, or those that are outside of this regulatory body – as in the case of complementary laws (law 24.240 on consumer protection). Thirdly, there is a group of regulations and rules emanating from comptroller authorities of legal entities and from judicial jurisprudence, such as the resolutions of the Inspección General de Justicia (General Inspectorate of Justice).

This three-level system results in a different set of regulations governing civil society organizations, especially those of associations and foundations.

In Argentina, the terms third sector or social sector organizations, non-profit organizations (NPOs) and non-governmental organizations (NGOs) are used indiscriminately. In the case of NPOs, the term is generally used for differentiating them from for-profit entities, and in the case of NGOs, the term is used to differentiate them from the state.

In 2001, the United Nations (UN) proposed the use of a new concept: civil society organizations (CSOs). This concept turned out to be more inclusive, allowing for a *symbiotic* relationship with the other two sectors while also introducing into the social sector the concept of carrying out for-profit activities, without assuming that it has *profit-making* goals. Beginning with this definition, in this chapter we will analyze the legal framework that governs CSO commercial activities in Argentina.

3.1.1 Constitutional regulations

In the National Constitution (herein referred to as NC), article 14 is the most relevant regulation within the constitutional order that governs the operation of non-profit organizations, as it guarantees the right *to form partnerships with the aim of lucrative gain*.

Other rights protected by the NC related to this subject are: the right to free and democratic assembly, and the principle held by article 19 of the NC which states that everything that is not prohibited is allowed: “as long as the private actions of man do not offend public order or morality or cause harm to others, they are only reserved for God, and are exempt from the authority of the magistrates”. This same principle offers up the possibility that it is not mandatory to request recognition as a legal entity for every group that gathers for selfless purposes. So, for example, there are institutions that, in complying with some formalities, but being without the legal status, are considered subjects of



law, as is the case of simple associations (article 46 of the Civil Code).

Some rights are protected by international treaties that, according to the Argentine constitution, take on constitutional hierarchy: the American Declaration of the Rights and Duties of Man and the Universal Declaration of Human Rights (1948).

Other related articles are:

- Article 14 bis, which guarantees free and democratic labor union organization.
- Article 42 (1994), which focuses on the importance of consumer associations and users of goods and services.
- Article 43, which recognizes that everyone has the ability, from the ombudsman⁷ to the associations, to bring about swift action and expedited protection against any form of discrimination, and on issues regarding the environment, competition, users and consumers, as well as on the rights of the masses in general. This article legitimizes the rights of civil society organizations with certain thematic subjects to submit habeas corpus petitions when any of the above-mentioned rights have been violated.

3.1.2 Civil legislation

The Civil Code, articles 30 to 50, legislates on the existence of for-profit and not-for-profit entities. For further understanding of the subject, extracts of the most relevant articles are presented below:

Article 30: Entities are all those capable of obtaining rights or contracting responsibilities.

Article 31: Entities can be either natural persons or legal entities.

Article 32: All entities capable of acquiring rights or contracting obligations, other than natural persons, are legal entities.

Article 33: Legal entities can be private or public, specifically:

- All national, provincial, and municipal autarkic entities, as well as the Catholic Church are considered public entities.
- Associations and foundations that have public benefit as their main purpose, possess their own patrimony, whose bylaws indicate their capacity to acquire property, do not subsist exclusively on state funding and have obtained proper authorization to operate, are of private character. Likewise, civil and commercial societies or entities that meet legal requirements have the capacity to acquire rights and contract obligations. However they do not require express state authorization for operation, according to Law 17.711.

Article 45: This article acknowledges the existence of corporations, associations, establishments, etc., that are legal entities, as of the day they are authorized by law or by the government, including the approval of their bylaws.

In keeping with the above, Argentine Civil Law indicates that CSOs can take on the legal form of either an association or foundation. The distinctions are explained below.

Civil Association

In broad terms, a civil association is a CSO that stems from the desire of a group of people to achieve a public benefit purpose. It is governed by the provisions of the Civil Code (Article 33, part II, clause 1 and following) and the regulations of the entities that grant legal status in each district (this capacity originates from the provinces and is

⁷ Autarkic and independent institution for the defense and protection of human rights and of all other rights, guarantees and interests protected in the national constitution.



not delegated to the state). In Buenos Aires, the corresponding entity is the Inspección General de Justicia (IGJ) [General Inspectorate of Justice] and in each province there is a corresponding Dirección de Personas Jurídicas (Directorate of Legal Entities). As is the case with foundations, there is no general law that regulates civil associations. Therefore, in order to act as such, they must obtain the authorization as indicated in Article 45 of above-cited code.

The legal nature of the civil association is defined as follows:

- The mission of the association is not fixed and can be changed by a majority vote of its members; and
- the association can have goals that are for charitable, cultural, scientific, research, and athletic purposes, wherein the majority are in the interests of the members.

Foundation

A foundation is a legal entity that is formed after assigning equity to a determined purpose. It is governed by the provisions of the Civil Code and by its own national law, the Law on Foundations (Law No.19.836). Article 1 of this law defines foundations as legal entities that are set up with a public benefit purpose, as a non-profit entity, with assets provided by one or more persons, for the purpose of achieving its goals. To act as such, they must also obtain authorization stipulated in Article 45 of the above-cited code.

Foundations differ from civil associations as defined below:

- The mission is established by the founder in the articles of incorporation and the bylaws; and
- the purpose must be immediate and must contribute directly to general public benefit; in other words, it must be altruistic.

Simple Association

Simple associations, recognized in Articles 46 and 47 of the Civil Code, are institutions that do not have legal status, similar to de facto associations, but unlike these, simple associations are *subject to law*, meaning they have a certain degree of *legal rights*. These associations acquire this status by registering before a notary public (Article 46 CC). This enables them to acquire property, whether or not this can be registered, and to receive donations and bestowals, etc. Members respond together – until the amount contributed – and they are not obliged to take on any social debt if it is not so stipulated in the bylaws (Article 47 CC).

In a broader sense, there are other associations that, although they have the aforementioned characteristics (nonprofit, public benefit purpose, etc.), they also have their own regulations and jurisdictional authority (sometimes dual), including:

- Political parties (Law 23.298).
- Professional associations (Law 23.551).
- Mutual benefit societies (Law 20.321).
- Social work activities formed as civic associations (Law 23.660).
- School districts (Federal Education Law and regulations of each district).
- National academies (Law 14.467).
- Non-Catholic religious groups (National Registry of Religions).
- Development societies (based on each district).

Whether or not mutual benefit societies and cooperatives belong to the CSO sector is a subject under discussion, as they are often considered a hybrid model. Business enterprises exist that have formed cooperatives (occasionally mobilizing significant amounts of capital) and others that actually do meet CSO definitions. For these reasons, they will not be analyzed in this study.



3.1.3 Evolution of the laws for CSOs considering different historical, political, economic and social contexts.

In Argentina, philanthropic actions had their origins in colonial society, mainly through initiatives carried forward by Catholicism (the clergy, religious followers and lay people). At that time, the first public benefit organizations emerged. Christian charity is a public benefit model that has been present throughout the country's history. Diverse papal encyclicals had great influence and direct consequences on local associations: the *Rerum Novarum* encyclical of 1890, for example, inspired the creation of the Workers' Circles in 1892, which carried out the task of religious indoctrination and offered welfare services through mutual action in the areas of health, education and recreation.

A large number of charities developed alongside these initiatives, in association with women from *high society*. The state, on the basis of its relationships, in many cases offered these charities subsidies for social welfare. Furthermore, a growing trend of cooperative and mutual association activities existed during this same period, a trend that grew without state support and with no evidence of cooperation or competition. Immigrants, in order to meet their needs, created cooperatives and mutual benefit societies without help from the state, because they were excluded and sometimes pursued by the state as presumed defenders of anarchism and socialism. These clearly left their impact on the workers.

Nevertheless, although the cooperatives and mutual benefit societies were created in the mid-19th century, their laws emerged at a later date, with the first law for cooperatives appearing in 1926 and the first law for mutual benefit societies in 1946.

Another milestone in the evolution of the sector was the creation of the National Welfare Registry in 1937, in order to regulate organizations that provide assistance and to regulate state subsidies. Later that year, the first Income Tax Law was sanctioned, which established exemptions for all civil entities that did not distribute their equity or profits among their members.

During the interventionist trends of the government of Juan Perón in 1945, a new cooperative relationship was structured between the state and nonprofit organizations, marked by the dissolution of the symbolic Charitable Society, and the separation of the state from Argentine high society charities. As important milestones, both social security and health insurance began to operate in national systems and participants included the state, social work activities, and labor unions.

In the same year (1945), decree 23.852 sanctioned the statutory scheme for professional workers associations, establishing freedom of association, although the status of *labor union* was granted only to the "most representative" unions. Only labor unions with labor union status from that date forward were considered legitimate employee representatives before the state and employers. This new legislation and the new position obtained by labor unions gave way to the rise of new nonprofit institutions, such as welfare and social aid institutions, vacation resorts, food kitchens, clinics, hospitals, production, consumption, credit and housing cooperatives, libraries, technical schools and workshops. Thus many social work activities developed in conjunction with the most important labor unions.

The first law on social work, Law 18.610, was sanctioned in 1970, although Law 14.370 (1954) had previously sanctioned the legal framework for the social security system, establishing a system of distribution and guaranteeing state redistribution.

In 1955, a period of major political instability unfolded and continued until the return to democracy in 1983. In this period, the state issued a series of regulatory initiatives concerning nonprofit organizations:

1955: Law 4.362 reestablished the independence of national academies with respect to the state, defining them as civil associations; in other words, private enterprise organizations.

1964: Law 16.656 exempted civil entities that provide public health services, social welfare activities and education from all national tax.



1968: Law 17.711 modified the Civil Code. From that moment on, within private law entities, Article 33 distinguished commercial societies (for profit) from civil associations and foundations (nonprofit).

1970: Law 18.610 institutionalized a social work system. This law legally established mandatory coverage for all dependent workers. It also established funding for social work activities through mandatory contributions from employers and workers.

1971: Law 19.331 created the Instituto Nacional de Acción Mutual (INAM, National Institute of Mutual Action), a single auditing and development body for mutual benefit societies. Two years later, Law 20.321 for mutual benefit societies was passed.

1972: Law 19.836 was passed for governing foundations, which up until then had no specific regulation. Instead they had been governed by the general provisions of the Civil Code.

1973: the new Law No. 20.337 for Cooperatives was passed. Similar to mutual benefit societies, this law established a single national auditing and development body, the Instituto Nacional de Acción Cooperativa (INAC, the National Institute for Cooperative Action).

1973: the new Law 20.628 on Income Tax was put into effect; clause f of article 20 recognized exemptions for cooperative societies, mutual benefit societies, religious institutions, civil associations and foundations.

In summary, from the late 1960s to the early 1970s, a series of reforms took place and new laws were passed, which permitted the formalization of social initiatives, the creation of governing bodies and the recognition of tax exemptions for the sector. Upon the reestablishment of democracy in 1983, and specifically from the 1990s onwards, a series of economic and political reforms was promoted and the state began to noticeably withdraw from many areas of the economy and social welfare activities, generating the birth of new CSOs to provide solutions for new problems.

3.1.4 Regulations specific to regulatory authorities

The Inspección General de Justicia (IGJ) in the city of Buenos Aires and similar entities in each province govern CSO legality and operations. A CSO must request authorization from these entities in order to function as a nonprofit legal entity.

The legal status granted in each province is recognized nationwide and enables entities to:

- Obtain their Clave Única de Identificación Tributaria (CUIT) (Taxpayer's Sole Identification Number) from AFIP (Public Revenue Agency).
- Manage tax exemptions.
- Limit the responsibility of members and boards.
- Communicate with other institutions.
- Manage and receive donations (from companies, state subsidies, international cooperation).
- Manage an appropriate domain for the creation of their website.
- Formalize their relationship with volunteers.

The IGJ and regional entities regulate CSO operations. CSOs must present an annual report and assessment of activities, current authorities, and updated addresses to verify legal status.

The rapid growth in the number of entities in recent years has meant in practice that this regulation is quite frequently only a formality. According to CENOC (Centro de Entidades de la Comunidad, Center of Community Entities), of the Ministerio de Desarrollo Social (Ministry of Social Development), in 1999 there were only around 80,000 CSOs in the entire country, but by 2005, this number had reached 105,000 (BID/PNUD/GADIS).

The Administración Federal de Ingresos Públicos (AFIP) is the federal government authority (at a



non-provincial level) responsible for tax collection and fiscal control. This entity is responsible for granting legal status to CSOs and after making the corresponding evaluations, it provides them with a certificate of recognition of income tax exemption and their Taxpayer Identification Number (CUIT). AFIP conducts ongoing monitoring of exempt CSOs, appeals the presentation of affidavits, and carries out comprehensive audits (which are currently quite similar to, if not more comprehensive than those required for a private business entity).

Under Article 46 of the Civil Code, simple civil associations are registered in the city of Buenos Aires. Under General Resolution 7/2005, these are not required to establish legal status; however, they face many limitations:

- In practice, this registry is still not in operation.
- Simple civil associations do not have the capacity to pay taxes and therefore cannot obtain exemptions.
- They cannot open a bank account without a CUIT, and therefore cannot receive donations by credit or debit card. Hence, they lose the ability to interact with companies with CSR (corporate social responsibility) units and to obtain tax-deductible donations.
- They cannot hire employees.
- They cannot receive state funds.
- As they do not have legal status, they cannot apply for international aid.
- Without legal status they also cannot create their own website with the *.org* extension granted to nonprofit organizations.

Therefore, in practice, in order for an association to develop its financial resources or commercial activities or to interact with other legal entities, it must formalize its legal status with CUIT and qualify for the corresponding tax exemption. To comply with these legal requirements, it must

incur legal and accounting fees, which can be difficult for many small associations.

3.1.5 Requirements for obtaining legal status as an NPO

The procedures for obtaining authorization for operating as a nonprofit legal entity vary based on the type of organization (association or foundation) and are relatively similar throughout the country. Obtaining this legal status in any jurisdiction authorizes the entity to function in any part of the country. However the regulating body is the entity that originally granted legal status. In the case of Buenos Aires, the corresponding regulations are stipulated in General Resolution No. 7/2005 of the General Inspectorate of Justice (IGJ).

In all cases, an attorney must be retained to draft the bylaws and write a *professional pre-qualifying opinion*. The consulting attorney should be registered with the Colegio Público de Abogados (Public College of Lawyers).

Civil Associations

Article 98 of General Resolution No. 7/2005 defines the following requisites for obtaining legal status:

- Articles of incorporation, containing: place and date of constitution; names of the founders; approval of bylaws; election of officers; and decision to request legal status, authorizing one or more persons to process it.
- Comprehensive and organized text of the bylaws.
- Pre-qualified professional opinion signed by an attorney, whose signature is registered with the Colegio Público de Abogados (Public College of Lawyers).
- Proof of equity through a temporary deposit at Banco de la Nación (most commonly used method to show equity), assets inventory signed by an accountant, or deposit of securities.



- Membership list of the association, indicating position, term of office, marital status, address, and tax identification number of each person.
- List of founding partners and other members, differentiated by categories.
- Document requesting establishment of legal entity.
- Payment of dues for processing legal status, as established by the comptroller agency.

Specifically, article 111 establishes that the bylaws of civil associations may not contain clauses that:

- Require associates to renounce administrative or judicial recourse, in the event that they feel their rights have been affected by any decision made by the associations.
- Imply interference or infringement on the sovereignty of their country of origin, in the case of entities constituted by non-nationals residing in Argentina.
- Impose restrictions on membership or on the rights of Argentine members, whatever their cultural origin may be.
- Limit the rights of Argentine members due to inability to use or express themselves in a foreign language within the entity.

Article 99 determines the following as reasons for refusing legal status:

- The existence, within the entity, of irreconcilable antagonistic elements that threaten the unity of the association.
- The existence of members within the administrative and auditing entities that are undergoing legal or police proceedings, the nature of which implies an inability to perform or remain in their respective functions.
- The stated social objective is directly or indirectly for profit by nature or yields economic benefits for members of the entity.

- The entity proposes to subsist on economic resources exclusively constituted by duties paid for services rendered.

Foundations

As a precondition for granting legal status to foundations, General Resolution No. 7/2005 of the General Inspectorate of Justice (IGJ) requires the presentation of a *Certificate of Good Conduct* for the founders and members of the Governing Council, provided by the Federal Police, as well as a legal background check granted by the National Registry of Recidivism and Criminal Statistics.

These entities may be constituted through a public or private instrument known as the bylaws, which are signed and notarized. This document must be presented to the corresponding administrative authority (in this case the General Inspectorate of Justice or similar provincial entity) in order to obtain authorization to operate.

The Articles of Incorporation must contain the following information regarding the founders:

- For physical persons: their name, age, marital status, nationality, profession, address and ID number and, if appropriate, all of the above for representatives of authorized persons.
- For legal entities: the entity name or designation and address, proof of existence, registration with the Public Registry of Commerce where necessary and information regarding legal representatives.
- Name and address of the foundation.
- Designation of purpose, which must be precise and resolute.
- Initial equity, membership, and future funding, which should be expressed in Argentine currency.
- Founding date of the organization.
- Organization of the board of directors, duration of positions, meeting schedule



and terms/procedures for the appointment of members.

- Clauses regarding entity operations.
- Procedures and processes for amending bylaws.
- Fiscal year-end date.
- Dissolution clauses and procedures related to liquidation and disposition of property.

After the above, the following must be presented to the IGJ:

- Bylaws signed by the founders and duly notarized.
- Signed constitution.
- Pre-qualified professional opinion signed by an attorney, whose signature is registered with the Colegio Público de Abogados (Public College of Lawyers).
- Proof of initial equity.
- Payroll of founders/authorities and information.
- Sworn statement –within the body of the articles of incorporation– which specifies the absence of incompatibilities or disqualifications of the founders in order to form part of the foundation.
- Document requesting establishment of legal entity.
- Professional assessment signed by a public accountant.

Article 9 of the Law on Foundations 19.836 specifies that the foundation must provide plans for

project performance of the entity during the first three years along with a request for granting legal status. This should include a precise definition of the nature and characteristics of the foundation and the activities that will be carried out to meet the performance objectives, as well as the budget required for these activities.

Finally, both foundations and associations must show proof that their initial social equity is at least Ar\$ 200 (US\$ 66) in the case of civil associations and Ar\$ 12,000 (US\$ 3,973) for foundations, or the corresponding amount required at the time of inscription. This proof can be documented by one or a combination of the following, depending on the type of equity.

a) Non-financial assets: through a property inventory, certified by a public accountant, who in turn prepares a report indicating the content of each area of the property and the valuation criterion used, substantiating its source.

b) Sums of money: through a deposit made on behalf of the entity at Banco de la Nación Argentina, which can be withdrawn by its president or authorized representative after being granted authorization to operate as a legal entity.⁸

3.2 Tax framework for CSOs and donations. Regulations on commercial activities⁹

In Argentina, legislation follows a more traditional approach to fundraising for foundations, emphasizing the way in which these entities must apply funds to the public benefit purposes for which they have been created and limiting their options for obtaining resources. Current legislation establishes limits on the tax benefits that should apply to most associations and foundations, and although not explicitly prohibited, there are restrictions on tax deductions on donations from both natural people and companies.

⁸ The information detailed herein can be obtained in Buenos Aires at the offices of IGJ or from its website www.jus.gov.ar. Outside of Buenos Aires, information can be found at the respective regulatory authorities equivalent to the IGJ. Furthermore, there is a good guide that has been developed by the Fundación YPF in which the details of the process are described: FUNDACION YPF. Manual

para constituir o regularizar una OSC: (*Manual for forming and regulating a CSO: Organizing for growth*) [online]: Buenos Aires, Argentina. 2008 [reference date: May 15, 2008]. Available at: www.fundacionypf.org.ar/publicaciones/docs/Brochure_ONG.pdf.

⁹ Guillermo Canova. Speaker. International Symposium on Tax Law. Held in Buenos Aires, August 2000.



The following section explains tax treatment for CSO commercial activities in Argentina.

3.2.1 Income tax law

The Law on Foundations No. 19.836 does not consider commercial activities within the scope of action of civil society organizations, however it does not prohibit them. This law establishes the regulations for reception of donations by charitable entities. In practice, however, many of these types of organizations develop some type of revenue-generating activity, whether through provision of services or the establishment of small enterprises that generate complementary funds. These may or may not be linked to their mission and specific purpose.

Article 20 of the Income Tax Law No. 20.628¹⁰ establishes the types of entities that qualify for income tax exemption, under the condition that these earnings are not under any circumstances distributed among members: “... public benefit associations, foundations, and civil entities, public health entities, as well as charitable, educational, scientific, literary and artistic entities, labor unions, athletic and cultural organizations, only when earnings and equity are reinvested in the purpose for which the organization was created and never distributed, directly or indirectly, among the members.” The law, therefore, does not prohibit the possibility of a charitable entity earning income through commercial activities.

Nevertheless, in 1998, Law 25.063 removed the tax-exempt status from foundations that undertook commercial and/or industrial activities. This situation resulted in many formal complaints from the nonprofit sector, presented to the District Attorney and the Executive Branch, requesting a revision of this law. A proposed reform law was drafted in order to revoke this ruling: “if the resources obtained are not one hundred percent reinvested in their specific purpose and mission”. Unfortunately this bill, although approved in the House of Representatives in October 1999, was never passed by the Senate, and thus it remained inoperative.

Subsequently, on July 29, 1999, Law 25.239 was approved and in article 1, clause e, introduced a reform to clause f of article 20, Law 20.628, by stipulating, in paragraph 2, that this exemption “will not be applicable to foundations and associations or civil entities that are trade associations and carry out commercial and/or industrial activities”.

A literal interpretation of this regulation, in isolation from other regulations and judicial and administrative jurisprudence, would negatively affect many foundations and associations that operate as trade associations and carry out commercial activities in order to meet their objectives as stipulated in their bylaws. In effect, they would become fiscally classified as commercial enterprises with respect to income tax and be taxed 35% on the budgetary surplus obtained from their operations. This would be a total loss of exemption, not only affecting the income generated from commercial activities, but extending to all earnings received by the organization, including donations. This complete loss of tax-exempt status would result in other disadvantages such as:

- Donations from companies would not be tax-deductible for the donor, considering that the law requires the beneficiaries to be tax-exempt entities.
- Loss of tax-exempt status would also mean loss of exemption from value added tax (VAT) for services rendered, even when these are directly related to the objectives of the organization.

Nevertheless, this provision has been interpreted in practice both administratively and legally, in conjunction with article 35 of the Civil Code, which grants CSOs full discretion in acquiring rights and contracting obligations within the scope of their objectives or intended purposes. In other words, the means by which CSOs obtain resources (or manage their equity) does not determine their nature as for profit or not-for-profit; rather, the essential factor here is the final destination of these resources, in other words, the social purpose.

¹⁰ 1997, article 20, clause f.



Both before and after this legal reform, both administrative and judicial jurisprudence have peacefully interpreted this principle (article 35 C.C.) using broad criteria. The IGJ has unequivocally stated that “a foundation can carry out commercial activities without losing its public benefit purpose and non-profit status, if these are used as a means to attain resources for furthering the purpose established in its bylaws.”¹¹

More specifically, in relation to the prohibition on foundations carrying out commercial activities, numerous rulings have interpreted that the qualification of such activities require an analysis of whether the profits were used to further the foundation's purpose: if the response is affirmative, the tax exemption remains intact.¹² On the other hand, tax exemption has been rejected or removed after determining and proving that a profit was sought, generated, and distributed under the guise of a non-profit entity.

Finally, the AFIP, through diverse rulings from its Directorate of Legal Counsel, has upheld a similar interpretation; stating, for example:

- a) “...we must rule out a literal interpretation of the analyzed regulation, considering that the resolute implementation of the stipulations in this new legislation could lead to an interpretation that is detrimental to society, which was clearly not the intention of the legislators when establishing the provision in question”. Later on it states “...when making a teleological interpretation of this rule, it is clear that its intention is to deny exemption to foundations that hide behind the guise of this legal status in order to conduct activities that are purely and exclusively commercial and/or industrial in nature, without any proof that these activities are necessary or contribute to any given social purpose” and it concludes: “....each particular case should be analyzed and formally inspected to determine whether the commer-

cial and/or industrial activity is a means to further the mission or a social purpose in itself of the foundations involved, and only then can its exemption be granted or denied” (cfr. Act N° 588/99, Directive Note N° 778-99); and

- b) “... it is not appropriate to establish guidelines for general interpretation(...) the legislator's intention has been to combat anomalous practices, such as the simulation of a real commercial or industrial activity, through the adoption of a particular legal form, for the purpose of gaining tax exemption” (cfr. Acts No. 283/00 and No. 674/00, Directorate of Legal Counsel, April 5, 2000).

Notwithstanding the foregoing, many organizations representing CSOs and tax law specialists have recommended eliminating the second paragraph added to clause f, article 20 of the Income Tax Law, thereby reverting to the situation prior to the 1999 reform, considering that this specification is not necessary and that if an organization abuses a nonprofit status for profit purposes (whether or not it carries out commercial activities), it is not entitled to tax exemption.

3.2.2 Regarding donations received by CSOs

The Income Tax Law (article 81, clause c) allows contributors to claim donations as tax-deductible, but only when these are made to tax-exempt entities, whose primary purpose or mission falls within any of the following areas: (i) medical aid (non-private sector); (ii) scientific and technological research; (iii) scientific research on economic, political and social issues related to political party development; and (iv) early education and higher education, and degrees bestowed officially by the National Ministry of Culture and Education.

Where applicable, the benefit specifically involves the following:

the foundation, nor having justified any diversion of funds or fraudulent behavior, a rejection of exemption is not fitting with the law...based merely on the fact that the entity conducted financial activity....”

11 Resolution IGJ 597/87 of 9-18-87, Fundación Acindar, N° 4.

12 Cfr., among others, case Fundación Emprender vs. DGI, National Chamber of Appeals in the Federal Administrative Litigation, Room IV, 11-28-00, which determined: “...upon not being able to rule out the social utility of the activity carried out by



- a) The donation is considered to be an expense that is deductible from the taxable base. In practice, the savings consists of the tax rate applied to the donation, which varies based on the different contributor categories (between 6% and 35%).
- b) The deduction can not exceed 5% of the donor's net profits for the fiscal year in which the donation is made.

3.2.3 Law on Value Added Tax (VAT)

Law 23.349 (Law on Value Added Tax) states that services provided by foundations and civil associations included under clause f of article 20 of the Income Tax Law are VAT-exempt if they are directly related to the specific institutional purpose;¹³ otherwise, they are not eligible for tax exemption. This means that only the provision of services is tax-exempt, whereas the sale of goods is not.

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This VAT benefit does not exempt civil associations and foundations from paying tax on purchases; they must pay the tax included in the final price when purchasing from registered entities. The only exempt products for the entities identified in article 20, clause f, of the Income Tax Law are regular natural water, bread, milk without additives, etc. (article 7, clause f of the Law on VAT). Tax is also not applied to the importation of duty-free goods (article 8, clause b). Nevertheless, associations that sell products can request VAT exemption for extraordinary sales, which the Administración Federal de Ingresos Públicos (AFIP) evaluates on a case by case basis. VAT applies to regular product sales much the same as in any private for-profit business, buying and selling with VAT, generating tax credits and debits.

There are, however, certain goods and services that are considered to be VAT-exempt, regardless of the type of entity responsible for the sale. These include: the sale of books, brochures, and similar printed matter; medications for specific treatments; educational services; education for disabled persons; and artistic, scientific, cultural or theatrical shows and gatherings.

3.2.4 Law on Social Volunteerism

Recent years have shown an enormous growth in volunteerism in Argentina. Unfortunately, alongside this, the country witnessed the misuse of Argentine labor law (Ley de Contrato e Trabajo LCT) -which states that all work must be compensated- by volunteers who filed lawsuits against CSOs where they had volunteered, alleging non-transparency and demanding compensation. In most cases the organizations paid a *reimbursement* to volunteers in the form of per diem expenses which consisted of a sum approximating the expenses incurred in doing the job, without requiring that the person show receipts for these expenses. Later, in 1999, 2000 and 2001, several bills were presented to the National Congress which, rather than providing a solution to the problem, merely increased CSO obligations, many of which were impossible to comply with, confusing volunteerism with employee-employer relationships. These bills were naturally rejected by many CSOs. Subsequently, in December 2003, Law No. 25.855 on Social Volunteerism was finally approved by the National Congress and was published on January 8, 2004. It was partially enacted by decree 17/04 and should have been enforced by April 8, 2004; however, as of May 2009, this had still not taken place. The law was only partially enacted because the Executive Branch of government vetoed two articles of the law: one that established compulsory insurance for volunteers and another that required organizations to provide identification for their volunteers.

In brief, the central points of this law are:

- a) A volunteer is considered to be a physical person who undertakes, of his/her free will and at no cost, general tasks in public or private non-profit organizations, whatever their legal status, without receiving remuneration, salary, or any form of monetary compensation whatsoever;
- b) the provision of services by the volunteer is presumed to fall outside the scope of an employment relationship and the social security system;

¹³ Article 7, clause h, part 6, of Law 23.349.



- c) volunteer services should be free by nature, although volunteers may be reimbursed for previously approved expenses;
- d) Volunteers are entitled to:
- Receive information about the goals and activities of the organization;
 - Receive the necessary training in order to undertake the tasks entrusted to them;
 - Be registered (dates they enter and leave the organization);
 - Have a form of identification that accredits their role in the organization;
 - Receive reimbursement for expenses incurred while volunteering, with explicit prior approval from the organization. Under no circumstances shall these reimbursements be considered remuneration.
- e) Volunteers are required to:
- Work with due diligence, accepting the goals and objectives of the organization;
 - Respect the rights of the program beneficiaries;
 - Maintain confidentiality regarding information received if its dissemination infringes on individual rights.
- f) Organizations are required to:
- Sign a Basic Volunteer Agreement with the volunteer prior to his/her start date;
 - Keep track of volunteer start and end dates.

The volunteer status does not change the premise of the Labor Law of Argentina (Ley de Contrato de Trabajo, LCT), (the premise is *iuris tantum* in nature, meaning admits evidence to the contrary), but it incorporates a new tool in relation to the legal recognition of volunteer work, which under certain circumstances can be invoked by labor judges in order to reject possible improper claims.

Although the law has yet to be enforced (May 2009), it has already been invoked in several labor cases, lending legal support to the concept of volunteering. For example, on March 13, 2006 the Superior Court of Justice of the Province of Río Negro filed a ruling in the case of *López, Néstor Javier vs. Radio Luján re. claim re. inapplicability of law* and established that “the presumption of onerosity from article 115 of the LCT is not applicable due to the nonexistence of a work contract under the terms of the cited regulation”. In fact, “it is within this (volunteer) framework where the link between the parties should be established..... as per Law 25.855...”

CSOs in Argentina hope that the enforcement of this law will be as respectful as possible in terms of the uses and practice of volunteerism, and will not create an unnecessary burden for the institutions, as this could hinder the benefits of the solidarity behind volunteerism. They feel it is necessary to find a balance between the spontaneous and natural motivation of volunteers and the need for both parties to have a legal safety net, without the relationship becoming overly bureaucratic, as this would act against the development and promotion of volunteerism, which should be preserved and supported and not surrounded by strict complicated regulations.

3.2.5 Administrative provisions on shareholding

The Argentine legal framework does not prohibit CSOs from owning shares. Nevertheless, General Resolution 7/2004 of the IGJ does impose certain restrictions with respect to the acquisition of shares, be they free of charge or against payment, by foundations constituted in Buenos Aires and/or authorized to function by the General Inspectorate of Justice. The primary considerations center on the fact that shareholding permits the generation of net resources from the moment the investment is made through financial surplus, unless the investment is not essential for other purposes. Shareholding is restricted when it involves tying up assets that are part of the civil entity’s net worth or incompatibility with its main purpose, as this results in the possibility of obligations or responsibilities that would be better not to incur. Although



the provisions established by the IGJ foresee foundations that hold shares as the most frequent case, they should also extend to civil associations and, in the case of foreign entities, to their established or anticipated representatives.¹⁴

3.2.6 Level of CSO knowledge regarding regulatory authorities

Many organizations, especially grassroots ones, do not have access to specific legal counsel on this subject; rather they act out of need in the moment and could easily misread information on the subject. The level of information they manage is rather general in nature, mainly focused on the process of formation and development of bylaws to be approved by the IGJ and the AFIP and to ensure compliance with the requirements that enable them to receive donations both nationally and from abroad.

In terms of development of business activities, organizations, especially the smaller ones, in general are unaware of the limitations, advantages and disadvantages of the tax system that regulates business activities for CSOs. As an example of this, many entities that were carrying out business activities before the 1998 reform continued them, unaware of the new tax provisions, and when audited lost their tax exemption. In this same year, RG 1815 went into effect, enforcing the presentation of a sworn declaration of earnings. The result was that 20,000 organizations listed in the AFIP Registry of Exempt Entities were expelled from it due to noncompliance with this obligation.

More information can be found in:

- IGJ on their website (www.jus.gov.ar), at their offices in Buenos Aires, and throughout the country in the respective local entities equivalent to the IGJ.
- The AFIP rulings can be found on their website: www.afip.gov.ar.

- The city of Buenos Aires has a website (www.buenosaires.gov.ar) with information and an advisory board for CSOs.
- Furthermore, Fundación YPF developed a very good guide that details the accounting requirements and procedures to follow, entitled *Manual para constituir o regularizar una OSC: Organizarse para crecer (Manual for forming and regulating a CSO: Organizing for growth)*, available on their website: www.fundacionypf.org.ar.

In all cases, it is advisable to have proper legal counsel and/or tax accounting support, in order to avoid omissions or problems as a result of lack of compliance with the new regulations.

3.2.7 Legislative trends for nonprofit organizations regarding CSO commercial activities

As already seen, there is currently no legislation that favors self-financing. On the contrary, the only law that addresses this subject is a restrictive law: Law 25.239 (article 1, clause e) in 1999, which modifies the Income Tax Law (Law 20.628) by establishing that “foundations and civil associations or entities that are guilds by nature and conduct commercial and/or industrial activities” lose their income tax exemption.

It appears that the purpose of the law is to limit self-financing, because the initial legislative project (1998) included civil associations, mutual benefit societies, cooperatives and foundations; after the legislative process all organizations were exempt from the prohibition except foundations and trade associations.

Nevertheless, the final law is still subject to interpretation based on other legislation and current practice and often left to the discretion of the administrative and judicial judges as well as the regulatory authorities.

Given this ambiguity in the application of the law, it would seem to make more sense to improve and clarify regulations and controls while permitting



all CSOs to engage in self-financing to generate income to support their social program and overhead costs.

3.2.8 Pending changes in the regulations

There are no bills to repeal the prohibition on foundations carrying out self-financing activities, despite the many attempts that have been made in both the legislative and executive branches.

Current minor regulations (IGJ General Resolutions) also limit an organization's possibility of separating its business activity through a separate commercial corporation in which the CSO owns shares (as with Spanish Law).

Organizations, such as Grupo de Fundaciones y Empresas (GDFE), Foro del Sector Social, and other entities that represent CSOs, are promoting legislative changes through different publications and actions. In 2007, for example, the Assembly *Fiscal framework of CSOs: incentives for and obstacles to social investment* took place, which clearly outlined obstacles in current legislation and some alternative solutions.

3.3 Taxes on CSO commercial activities

3.3.1 Income Tax

Income Tax Law 20.268 authorizes income tax collection throughout the country. This taxes business profits and exempts CSOs under certain conditions, according to article 20 of the law. The tax rate for non-exempt CSOs or businesses is 35% of earnings.

The business assets tax (enforced by Law N° 25.063) taxes a company's assets and operates like an advance from the income tax and its rate is 1.0% of the assets. Article 3 exempts CSOs from this tax if they are exempt from paying income tax.

3.3.2 Commercial activities and Value Added Tax (VAT)

As mentioned in point 3.2.3, in 1997, in the text of Law 23.349 on Value Added Tax (VAT), article 7, clause h, section 6, establishes that services provided by foundations and civil associations included in clause f, article 20 of the Income Tax Law are exempt from VAT if they are directly related to the specific institutional purpose. In other words, the exemption is exclusively applied to the provision of services and not to the sale of goods. If an organization loses its income tax exemption, this benefit is also lost. Therefore, foundations with self-financing activities will lose the income tax exemption and VAT exemption along with it.

Value Added Tax is collected throughout the country. The VAT-exempt benefit for foundations and civil associations does not exempt them from paying sales tax, which is applied to the final purchase price. The only purchases that are VAT-exempt for entities with exemption from this tax are water, bread, milk with no additives, etc. The exemption extends to the importation of duty-free merchandise, whose final destination is for medical work or scientific or technological research. The VAT rate taxes the purchases and sales of goods and services of both companies and physical persons and exempts CSOs under the previously defined conditions. The rate for goods and services is 21%, with the exception of some cases in which 10.5% is credited for the purchase of goods for use in providing medical services to prepaid entities. This guide does not enter into detail on these rates, since they are not the focus of this study.¹⁵

3.3.3 Other taxes

Taxes on credits and debits

Law N° 25.453 established the tax on credits and debits on bank accounts and other operations, fixing a rate of 0.6% for all movements of funds, be

¹⁵ The general aliquota (applicable rate) in the payment of public services is 21%. According to the Law on VAT No. 23.349, in the case of gas, electricity, meter-regulated water and other provisions covered in points 4, 5, 6 of clause e of article 3, it increases

to 27% for those small taxpayers or responsible registrants, when a service is provided in a place that is not exclusively destined for housing, including for nonprofit entities.



they personal or of third parties, even in cash, that anyone, including those covered by the Law on Financial Entities, carries out on their own account and/or on an account in the name of others, whatever the mechanism used to carry them out, the denominations that are authorized and their legal instrument, including those destined for accreditation in favor of establishments supporting the systems of credit and/or debit cards.

Tax exemption is granted in the following cases:

- a) Credits and debits to bank accounts, as well as in the operations and movement of funds, corresponding to national states, provinces, municipalities and to the Government of the city of Buenos Aires, and the National Institute of Social Services for Retired and Pensioned Persons. Those entities (belonging to the national state) mentioned in article 1 of Law N° 22.016 are excluded.
- b) Credits and debits to bank accounts corresponding to diplomatic missions and foreign consuls accredited in the Republic of Argentina, on condition of reciprocity.
- c) Credits to savings or checking accounts, up to the accredited sum for employee salaries or of retirement and pensions, and debits to these accounts up to the same amount.

In 2001, faced with countless demands from CSOs with complaints about this tax, the Government decided to reduce the tax rate for operations carried out by income tax-exempt entities. In order to qualify for this reduction, CSOs must present a letter to the bank where they have their bank account and request the established reduction: they are then taxed at a lower rate of 0.25% for all transfer of funds.

Internal Revenue: the sale of alcohol, tobacco and luxury products are taxed; however these are not especially applicable to CSOs. The rate is variable and all consumers, whether individuals or legal entities are liable; there are no exemptions in this case.

Local Taxes: various types of local taxes exist that can affect CSOs, namely:

- **Tax on gross income:** this depends on the physical jurisdiction. In Buenos Aires (according to article 126 clause 7, of the Text of the Fiscal Code 2002) all income from operations carried out by foundations, associations, entities or charitable commissions, for public benefit, social welfare, education and instruction, artistic, cultural and athletic activities, are taxed at a rate of *zero*. This applies to all nonprofit entities, when the income obtained is used exclusively for the purpose outlined in its bylaws and is not distributed amongst its members, and when the organizations have the corresponding legal status or authorization. The general taxation rate for those that are not exempt is 3% on gross sales.

In all other jurisdictions of the country, CSOs are exempt if they are exempt from income tax. In the province of Buenos Aires, this tax exemption is limited to commercial activities up to the sum of Ar\$180,000 (US\$59,584) of annual revenue.

- **Tax stamps:** these are taxes on activities, contracts and operations that are onerous in nature, formalized in the jurisdiction in which the person or entity resides, through signed public or private instruments that express the purpose of the parties. These taxes are different in each province. There are no exemptions to this tax for CSOs, except for the purchase of property.

These taxes include for example car licenses, street lighting, street cleaning, and other local taxes. Unless a general exemption exists – which is not very common– CSOs are liable to the same rates and municipal contributions as businesses or individuals. The method of calculation varies according to the type of tax: in the case of automobile licenses, this is a percentage of the value of the car. Street cleaning and lighting is calculated by applying a formula that considers the price of



land plus the added value of buildings, then this total is multiplied using a coefficient which varies according to the area.

- **Employment Contributions:** these relate to *social contributions* or social security payments, where there is no different treatment between CSOs and private, for-profit enterprises. Employment contributions are paid by the employer and by the employee. This tax is based on the employee's salary and the retirement and pension system, family allowances, national employment fund, social work activities, wherein the total percentages are: 32% paid by the employer and 17% by the employee.

Using the same criteria, they also make other contributions for labor-specific issues: contributions to workers' compensation, labor union contributions, life insurance, etc.

3.4 Process for tax declaration and other legal reports

The following pages detail the regulations and procedures for registering information that applies to CSOs that develop some kind of business activity.

3.4.1 Fiscal control of the destination of funds

The entity responsible for preventing the direct or indirect distribution of profits among members of CSOs is AFIP.

This entity has permanent power to control and audit. Each time it grants an exemption for a period of time (usually a year) and prior to renewing it, it audits the entity again. Furthermore, the president of the board must upload sworn statements and information about the board to AFIP's online service using a password, as well as the income tax application form for for-profit entities, which requests information regarding bank accounts, CBU banks, accounts abroad, investments, CUIT numbers of suppliers, CUIT numbers of donors and recipients, and other information about the financial balance sheet.

Furthermore, the IGJ and the equivalent bodies in each province annually review the balance sheets presented by each CSO. Each CSO is required to present financial statements such as the Equity Statement or General Balance Sheet, Resources and Expenditure Statement, State of Equity Evolution and Cash Flow Statement. The IGJ will require a comparative presentation of the financial statements, with the financials from the previous year, when total assets or all the resources exceed Ar\$ 1,000,000 (US\$ 331,024) for associations and Ar\$ 500,000 (US\$ 165,509) for foundations.

The following reports must be presented in person to the IGJ each year:

For Civil Associations:

A. Documentation prior to the meeting (to be presented 15 working days before the meeting date):

1. Form 2 stamped. The reverse side must include the list of active authorities as well as personal information.
2. Copy of the minutes of the meeting of the administrative body in which the financial statements and annual report were approved, and in which the annual meeting was convened, signed by the president and secretary.
3. An original copy of the financial statements, signed by the legal representative, by the fiscal entity and the public accountant. This should also include the auditor's report and opinion, along with his/her signature legalized by the respective professional council.
4. A copy of the annual report signed by the president and secretary, as well as the annual inventory certified by a public accountant and signed by the legal representative and fiscal entity (Art. 381 RG IGJ 7/2005).
5. Accreditation of the advertising medium for the official announcement of the assembly or annual meeting, as outlined in the provisions of the bylaws, or alternatively, by means of a circular to the members.



6. A copy of the fiscal entity's report with original signatures of its members (in cases of civil associations).

B. Documentation following the annual meeting (to be presented within 15 working days after its occurrence):

1. Form 2 (which does not need to be stamped). The reverse side must include the list of active authorities as well as personal information.
2. Accreditation of the advertising medium as laid down in the bylaws for the official announcement of the meeting for the Administrative Council or the Commission Directive.
3. A copy of the minutes of the assembly or annual meeting in which the financial statements and annual report were approved. Proof that supports the attendance of associates or members of the Administrative Council, signed by the president and the secretary.
4. A new copy of the financial statements, if these have been modified at the assembly or annual meeting.
5. A copy of the annual report signed by the legal representative and secretary, if it has been modified.

Foundations should only present information subsequent to the annual meeting, gathering together all of the documentation (financial statements, annual report, inventory) along with a stamped form.

3.4.2 Process for tax declaration and other legal reports

Civil associations and foundations, despite being nonprofit organizations, in accordance with the current regulations (RG 1815, AFIP), must present the same income tax statement as any for-profit commercial company. The form, requirements, and information are the same. The only difference is that they state their status as an exempt entity at the beginning, regardless of whether they under-

take business activities, as the information required is the same.

Exempt entities must declare all donations received and awarded. The requirements create a heavy burden for the organizations, as the form is awkward and complex even for an expert professional accountant and it must be presented online with a *fiscal password*, which is obtained at the corresponding AFIP office, which is the exact same procedure as for commercial companies.

This sworn income tax statement must be presented to the AFIP. The timeframe for its presentation is within the first days of the fifth month subsequent to the close of the fiscal year (the same applies to companies). For example, if the close of the fiscal year is December 31, 2007, the sworn income tax statement is due by May 7, 2008.

The specific regulation for CSOs is General Resolution 992 (RG 992) regarding compliance and formal timeframes, which also applies to commercial companies. If for any reason an organization does not present its sworn income tax statement via the Internet with the fiscal password, the AFIP can suspend its exempt status (article RG 1815) until all pending presentations are in order.

In addition to the sworn income tax statements, organizations must comply with other obligations. Although they are not subject to fiscal interest, since they do not pay taxes, they are responsible for:

1. Withholding tax obligations (when making payments to suppliers, employees, etc):
 - As per General Resolution (RG) 830: regarding fees, rentals and others.
 - As per RG. 739: regarding beneficiaries from abroad.
 - As per RG. 4139: regarding salaries.
2. Information obligations:
 - As per RG 992: Organizations must provide information through a sworn income tax



statement (as previously explained) for each individual donation received, itemized with the CUIT number, amount, type, date of bank deposit, etc.

- As per RG 4120: Organizations must provide a description of the governing body as of December 31 of each year.
- As per RG 992: The certification of tax accounting books, form 760/c, which must be completed and signed by a registered public accountant whose signature is certified with the Professional Council of Economic Science.

3.4.3 CSO accounting

As with private for-profit businesses, CSO must keep accounting books, accounting records, and balance sheets (these should also be signed by an accountant).

In this sense, the law is the same for all CSOs, whether or not they engage in self-financing. Nevertheless, there is one difference for CSOs with respect to VAT. If the CSO buys and sells goods, they should register for this tax, have a book for *VAT purchases* and another for *VAT sales*, and calculate VAT in order to make monthly deposits and present the relevant documents from the AFIP in the SIAP.¹⁶ All taxes are presented on AFIP forms, which can be found on the internet.

All CSOs must maintain the following mandatory books:

Book of records: This book should include minutes relating to advisory council or board meetings, annual meetings, and ordinary and extraordinary general meetings. The following should be recorded: place, date, time of meeting, nature of meeting, first name and last name of attendees, agenda, items discussed, decisions made and resolutions made. If the association has a separate book for recording attendance for annual meetings, the names of the attendees can be omitted,

making reference to the data in this record. The articles of incorporation and bylaws should be transcribed in this book and signed by all constituents.

Balance sheets: This must include the details and valuation of an organization's assets from the moment it obtained legal status, as well as a transcription of financial statements, the annual report, and an precise and complete description of its assets and liabilities during the corresponding fiscal year.

Journal: This journal registers all income and expenditures, indicating each payment and receipt, detailing the proof of payment or document supporting each movement.

Book of associates (in the case of civil associations): This is a list of members, along with the category to which each belongs (based on bylaw classifications), date of admission, dues paid, suspensions imposed on the exercise of their social rights, and date of retirement or cessation of activities, indicating cause of the latter.

The CSOs that are covered in article 20 clause f of Law 20.628 (Income Tax Law) are required to issue receipts and register their operations in the manner in which AFIP stipulates in RG 1415.

3.5 Background required for launching commercial activities and existing sources of information

The significant legal, accounting, and tax obstacles to CSOs setting up social enterprises, when coupled with their limited experience in managing them, results in a growing demand for technical support in finance, law (especially tax law) and accounting.

Often CSOs lack the economic means to pay for specialized assistance to help them meet the requirements. In addition, there are currently not enough accounting and legal specialists in these

¹⁶ The SIAP is a system designed for AFIP, where general information about contributors is entered and which serves as a base for

generating sworn statements that those responsible must present for different types of taxes.



areas. Consequently, it is extremely important to make this information accessible to CSOs so they can start up, strengthen and increase their self-financing mechanisms without losing their tax exemption and without exacerbating the workload to the point that it negatively affects the organization's ability to carry out its work.

The following is a list of institutions - which is illustrative rather than exhaustive – that provide support to CSOs in Argentina. While these do not all provide services specifically related to commercial activities, their expertise may be useful to CSOs seeking assistance in this area.

Governmental organizations:

Administración Federal de Ingresos Públicos
(AFIP)

www.afip.gov.ar

Centro Nacional de Organizaciones de la
Comunidad (CENOC - national center of
community entities)

www.cenoc.gov.ar

Inspección General de Justicia (IGJ)

www.jus.gov.ar

Nonprofit organizations:

Ashoka Emprendedores Sociales

www.ashoka.org.ar

Foro del Sector Social (social sector forum)

www.forodelsectorsocial.org.ar

Fundación Compromiso

www.compromiso.org

Help Argentina

www.helpargentina.org

NESsT

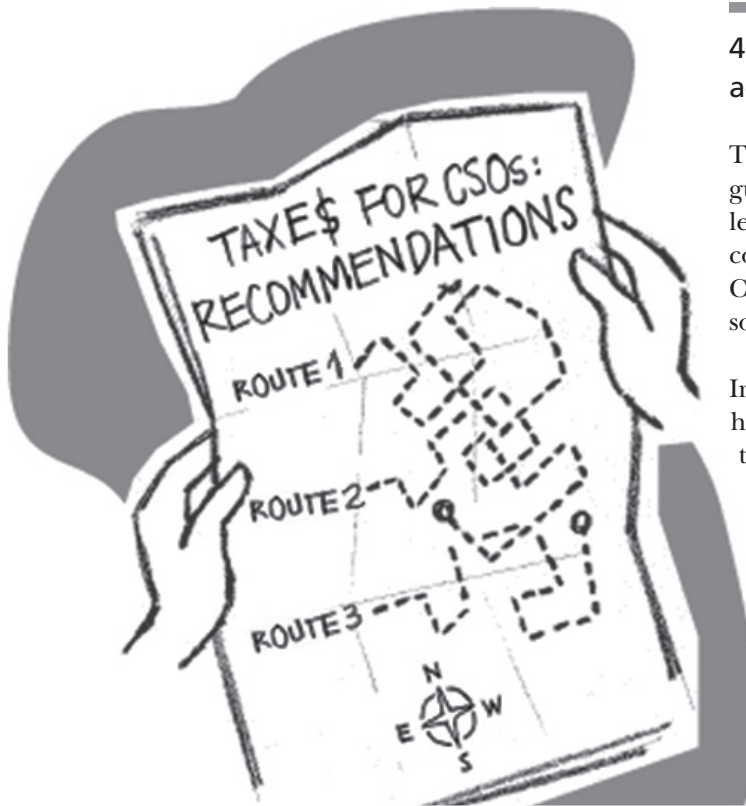
www.nesst.org

Soluciones ONG (NGO solutions)

www.solucionesong.org



Interpreting and Critiquing the Argentine Legal Framework



4.1 Interpreting the legal framework in accordance with ICNL

The information contained in Chapter 3 of this guide, which analyzes the legal and tax legislation, leads to interesting conclusions based on ICNL concepts, which could be of help to Argentine CSOs in developing self-financing activities and social enterprises.

In terms of legislation on self-financing, Argentina has a hybrid model which combines the destination-of-income and principal-purpose criteria.

Current legislation on self-financing activities is blind to the economic or commercial nature of the activity in question and focuses exclusively on the final purpose of the activity's profits (destination-of income test). Under this test, an organization must devote all of its income to its not-for-profit purposes in order to qualify as an NPO. This is the case in Argentina where, based on legislation, associations and foundations can conduct commercial activities provided that the profits are all reinvested in the organizational mission.

However, this is not sufficient; in an organization's registration, it must clarify its objectives in the bylaws. It is at this stage that Argentina



imposes restrictions that are more in line with the principal-purpose test, as the objectives must clearly state that self-financing is for furthering the organization's mission and is not the main activity of the organization. This test provides a legal model for regulating NPO self-financing. It does not prohibit the use of self-financing activities, but rather emphasizes that the NPO is established and operated primarily for nonprofit purposes and not for private gain.

Thus in Argentina an NPO is permitted to engage in economic activities that further the mission (nonprofit purposes) for which it is organized. A combination of conditions under the principal-purpose test and the destination-of-income test should be set up to determine whether the economic activities of an NPO are permitted.

After an analysis of the taxation on self-financing activities in accordance with the ICNL theoretical framework, it is possible to conclude that Argentina applies a combination of the destination-of-income tax and the source-of-income tax together. Thus a destination-of-income tax policy is applied, which exempts income from economic activities that have public-benefit purposes, and at the same time a source-of-income tax policy is applied, that grants a tax exemption only when the income is generated by activities that are related to the public-benefit purposes of the organization. Under this approach, the organization is taxed for all income generated from non-mission-related activity even if the income is used to support mission-related programs.

Argentine legislation was not based on ICNL criteria and therefore any similarity is not necessarily related to the design but to the application of the law. It is important to emphasize that the tax treatment makes exceptions for certain cases and that these are analyzed on a case-by-case basis by the regulatory authorities. It is entirely possible that the legislation will impose greater restrictions than those specified by the ICNL criteria. Furthermore, as we saw in chapter 3, Argentina has created hybrid tax policies, which discriminate based on the type of organization: association or foundation.

4.1.1 Design of the current regulatory framework

As aforementioned, there is almost no legislation specifically relating to CSOs in Argentina: they are principally governed by the Civil Code and in some cases by specific laws, depending on the typology: foundations, mutual benefit societies, cooperatives, charitable affiliations or unions.

Since 1995, legislation has tried to limit income from donations and has prohibited foundations from carrying out commercial or industrial activities under penalty of losing the benefit of tax exemptions. They also have to pay the same taxes as any business corporation, but without any profit option or possible distribution of earnings.

As a result of these restrictions, some institutions have started a process aimed at reforming the fiscal framework regulating nonprofit organizations in Argentina. Among these are the Foro del Sector Social (social sector forum), GADIS, the Universidad de San Andrés, the United Nations Development Program in Argentina and more recently, the Grupo de Fundaciones y Empresas.

This process relies on the participation of social leaders, professionals, officials and academics. Conferences, workshops and research projects have been carried out allowing a consensus to be reached and helping to identify the main areas (conducting legal and administrative tax reforms, offering incentives for social investment, speeding up administrative procedures, eliminating taxes such as processing charges etc.). These issues are now becoming the subject of debate, and reforms aimed at promoting the creation and development of CSOs have been introduced.

Despite the efforts made by various organizations in the sector, singly or in combination, it has thus far been impossible to hold serious debate with government officials and legislators regarding the improvement of the legal and fiscal framework for CSOs. The best solution would be for CSOs, the organizations which bring them together, citizens, employees, legislators, and regulatory agencies to work together in order to achieve a better consensus relating to fostering the development of CSOs.



Methods of screening and controlling by the institutions themselves need to be discussed, but this should be accompanied by a serious policy of incentives for the sector and a reduction in excessive formalities, which particularly affect smaller and institutionally weaker CSOs, which nonetheless do proven and efficient work. The law should seek the development and effective functioning of CSOs as well as the necessary conditions to enable them to be sustainable over time and achieve their founding social purpose.

Unfortunately, progress in reform proposals have so far been lacking as they have met with a great deal of resistance from the policy-makers and their lack of knowledge and understanding with regard to the nature, dimensions, and financing of the CSO sector.

The government, through its Public Revenue Agency (AFIP), views the work of CSOs with suspicion and distrust. There is no plan to introduce incentives for donations within the fiscal framework, and regulations governing controls and penalties of the institutions have intensified over the last few years. The main problem concerns the government's view of the sector as being *fraudulent*. It has shown a keen interest in broadening its tax revenue base while limiting tax exemptions as much as possible, incorporating new checks and restricting authorization of tax exemption certificates submitted by the institutes.

4.1.2 Perception of CSOs regarding self-financing

It seems that the Argentine government still does not recognize the importance or the impact of the activities carried out by CSOs, although to a certain degree it has respected the freedom of association without systematically interfering in private corporate life. Tax law in practice shows the government's serious lack of knowledge of and lack of support for CSOs.

Due to the growth of the sector alongside the regrettable malpractice of various organizations in their use of tax benefits, the government has restricted tax benefits given to CSOs. Although it recognizes them as being tax-exempt organiza-

tions, the government has progressively limited their access to donations, as explained in the Income Tax Law (Article 81, clause c).

Faced with this situation, CSOs started to develop other financing strategies including self-financing, which allowed them to diversify their resources and contribute to the sustainability of their social programs. In 1998 and 1999, however, the government prohibited foundations from carrying out commercial and industrial activities, as has been previously mentioned.

As a result, CSOs currently face the challenges of:

1. Obtaining sources of financing from overseas.
2. Obtaining donations from private parties who do not need tax deductions.
3. Obtaining state subsidies.
4. Engaging in taxable activities as if they were commercial organizations in the case of foundations who have lost their tax exemption or registering for value added tax in the case of associations, charging and billing these transactions with VAT.

As a result of current legislation, many entities are now faced with the dilemma of whether or not to engage in self-financing.

The AFIP currently places special emphasis on whether CSOs are buying and selling products or services or providing paid consulting services. If detected, these commercial activities must be irrefutably proven to be absolutely essential in achieving the social purpose of the CSO and that part of these services are provided pro bono to benefit those who cannot pay for them.

The experience of the accountants consulted shows that audits are extremely exhaustive; in many cases the AFIP applies the concept of *economic reality* and fails to recognize that the money collected is dedicated to just causes with no profit gained. It instead concentrates on the manner in which it is collected rather than how it is spent.



4.2 Implications of the regulatory framework in public administration. A theoretical and rational explication

4.2.1 Simplicity or complexity of administration

Knowledge of and compliance with the tax framework is not a simple task in Argentina and from an administrative perspective is extremely complex. This is particularly evident regarding compliance with formalities associated with tax payment (accounting, completion of tax forms, tax declarations, etc.). On reviewing those requirements expected to be registered with the IGJ, it is evident that organizations need specialized technical consultancy (legal and accounting). The AFIP does not provide special treatment or a simplified system for CSOs. Taking into account the complexity of the Argentine tax system, its use or understanding by many CSOs is almost impossible without the help of accounting specialists.

4.2.2 Effects on tax collection

Tax revenue has increased and improved but there are still wide margins on informal economy. Despite the fact that many sectors feel that taxes are already too high, the AFIP is continuing its efforts to increase tax collection and eliminate tax exemptions and special treatment. Although income tax regulations allow for exemptions on taxable earnings, the procedure is far from simple and in many cases is subject to long delays (months or years). It also must be done on a yearly basis, along with the resulting administrative burden.

4.2.3 Effects on the commercial sector

In general, the business sector does not view CSO self-financing activities as disloyal competition, and therefore maintains good relationships with the CSO sector. Also, CSOs engage in self-financing and social enterprise to further their social purpose and their nonprofit mission: their purpose is to generate an income which allows them to constantly develop their social programs.

In Argentina, CSO self-financing and social enterprise are usually restricted to specialized consultation services or small-scale production and sale of hand-crafted goods, areas in which the business sector has not felt an impact. In addition, the target market is different in the case of provision of services (human rights, environment, support to more disadvantaged sectors, among others).

4.2.4 Effects on the development of the third sector

Government distrust, along with the intensification of regulations for CSOs, and in particular foundations, has limited the development of these organizations mainly in the area of their self-financing activities, which has had a detrimental effect on the development of the sector. As has already been mentioned, foundations have lost their exemption from income tax, VAT, and other taxes. Associations can, however, engage in commercial activities with some VAT restrictions depending on the particular activity. Donations to CSOs from businesses or individuals have also been limited owing to tax burdens established by the new regulations.

Furthermore, the considerable complexity in submitting the information, regardless of the size of the CSO, makes administration in small organizations incredibly complex. Many forms are frequently modified and the regulations imposed by the AFIP and the IGJ are usually very far removed from the activities and daily reality of CSOs.

The AFIP has no specific tax regulations or laws for CSO self-financing and the respective limitations and formalities are extremely complex for CSOs to understand. There are no real incentives for the sector to develop, such as the promotion of legal sources of financing.

This explains the need for a legal regulation on this issue, which is specific to CSOs.



4.3 Limitations of the legal and regulatory framework

There are generally no incentives to promote associative culture and donations in Argentina. Furthermore, there are legal, fiscal, and regulatory obstacles that affect the management capabilities of CSOs, limiting their income and sustainability.

As has been presented in this document, Argentine legislation distinguishes between different types of CSOs, mainly associations and foundations. The only regulations that strictly affect associations, despite their contribution to social development, are those of a general nature in the Civil Code. The legislation regulating these institutions comes from the standards issued by the regulatory authorities and from the case law stemming from the judicial seat or the administrative jurisdiction.

This causes legislative imposition and dispersion, and even a legal vacuum. It also draws attention to the need for a law to regulate this group of entities and not stifle their operations with bureaucratic and unjustified demands.

At the same time, the Argentine tax structure is difficult for taxpayers in general and for CSOs in particular to understand and put into practice. This is added to a policy of limiting tax exemptions, which has been applied by the last few governments and restricts CSOs in their ability to develop business management skills. These organizations have access to neither the capital nor the marketing required to begin self-financing and social enterprise activities. All these conditions inhibit and negatively affect their development.

In summary, the main limitations governing CSOs in Argentina resulting from the legal and regulatory framework are:

- Prohibition on foundations engaging in self-financing activities.

- Complexity of the required tax information, which does not take into account the size of the entity (requirements for small-scale CSOs are the same as those for company foundations or large-budget operations).
- Application of the tax law and control over criteria, which in many cases are subjective and subject to interpretation by the regulatory authorities (AFIP).
- Lack of suitable modern legislation relating to the various sources of financing for CSOs in keeping with legislation in other developing countries.

In order to strengthen civil society, it is essential to quickly adapt the fiscal and legal systems using methods of efficient control –to avoid cases of abuse- while at the same time giving the necessary freedom to promote the development of the sector and allowing it to use its creative talent freely.

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4.4 Case studies that demonstrate important issues within the regulatory framework

Short case studies of two associations have been chosen in order to more closely examine how the legal and regulatory framework plays out within Argentine CSOs. Below is a brief description of each organization and their self-financing activities, followed by a summary of the legal aspects affecting these activities.

4.4.1 Asociación de Ejecutivos en Desarrollo de Recursos para Organizaciones Sociales de Argentina (AEDROS)

The Organization

Established as a civil association in June 2001, the Asociación de Ejecutivos en Desarrollo de Recursos para Organizaciones Sociales de Argentina (AEDROS) provides opportunities for



professional development to people working in nonprofit fundraising, helping to foster leadership qualities within an ethical framework. AEDROS addresses aspects of professions related to resource development for social organizations as well as the responsible practice of philanthropy and volunteerism within Argentina.

Its mission is to promote, encourage and disseminate the importance of and need for the development of human and economic resources for nonprofit organizations and their causes.

Its aims are to: (1) help its members improve their professional performance; (2) encourage networking and establishment of alliances among members; (3) promote ethical standards for professional fundraising; (4) analyze and guide its members through the resolution of common problems.

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Its programs can be grouped as follows:

- **Training:** This is its main activity; its beneficiaries are AEDROS members and any individual interested in helping with CSO financing. Its purpose is to develop capacities in participants which lead to an increased performance in annual fundraising activities.
- **Promotion of ethical standards for professional practice:** This activity establishes criteria and a code of ethics that is signed by all members regarding the development of activities.
- **Promotion of meetings and exchanges between members (networking):** This activity aims to generate mutual learning experiences between those working or planning to work in fundraising.
- **Job searches:** This activity serves as a key point of reference for job vacancies within the sector; its beneficiaries are development professionals as well as organizations.

- **Orientation/training for individuals and organizations in the nonprofit field:** This activity is supplemented with presentations, one-on-one assistance and advice, and exchanges, directly benefiting the sector and society through CSOs.

The AEDROS team consists of two paid full-time staff members, 40 volunteers, and 150 members. Its main self-financing activities include income from training, which amounted to Ar\$ 4,245 (US\$ 1,392) in 2007, as well as membership dues of Ar\$ 23,270 (US\$ 7,630) (monthly membership dues are on average Ar\$ 15 (US\$ 5) per month, depending on the membership type), which together make up 37% of revenue.

Since its creation, the number of members has risen from 40 in 2003 to almost 300 in 2007. The number of training activities has also increased from 2 to 9 per year and two international conferences have also taken place with the support of the Association of Fundraising Professionals in the USA, the Resource Alliance in the UK, and the Argentine Professional Council of Economic Sciences. Within seven years it has become a national and international model for fundraising, consulted by organizations seeking fundraising/development professionals as well as individuals working in the sector.

Self-financing activities

Self-financing at AEDROS was motivated by the experience of the steering committee members themselves (experts in resource development) who envisioned, through training courses and memberships, activities that would strengthen the mission and generate income to increase activities. The organization relied on board financial contributions and in-kind donations to get the office up-and-running and to pay the administrative secretary for the first few months. It also obtained the support of the Universidad de San Andrés, which provided classrooms and equipment during the first two years, and recruited a staff member in charge of



course registration. After bringing a paid staff member on board, AEDROS was able to increase its members from 40 to 200 in two years.

AEDROS designed a self-financing model and began to grow an important membership base, which received substantial benefits for their contributions. It conducted significant training activities, which helped to raise its current funds. A strategy is currently being devised to diversify revenue in order to continue growth. To do this, AEDROS has considered seeking donations from non-donor third parties and sponsors to enable it to broaden its training activities, introduce new courses, and offer courses throughout the country. It hopes to devise a business plan in order to strategically develop current training activities as well as new ones related to its *know-how*.

When designing and starting its self-financing activities, AEDROS' proposed objectives were to cover its overhead and office expenses (the area that donors least want to finance, according to AEDROS), generate funds to cover the costs of other projects and activities, give the organization more visibility, further its mission, and become a more sustainable organization.

The organization's strength lies in the widespread and effective dissemination of its activities, and its strong ties with the Universidad de San Andrés in Argentina, the Association of Fundraising Professionals in the USA, and the Resource Alliance in the UK. Another of its strengths is expressed in its training slogan *Fundraising por los que hacen*, which translates as Fundraising by Fundraisers, as the courses are taught by reputable trainers who have successful careers as fundraisers in the Argentine (and in many cases international) social sector. These courses demonstrate examples of resource development in local and international campaigns.

Self-financing activities have had a major impact on AEDROS' mission and although it has as yet been unable to carry out training activities in the rest of the country, since its conception it has annually held seven training courses with almost 60

participants per course. The cost of the courses is currently Ar\$ 200 (US\$ 66) for members and Ar\$ 250 (US\$ 83) for non-members.

Its biggest weakness, however, is the lack of paid staff members dedicated to fundraising activities, as well as the management of its self-financing activities, which both rely heavily on volunteer efforts from board members.

Challenges of self-financing

The most significant challenge currently facing AEDROS is related to the growth of its activities, as this requires a stronger structure and permanent staff in order to be able to manage its self-financing activities: delivering training days, charging membership dues, promoting better and more widespread dissemination of AEDROS in order to increase the number of members and provide them with better services.

Another challenge involves the ability to carry out training activities in the rest of the country, a request from members in the provinces.

AEDROS has also identified the need to develop a business plan to make its training activities more profitable. In addition to its current preparation of the annual budget planning and a one-day strategic planning session every two years, AEDROS recognizes the need for a long-term organizational plan.

4.4.2 El Ceibal Asociación Civil

The Organization

The mission of El Ceibal Asociación Civil is to implement sustainable development programs, with special emphasis on those that promote the autonomy of individuals and communities with fewer resources, promoting their economic and social development and improving the quantity and quality of the opportunities to which they have access.

The organization was created in 1997 and was run by of a group of young professionals from



both urban (Buenos Aires) and rural sectors who, through church-related activities, worked with rural communities from the province of Santiago del Estero. The founders had a strong commitment to the local rural community, working toward more equitable relations with local stakeholders and developing a base for real social change at a local level. In 2001, they formalized their situation and obtained legal status for the association.

The Association's activities focus on four areas: (1) Support to a Network of Producers in Chaco, (2) La Ruta del Tejido (the textile trail), (3) The Land Use Program, and (4) The Youth Forum, all focusing on community development, human rights and the environment.

In 2003, El Ceibal initiated The Fortalecimiento de la Red de Pequeños y Medianos Productores del Chaco, a program designed to strengthen the network of small and medium-sized producers in the region of Chaco. Its objective is to organize these producers so that they can increase their sales volume targeted at a global market.

The Ruta del Tejido Project was initiated in 2005, bringing together artisans from two provinces -Tucumán and Santiago- with the aim of reviving and increasing the value of textile art. The organization has also created a museum to show different textile techniques, recreating those carried out in the Calchaquí valleys and Santiago del Estero. This project, which continues to this day, has a direct impact on 70 artisans and indirectly affects 250 artisans from both provinces.

At the same time, the organization initiated a project in Land Use aimed at recognizing the land rights of rural communities and helping them to acquire title to their lands. An interdisciplinary team from the institution is conducting, in conjunction with local young people, an assessment of land rights associated with the Dirección General Tierras (DGT) of the province of Santiago del Estero. This directly impacts 1000 families and another 7000 indirectly.

The organization has also created a Youth Forum, drawing on the potential of young people (urban

and rural) who have public concerns about the aforementioned projects. This forum has a direct impact on 350 young people.

El Ceibal currently has 2 full-time and 10 part-time staff members, 7 freelance workers, 10 unpaid volunteers and a 5-member Board of Directors.

With regard to its sources of income, in 2007 it received Ar\$ 232,500 (US\$ 77,500) from international/foreign sources, Ar\$ 49,798 (US\$ 16,600) from public/government sources, Ar\$ 4,680 (US\$ 1,560) from individual sources within Argentina, Ar\$ 700 (US\$ 233) from Argentine companies, and Ar\$ 75,000 (US\$ 25,000) from in-kind donations.

Self-financing activities

Prior to the establishment of its legal entity, in 1999 El Ceibal created a rural micro-credit program with the aim of assisting the development of the local rural community. When it was formally established in 2001, this program was included within El Ceibal Asociación Civil. The idea arose from the experiences of Muhammad Yunus, creator of the Grameen Bank, the bank of the poor in Bangladesh, and as a result of the high demand for credit among in the rural sector with whom El Ceibal was working.

The high demand for the program led to the establishment of two branches in Buenos Aires, and eventually to the decision to set up the program independently. For a year, the founders of El Ceibal analyzed the best format for the company to take and finally established it as FIS S.A. in September, 2005, i.e. a limited company. It operates a social investment fund (FIS Fondo de Inversión Social) managed by an economist, Juan José Ochoa, Julián Costabile (both founding members of El Ceibal AC), and Patricio Boyd, a political expert who had worked with the Grameen Foundation in Buenos Aires. More than 100 Argentine individuals and two entities (one of them being El Ceibal Association) currently invest in this fund. It currently receives Ar\$ 55,800 (US\$ 18,600) from the investment fund, solely from the interest generated from its investment, and it has 4,207 active loans (beneficiaries).



El Ceibal carries out another self-financing activity through the Land Use Program. It provides services to the provincial and national government and rural organizations for helping rural communities register and obtain title to the land where they live. El Ceibal had set up a sustainable community development program to help the rural inhabitants of unclaimed land establish land ownership. The work started in 2004 with a pilot project that was 50% funded by the AVINA Foundation. In 2005, the organization defined a work plan, with 10% of sales coming from the rural communities themselves, 50% from national and provincial public programs and the remaining 40% subsidized by El Ceibal. The work plan took three years to implement and has to be adjusted annually due to the high complexity of the issue and lack of prior experience in this type of activity.

There is currently a greater demand for this service from the communities of Salado Norte. At the outset the organization worked with approximately four communities and 70 families, compared with around 500 families today. This considerable growth has led to the formation of a local development plan for the next three years with organizations from Salado Norte, which aims to work with around 1000 artisan families.

The activity enables El Ceibal to maintain its overhead costs and pay its staff, although it only covers 60% of the actual staff salaries.

The Land Use activity has however brought it closer to its mission and at the same time has generated a greater autonomy in terms of funding and donor relations. The Land Use has become an issue that crosses all areas of the institution and has led to greater synergies with other areas. In order to guarantee a quality service of this kind, which is politically and culturally complex, the organization's experience thus far indicates that it must continue to create organizational conditions with the rural sector. To maintain sustainable development of rural communities, El Ceibal believes that these communities must first gain access to the land on which they live.

The income earned from self-financing activities represents 37% of the annual budget and was

as follows for 2007: Ar\$ 42,170 (US\$ 14,056) in investment dividends from the FIS, Ar\$ 4,500 (US\$ 1,500) in membership dues, Ar\$ 159,820 (US\$ 53,273) from its Land Use activity, and Ar\$ 2,640 (US\$ 880) from rentals.

Challenges of self-financing

El Ceibal sees itself playing a pivotal role in the development of rural communities through these activities. It now faces the challenge of sustaining grassroots organizations while working toward its own sustainability. This is a challenge that it is taking on one step at a time, and the organization has identified the following areas as key goals to accomplish in this process:

- The need to have: a vision, plan, and strategic management of all organizational processes, expressed through strategic goals and work plans; participative processes driven and implemented by 3 to 5 people, with the participation of other people from various membership circles and positions of responsibility; and an outline of risks and opportunities.
- The creation of a local development plan with the organizations of Salado Norte for 1000 rural families for the next three years, supplementing its income through the Land Use activity.
- The systematization and communication of practices to increase knowledge, using suitable methodologies and developing a *social technology*. A precise definition of the standards, process flows, procedures, guidelines and mechanisms to ensure ongoing improvement in this area.
- The need to work with qualified, competent and committed people, putting together teams of people who share the same vision, ethical values, relationships based on trust and belonging, strong commitment and high levels of efficiency and effectiveness.
- The design of a decentralized structure that guarantees low overhead costs; setting up a



core team to summarize, provide guidance and assistance, and monitor the processes.

- Preparation of the organization so it can operate simultaneously on a local, national, and international levels.

4.4.3 Legal aspects of the organizations for the development of commercial activities

AEDROS and El Ceibal Asociación Civil are exempt from paying income taxes under the national Income Tax Law, Law 20,628, which establishes tax exemptions for associations that comply with certain conditions. Also, as income tax-exempt entities, they are also exempt from paying the Business Assets Tax under Law 25,063. They are VAT-exempt under Law 23,349, the Value Added Tax Law, as they provide services directly related to their institutional mission.

AEDROS is taxed at zero-rate on its gross income under article 126, clause 7 of the Consolidated Fiscal Text 2002 (Autonomous City of Buenos Aires). El Ceibal is also exempt from paying this tax under current legislation in the province of Santiago del Estero.

These tax exemptions apply to all their activities, including self-financing, because both associations qualify for the exemptions. Furthermore, both AEDROS and El Ceibal have successfully applied for and been granted all exemptions for which they are eligible.

As civil associations, both file the same income taxes returns that any for-profit commercial enterprise would file under current regulations (RG 1815, AFIP). The form, information and requirements are the same, the only difference being that they have to state their exempt status in order to declare the final tax rate as zero, regardless of whether they carry out commercial activities or not. Both associations use the AFIP online forms and a fiscal password to declare the donations they have received and given. They are also required to:

1. Make the following deductions (for payments to suppliers, employees etc.):

- Under General Resolution (RG) 830 on fees, rentals, and others.
- Under RG 739 on beneficiaries from abroad.
- Under RG 4139 on salaries.

2. Provide the following information:

- As per RG 992: Detail each donation received and made, stating CUIT number, amount, type, date of bank deposit etc. for each one, by means of a sworn income tax declaration.
- As per RG 4120: List the current board members at December 31 of each year.
- As per RG 992: Provide certification of tax accounting books, form 760/c, which must be completed and signed by a certified public accountant whose signature is certified with the Professional Council of Economic Sciences.

A balance sheet and annual accounting report must also be submitted. AEDROS has to submit these documents to the IGJ and El Ceibal to its equivalent organization in Santiago del Estero. These must be declared annually, along with its members' registry. Both must also pay employer's contributions for all employees.

These requirements are reviewed by attorneys and accountants; the latter must be certified and have their signatures on file with the Professional Council of Economic Sciences. Both organizations indicate that having being assessed, they are aware of the regulations for their activities but that the laws are clear but inaccessible. Furthermore, they would be unable to submit the necessary information without the help of an accountant.

AEDROS would like procedures for submitting tax return forms for gross income and AFIP formalities under RG 1815 to be more efficient. Specifically regarding tax return forms for gross income, it feels that it shouldn't have to file these



forms annually in order to requalify for tax exemption. AEDROS would like to see a reduction in formalities required by AFIP under R1815 depending on the income of the CSO (those having an income below a certain level could be exempt from certain obligations) in order to reduce administrative expenses.

El Ceibal Asociación Civil has suggested improving and speeding up the procedures for completing the AFIP formalities under RG 1815. With relation to civil associations, it believes that there is a legal vacuum as the current laws do not take into consideration the social obligations of these organizations. It asks for a specific regulation governing CSOs.

4.5 Recommendations for the legal framework

As stated in previous chapters, this guide examines Argentine laws and regulations relating to the commercial activities of CSOs and analyzes their practical effects. NESST's experience and the information it has gathered lead to the conclusion that self-financing should be considered an additional means of generating resources and supplementing contributions from different donors, including the government. The existing laws governing self-financing need to be modified, given that associations and foundations are not treated equally.

4.5.1 General regulatory framework governing CSOs

In order to improve the general regulatory framework, a consensus between CSOs and their donors must be reached to produce a change in current legislation. To broaden the exemption framework in the future, a set of clear incentives must be established, which can be applied across the board under a clear legal framework.

4.5.2 Regulations applicable to CSOs relating to self-financing (including pending reforms)

The first required step in terms of legislative change is to put an end to the elimination of exemptions for CSOs engaging in self-financing

(destination-of-income). Furthermore, in order to recognize the social value of self-financing activities carried out by foundations, the distinctions between foundations and associations should be eliminated. Therefore, foundations should be allowed to engage in self-financing and maintain tax exemption on the income they gain from them, provided they are related to their mission.

Were there to be a significant rise in the level of self-financing within CSOs, the legislation could be adapted so that CSOs can become 100% shareholders (limited company of one member only) and that the profit gained would be wholly received by the parent CSO and not subject to income tax.

The experience of other countries, where different legislative systems have been designed, could also be considered:

- a. Apply the destination-of-income doctrine which prioritizes the destination given to the funds regardless of whether the income is related to a CSO objective or not. What matters is that the funds are not distributed but instead used to finance the organization's social purpose.
- b. Apply the principal purpose doctrine which allows (or does not penalize) those self-financing activities related to the fulfillment of their social purpose.

4.5.3 Taxes on CSO commercial activities

To broaden the exemption framework in the future, a set of clear incentives must be established, which can be applied across the board. However, although a certain consensus has been reached, the proposals made by CSOs regarding VAT vary from the desire to broaden the exemption framework for determined self-financing activities, regardless of who carries them out, to the request for VAT exemption to be authorized for all CSOs, but limited to income generated from the fulfillment of their social purpose. This would lead to activities, such as the provision of services or sale of goods not related to the organization's principal



activity, being subject to value added tax. There are also those who would like to see CSOs exempt from paying value added tax with no restrictions.

However, the government continues to establish reforms limiting VAT exemptions for tax revenue reasons, claiming that this tax works well when its application is generalized. Taking into account this claim by the AFIP, it is also highly likely that the measure is supported by commercial businesses who claim that there would otherwise be unfair competition by CSOs.

Tax credit on purchases could be recovered by requesting refunds (similar to the procedure relating to exports), or by applying the tax credit generated by the purchase of exempt operations to the tax debit of taxable transactions.

In view of this government position, the most viable option is to obtain VAT exemption on those transactions related to the principal purpose, thus reducing the price of products and services that CSOs provide to more vulnerable communities. It would also be technically faster and bureaucratically easier to allow tax credit to be applied to the tax debit of taxable transactions.

4.5.4 Other relevant laws applicable to non-commercial sources of financing

Argentine law sets out that deductible donations in the tax returns of companies or individuals who donate should not be more than 5% of profit, with no possibility of generating losses. If the donations exceed this percentage, this surplus cannot legally be transferred to the next tax year. In the 1980s, this limit was 20%.

CSOs have always tried to maintain the limit at 20%, although in reality the average levels are significantly below this. However, fundraising campaigns for large philanthropic operations require donations considerably higher than 20% of income.

The government has failed to understand that, in the case of large donations, eliminating this limit

is detrimental to tax collection only in exceptional cases, and overall is insignificant in terms of general loss of revenue.

Tax treatment of donations

It is universally known that donations represent a crucial resource for CSOs. As stated in Chapter 3, Argentine law allows donations made to CSOs to be deducted from the tax returns of the donors, provided that they have previously obtained income tax exemption and are pursuing determined social purposes, such as medical or welfare nonprofit purposes, scientific or technological research, scientific research into economic, political or social issues aimed at developing ideas for political parties, and formal educational activities.

Until 1995 there was no discrimination in relation to social purpose regarding deductions from donor donations. This conditioning of deductibility on the basis of determined purposes has been controversial and difficult to apply in Argentina, generating legal insecurity.

The situation often arises wherein certain purposes are included or excluded within the same CSO and this causes uncertainty when determining whether a donation can be deducted or not. The general opinion is that this benefit should apply to all donations to CSOs with legal status and that they should also be exempt from income taxes without discrimination based on social purpose. Generalizing this incentive would undoubtedly help to increase philanthropy and eliminate uncertainty regarding the issue of tax deductions.

Taxes on bank credits and debits

Law N° 25.453 regarding taxes on credits and debits in bank accounts and other operations sets a rate of 0.6% on all movements of funds, including cash funds, whether one's own or from a third party, made by any person including those mentioned in the Ley de Entidades Financieras (Law of Financial Entities), via an account in his/her own name and/or that of another person, whatever the mechanisms used to carry it out, the



denominations being authorized to them and their legal instrumentation, including those destined for accreditation to establishments using credit and/or debit card systems.

CSOs have always protested strongly against this tax. By means of decree 1287/01, the government established a differential rate for credits and debits in checking accounts of two point five per thousand (2.50 0/00) for those concurrently carrying out transactions exempt from value added tax and therefore exempt from income tax. To obtain this benefit, the entities have to make a presentation to their bank and submit the required documentation.

4.5.5 Process of declaring taxes and other reports

Authorization of income tax exemption

To fulfill its mission and achieve its goals, it is essential for a CSO to be exempt from paying income tax. This is necessary to keep its operations economically viable and to maximize its social impact. The income tax exemption certificate is also important because it is *the key* to obtaining other tax benefits, such as to enable donors to deduct donations from their income tax or to qualify for other tax exemptions.

As aforementioned, exemption is not automatically granted and has to be requested and authorized by AFIP. Authorization is first given provisionally then confirmed for a determined length of time at the end of which the CSO has to request an extension. During this time, inspections can be carried out which may result in a revocation of the exemption should any anomalies be found. In some cases the process is long and can take over six months to complete.

CSOs have complained that the process of gaining legal status is lengthy and requires a major institutional and economic effort, and would like to see permanent renewal following the temporary authorization.

CSOs agree that the authorization process for exemptions needs to be faster and that once authorized

should be of a permanent nature. This would help ease a complicated process which takes up a lot of time and resources.

They are also seeking defined parameters for its rejection, which would avoid the discretionary nature or even arbitrariness of the bureaucracy.

Tax on gross income. Presentations

In the city of Buenos Aires and the rest of the country, CSOs have always been considered exempt from the tax on gross income. In 2004, the city of Buenos Aires began to treat CSOs as zero tax entities.

This produced many changes for the organizations, which then had to register themselves and make monthly presentations of their gross income and annual affidavits in order to be able to receive the same treatment the following year.

There is consensus that CSOs should once again be considered as exempt, as was previously the case, and that tax treatment should be standardized throughout the country.

Formal obligations for CSOs regarding AFIP RG 1815

The AFIP General Resolution (RG 1815) came into effect in January of 2005 and established a new procedure to recognize and register exempt entities as well as procedures regarding information on donations made to them. This resolution made it necessary for exempt entities to present a sworn declaration of income tax and also incorporated specific new formalities and sanctions such as loss of exemption for non-fulfillment. Whilst it is true that this norm puts information in order and makes it transparent, it comes at a high cost to CSOs since it establishes important formal burdens along with fines and loss of exemption if sworn income tax statements and sworn statements from record books (form 706/C), signed by a public accountant, are not presented. This creates a high administrative and financial cost for organizations that benefit from donations.



CSOs propose that obligations be limited depending on the income of the organization, considering that smaller CSOs usually having fewer administrative capabilities and less access to information from the AFIP.

Conclusion

Legislation should aim to benefit society as a whole, encouraging initiatives that are of public benefit. The countless initiatives developed by CSOs throughout the world are quietly generating an elaborate network of human relationships which, although difficult to measure, contribute enormously to the general strengthening of society and the resolution of important social problems. There is currently a global trend to facilitate the growth of CSOs by providing incentives for donations, and to enable the development of self-financing in order to contribute to CSO sustainability.

This study has shown that the legal framework and administrative processes related to self-financing and social enterprise for CSOs in Argentina need to be reformed or improved.

1. Income Tax

Treatment of associations and foundations should be equal, and it should be easier for foundations to carry out self-financing activities, allowing them to maintain exemption on taxable earnings.

The percentage that donors can deduct from their net earnings should be increased. The limitations, which only allows CSOs who classify their activities and objectives within the four thematic areas mentioned previously to receive deductible donations, should be eliminated.

The legal tax framework is generally identified as a favorable mechanism for the promotion of CSO activities through the authorization of special tax breaks or benefits (such as income tax exemption). Thus, by granting tax exemptions to CSOs (and therefore to their activities, including commercial ones which derive from or further their

social mission), the government provides a sort of indirect financing through the partial waiver mechanism (a tax waiver when certain income is not taxed) on its tax revenue expectations. This has important redistribution effects: it contributes to the strengthening of nonprofit organizations that further the provision of social-purpose goods and services in a way that complements the state, or in areas that the state does not reach. This benefits a broader group of stakeholders (CSOs, local organizations or beneficiaries of the social programs that CSOs develop, and donor agencies), including the government itself. CSO involvement in economic or commercial activities should be regarded as contributing to the fulfillment of the organization's social purpose and its sustainability and should be promoted by the government.

2. Value Added Tax (VAT)

It would be helpful for CSOs to be able to apply for refunds of VAT applied on the acquisition of goods and services in Argentina. Currently not recovering VAT implies a significant cost (17%) for CSOs, especially for those who cannot use it as a tax credit because they don't run business activities and cannot recover the VAT paid. Its recovery would enable these organizations to have additional resources to put towards their social purpose.

Likewise, in business activities where CSOs transfer the corresponding 21% value added tax for their goods and services to their users or buyers, this also results in a significant cost as the users or buyers are often low-income people.

3. Training on the legal framework

Aside from the tax reforms mentioned in the previous two points, it is important to promote dissemination programs or policies on the legal framework – especially those of a tax nature – of CSO economic activities and their general operations, placing special emphasis on training government officials responsible for application of the legislation and civil society as a whole.

CSOs currently need support and specialized technical assistance, not only for regular commercial



management but also to help them comply with the requirements imposed by the tax regulations.

In summary, the best solution would be to work together with CSOs, the organizations that bring them together, citizens, employees, legislators, and regulatory organizations in order to achieve a better consensus relating to fostering the development of CSOs. Methods of screening and controlling by the institutions themselves for example need to be discussed, but alongside a serious policy of incentives for the sector and a reduction in excessive formalities, which particularly affect smaller and weaker CSOs, but with proven and efficient work. Measures allowing the development and effective functioning of civil society organizations need to be adopted along with the necessary conditions that will allow them to be sustainable over time and to achieve the social purpose for which they were created.



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