

# DETECTING IRREGULAR POLITICAL FINANCING

**Training manual**

COUNCIL OF EUROPE



CONSEIL DE L'EUROPE



# **DETECTING IRREGULAR POLITICAL FINANCING**

**Training manual**

**English edition**

Published by the Council of Europe  
F-67075 Strasbourg Cedex  
www.coe.int

© Council of Europe, July 2016

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Pictures @ Council of Europe

Layout and cover design:  
Council of Europe

Printed by Council of Europe,  
F-67075 Strasbourg Cedex  
Circulation: 150 copies

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This publication content has been produced within the framework of the Eastern Partnership-Council of Europe Facility Project on “Good Governance and Fight against Corruption” with the financial assistance of the European Union and the Council of Europe. The views expressed herein can in no way be taken to reflect the official position of the European Union and/or Council of Europe.

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# 1. Introduction

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**D**iscussions regarding political party financing namely focus on (non) existence of legislative frameworks regulating political funding and the level of their implementation. In countries where rules on political financing are introduced, the functioning of such a system depends largely on the effectiveness in ensuring that political actors follow such rules and omissions or violations are identified and properly sanctioned.

The current publication aims to support authorities tasked with overseeing implementation of political financing regulation. It aims to do so by providing concrete guidance on issues to be considered by both administrative oversight bodies and investigating agencies as part of inquiries/investigations into possible irregular political financing. Furthermore, it explains most frequent modalities of avoidance and evasion of political financing rules, possible red flags, and steps available to authorities in gathering information and evidence on any such wrongdoing.

The publication also incorporates more than thirty case examples involving irregular political funding as an illustration of issues discussed, as well as a hypothetical case-study that can be used by authorities as part of internal trainings. Information presented in the current publication does not reflect any specific legal or organisational framework, but relies on common European principles related to political financing and oversight. In that sense, it will be useful for all political funding oversight authorities irrespective of the specific regulatory context.

The idea on developing a publication on Detecting Irregular Political Financing was piloted during trainings for representatives of governmental authorities and structures in charge with monitoring and implementing political finance regulations in Eastern Partnership countries. The content of this publication has been prepared by the Secretariat of the Economic Crime and Cooperation Division with contributions and input from the following Council of Europe experts: Tilman Hoppe, Yves-Marie Doublet, Natalia Iuras, and Inga Soloveja.

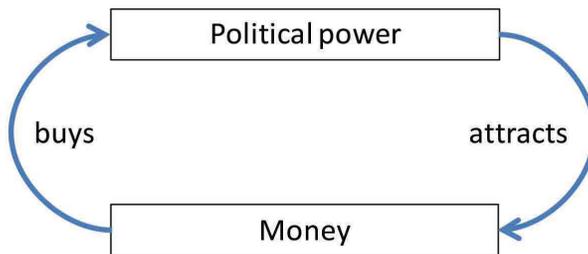


# 2. Political finance

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## 2.1 Money and democracy

Election campaign and party funding is an important factor of the electoral process: no money, no political parties, no elections, no (representative) democracy. But money in politics can also mean that political influence will be “auctioned” to those with money; and that the ones in power will stay there, because they can raise more money:



Money influences politics from two angles:

- ▶ Elections: which parties and candidates have the most money to fight for power?
- ▶ Political Parties: which parties have the most money to influence politics (and the next election)?

Virtue of democracy is to separate politics from money. This separation applies to reaching and exercising power, to ensure that neither candidates, political parties nor voters are subject to improper influences or pressures and to provide equality of means between candidates and political parties. Transparency of resources and electoral expenditures is a key policy instrument to achieve this aim. Monitoring and sanctions of violations of rules governing political finance are the adequate mechanisms to enhance transparency and the implementation of political finance regulations. Although institutions, historical background, social context, voting system can differ significantly from member state of the Council of Europe (CoE) to another, these states share same democratic values and transparency is essential for democracy whatever the level of political and economical development of the country is. Over the last decades each member state of the CoE provided for a regulatory framework for political parties and campaign finance. These legislations have been inspired by international instruments.

Common standards to ensure an appropriate level of transparency, supervision and enforcement have been defined in particular by the Recommendation of the Committee of Ministers of the CoE of 2003 on common rules against corruption in the funding of political parties and electoral campaigns, the 2003 United Nations Convention against Corruption (UNCAC), the Group of States against Corruption (GRECO), the Venice Commission, and the Organization for Security and Cooperation in Europe (OSCE).

The Recommendation of the Committee of Ministers of the CoE of 8 April 2003 on common rules against corruption in the funding of political parties and electoral campaigns contains several principles on transparency of funding of political parties accounts, on supervision and sanctions for offences which have been stipulated by acts on political parties' finances of the member states of the CoE. Principles provided for by the recommendation are required to be applied by member states. Article 8 of the Recommendation considers that the regulations regarding funding of political parties should apply *mutatis mutandis* to funding of electoral campaigns of candidates.

Article 7.3 of the UNCAC calls on each Party to the convention to consider taking appropriate legislative and administrative measures consistent with the objectives of the convention and in accordance with the fundamental principles of its domestic law to enhance transparency in the funding of candidatures for elected public offices and where applicable the funding of political parties.

In their field of activity and according to their purposes and their proper methodology, the GRECO, the Venice Commission, and the OSCE help to identify deficiencies in domestic law regarding transparency of political finance.

Reoccurring types of irregularities of political finance are the evasion of legal restrictions on donations from physical or legal persons, funding from illegal sources, providing false information, bribery of voters, excess of the limits on campaign expenditures, breach of reporting and disclosure requirements.

Issues of transparency, monitoring and sanctions of infringements of the law on political finance are closely interconnected. No efficient monitoring may be carried out without transparency of funding and no sanctions may be imposed without investigations and efficient monitoring.

If candidates and political parties don't comply with rules ensuring transparency and equality of opportunity, violations of these regulations have to be detected. Persons involved in the monitoring process have to take into account the seriousness of the non-compliance and to assess if it is a willful misrepresentation or a genuine act. This monitoring may be carried out by investigation mechanisms of supervision authorities, by civil society, media, the judiciary, investigative journalists, electoral contestants, voters or coalitions of voters and NGO's. But information gathered by these stakeholders may be valuable too in identifying issues, legal loopholes or ambiguous regulations. To correct these shortcomings, enforcers may make proposals for introducing in the national legal framework on political finance of the relevant country, regulations or good practices in line with international commitments. Reporting after elections may contribute too to address the implementation of these

regulations and to suggest amendments to correct them in light of experience. For this reason observations on wrongdoings may be completed by proposals to review regulations when they are inadequate.

## 2.2 Cash-flow in politics

Money in politics comes mainly from the following sources:

- ▶ Membership fees (incl. taxation of salaries);
- ▶ Private donations (incl. fundraising activities) in cash and in kind;
- ▶ State funds (direct financial support from the budget);
- ▶ Income from business activities; and
- ▶ Income from property.

Money means more than cash:

- ▶ Free media time;
- ▶ Use of administrative resources (offices, staff, transportation, communication, energy, etc.);
- ▶ Use of private resources (offices, staff, energy, transportation, communication etc.);
- ▶ Indirect state support (tax exemption for parties, tax deductibility of donations, free airtime on radio and TV, free public services, such as postal, energy, telephone, transportation), and free use of public facilities.

Who are the recipients of political finance?

The most frequently cited recipients of political finance are political parties and election campaigns/candidates. However, there are two more stakeholders that are often overlooked: parliamentary groups (political factions) and members of parliament. Both are often recipients of separate flows of private and public funding. In Germany, for example, the work of parliamentary groups is completely financed by the state; members of parliament receive a state financed budget for hiring staff and renting offices; they can also receive personal donations which are subject to little, if any, oversight.

## 2.3 State funding

There is not even one single state in Europe which does not allow for some type of state funding to political parties. The main arguments for state funding are:

- ▶ There is less risk of (rich) individuals unduly influencing the political process;
- ▶ Parties do not have to spend their time on fundraising;
- ▶ Funding can be linked to more objective criteria such as voting results;
- ▶ It can provide opportunities to new political parties, underrepresented population (young voters, women, national minorities etc)
- ▶ It ensures the independence of political parties.

The downsides of state funding are:

- ▶ Impact on budget;
- ▶ State mixes with politics;

- ▶ Public funding does not foster civic involvement;
- ▶ Risk of government funding parties with extremist positions;
- ▶ Lack of a fully just allocation system: What is the formula for allocating funds – voting results in previous elections? Private donations? Number of members? Number of seats in parliament? Number of women elected?

The State cannot, and probably should not, allocate the same amount of money to both very small and very big parties, for example, there ought to be a distinction between those parties represented in Parliament and those that have not yet won any seats. Neither with private nor with public funding systems or a combination of both is there a system that will be ideal and “just” for all stakeholders.

# 3. Issues for consideration regarding irregular political financing

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## 3.1 Transparency of financial administration

### 3.1.1 Duration of election campaign

Transparency supposes that financial statements of political parties and election candidates reflect closely their resources and expenditures. Definition of duration of election campaign is a key issue to ensure this transparency. If duration of the election campaign is not clearly defined or if it is too short, the financial reference period applicable to the real campaign period will allow political parties and candidates to collect money and spend it outside the official election period and for that reason, financial reports of political parties and candidates will record only a part of election campaign funding and electoral expenses. Observers of the electoral campaign may encounter three different situations in practice.

There are countries where duration of election campaign is not precisely defined (Austria, Serbia). Regulations have to remedy this shortcoming and to define this financial reference period. In other countries this period is very short (Azerbaijan, Greece, Lithuania, Former Yugoslav Republic of Macedonia). In this context parties and candidates are not required to record income and expenditures incurred before this period even they are related to an election campaign. When a candidate is the incumbent candidate, he may use institutional resources during that time to promote his electoral interests. This conflicts with the principle of equal treatment of candidates and of a fair electoral process. One has to bear in mind that paragraph 7.6 of the 1990 OSCE Copenhagen meeting of the Conference of the Human Dimension of the Conference on Security and Cooperation in Europe provides that the states respect the right of individuals and groups to establish, in full freedom, their own political parties or other political organizations and provide such political parties and organizations with the necessary legal guarantees to enable them to equally compete with each other before the law and by the authorities. Short campaign periods therefore need to be revisited and preferably extended.

A third type of duration of election campaign makes a distinction between two periods: the “long campaign” and the “short campaign”. It applies in the United Kingdom with two different spending limits for every time period. The “long campaign” refers to the period of several months prior to a person formally becoming a candidate at a general election. The “short campaign” is the period of weeks after the person formally is a candidate and ends with the polling day.

***Length of election campaign must deserve attention of the supervisors. When there is no financial reference period, or when this one is too short, it is recommended to establish such a period or to extend it so that the financial activity of candidates and political parties should be accurately and comprehensively recorded.***

### **3.1.2 Financial agents**

In many countries candidates or political parties have to appoint financial agents or registered associations (France, Ireland, Italy, United Kingdom, and Canada). They have to open a bank account for the funding of the election campaign and to keep comprehensive and accurate records of the political finance of the entity they work for candidate, election fund or political party. All monetary transactions have to go through this account. These agents or associations collect the funds and pay the campaign expenses in conformity with rules. Scrutiny in that field will require verifying if the agents or the associations are qualified to act as financial intermediaries with the party or the candidate. A candidate for instance is not eligible to be a financial agent. In France all electoral expenses of the candidate have to be paid by the financial agent and according to jurisprudence, the candidate is entitled to settle just a tiny proportion of these expenses.

***Supervisors have to assess if expenses have been settled directly by the candidate or the political party or escaped to the oversight of the financial agent, which might be considered as an irregularity.***

### **3.1.3 Keeping books and accounts**

A way to be sure that income, expenditures, assets and debts of political parties are accounted for in a comprehensive manner for the appropriate period of time provided for by the law is to verify if the relevant party accounts cover the central, regional and local levels<sup>1</sup> and entities which are related directly or indirectly to the party or under its control such as youth movements, women associations, party foundations or persons with “declared electoral goals” affiliated to a political party (Georgia). They may be involved in a variety of activities including charity, culture and education, printing and editing, event organizing. They may take part to parties’ activity, especially during campaign periods. Supervisors should, among other things, verify if these entities have registered addresses same as the party. If associated entities are not covered in the annual accounts of political parties, appropriate measures should be taken to remedy this shortcoming.

***Supervisors have to assess if all financial documentation related to election campaign and party funding is comprehensive and kept for an appropriate period of time. If these legal requirements are not regulated, rules that provide for full and appropriate counts should be introduced.***

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1. For instance in Sweden reporting is limited to the central level of political parties.

## 3.2 Transparency of sources of income

### 3.2.1 Private sources

#### 3.2.1.1 Membership fees

Membership fees are a legitimate source of political party funding. No limitations on membership fees apply in Austria, Denmark, Finland and Germany. Amounts of membership fees are usually set forth in statutes of political parties. Supervisors have to check if the statutes of political parties limit the amount of membership fees and if they have to be made through the banking system. Political parties may also decide not to set up such limit calling upon freedom of activity of a political party.

Membership fees may be considered by tax authorities as donations if there is a tax benefit accrued to the membership fee as for a donation (France, Germany). In cases where their permissible amount is not clearly defined, and if they are not liable to a specific threshold, membership fees can be used to circumvent the rules on limitations on donations to be made by natural persons.

Disclosure of membership fees is also an important issue. If political parties are only required to disclose the total amount of membership fees, like in Korea, it will be impossible to get information on party members who paid a large amount of membership fees and to permit supervisors and voters to be informed about the specific interests behind a party. Similarly, in Armenia data regarding membership fees must include the total number of party members who paid fees. This is however not sufficient to ensure that membership fees are not used to make covert donations to political parties.

Membership fees may be paid in cash if such a source of funding is not prohibited by the relevant statutes of the party. In Estonia the public register of the party includes the name, the personal identification of the member, the amount of the fee paid, and the date of its payment. Membership fees are separately declared from donations.

***It is advisable for supervisors to look to see that membership fees are not used to circumvent rules on donations and to recommend to take measures to limit this risk.***

#### 3.2.1.2 Donations

Article 2 of the above-mentioned Council of Europe Recommendation (2003) 4 on common rules against corruption in the funding of political parties and electoral campaigns defines donations in fairly broad terms as "*any deliberate act to bestow advantage, economic or otherwise, on a political party*". It means that donations should not influence the decision-making process.

Identification of donors is a central issue. Only donations from permissible sources are regular. If a candidate or a political party accepted a donation from an illegal source and if rules provide for the return of such irregular donations to the person who transferred the donation or to the State, parties and candidates have to comply with these rules. In the United Kingdom the register of donations reports impermissible donations returned by parties within the 30-day period provides by law. Details of how and when an impermissible donation was returned are also published. For

instance, in Austria illegal donations to political parties have to be recorded on a specially designated account of the Court of Audit. Supervisors must know if this kind of regulations are being implemented in practice.

***The form, the amount and the timing of political contributions should be reviewed to ensure that they are not used as camouflage for corruption.***

### *3.2.1.2.1 Anonymous and cash donations*

Because they can shield influence on decision making from any form of scrutiny, anonymous donations are generally forbidden (Albania, Azerbaijan, Belarus, Estonia, France, Georgia, Latvia, Moldova, and Portugal). They however remain permissible in a few countries (Denmark, Liechtenstein, Monaco, Sweden, and Switzerland). Where it is mandatory to make payments through bank transfer, bank check or bank credit card, making anonymous donations is more difficult as any payment is traceable.

Illegal cash donations, on the other hand, may potentially come from sources such as tax fraud, money laundering, kicks backs, and embezzlement. They are however not fully always prohibited and can be allowed up to a certain amount (Estonia, France, Germany, Ireland, Poland, and United Kingdom). They are also not inevitably anonymous. In fact, cash donations may be made by an identified donor who expects to get certain benefits from his/her donation.

***For supervisors, it is important to distinguish the two categories of donations (anonymous donations and cash donations), which don't systematically overlap. In some cases cash donations are considered as anonymous but in other cases donors of cash donations are well known. Supervisors have to check if regulations on donations expressly prohibit cash donations. Where this is not the case, it would be useful to introduce prohibitions or rules that require donations to be made through bank transfers.***

### *3.2.1.2.2 Donations from natural persons*

If only individuals can make donations, supervisors have to check if a given natural person is entitled to make a contribution because very frequently only nationals or permanent residents are allowed to contribute.

It may happen that the status of the natural person as a donor is not always clear. If the donation originates from a person who is self-employed, while at the same time donations from legal persons are prohibited, such a donation would be considered as ambiguous. It would therefore be necessary that criteria of donations from natural persons are defined and assessed precisely.

Splitting of donations and channeling donations through a large number of donors is a traditional way, under any domestic legislation, to circumnavigate the rules on donation transparency. It is not a breach of law but it affects the reporting of party and election campaign accounts.

### *3.2.1.2.3 Disclosure of donations above a threshold*

Donations from natural persons are considered to foster political participation, in particular when a tax benefit is attached to the donations (France, Germany). On the

other hand, if the threshold for disclosure of donations is relatively high, this may favour more anonymous and cash donations and undermine the impact of the rules on disclosure of the identity of the donor. Many countries opted for disclosures above a certain threshold: Albania, Austria, Bulgaria, Cyprus, Finland, Georgia, Germany, Italy, and Norway, for instance. This disclosure applies for natural and legal persons in Albania, Austria, Cyprus, Germany, Italy and the Netherlands. When the level of the threshold is particularly high (Germany), this limit may not serve its purpose to mitigate undue influence on political parties and candidates. High thresholds may be used by wealthy donors to split donations through donations of straw men.

***Lower limits for the disclosure of the identity of donors increases transparency and makes supervision easier. Supervisors should be mindful of reporting thresholds and issues associated with high threshold.***

#### *3.2.1.2.4 Donations from private companies*

Increasing number of CoE member states are prohibiting donations from companies to political parties and election candidates. Acceptance of donations from private companies in Belgium, Estonia, France, Lithuania, Poland, Portugal and Spain is a breach of law and is liable to sanctions. But such bans may have limited effect if money can still be “sent through” political foundations or associations closed to political parties, as is the case in Spain.

***When donations of private companies are forbidden, special attention must be paid to effective implementation of such a prohibition namely by looking at whether any such donations are not being made through entities connected to election campaigns and political parties.***

Approval of shareholders

In some countries, such as the United Kingdom, shareholder approval resolutions are required for companies to make political donations.<sup>2</sup> General approval to make donations and incur expenditures up to a prescribed amount determined by the company must be given by shareholders every four years. There is an exception for donations – not expenditures – of up to £ 5 000 in total annually which does not require shareholder approval. Where such rules exist, investigations on donations of private companies should verify if this legal requirement has been fulfilled when such donations have been made.

***When approval of shareholder is required, oversight of enforcement is a tool for ensuring accountability of the donors and transparency of the funding channel.***

#### *3.2.1.2.5 Donations in return of public procurements*

In states which allow company donations such generosity may be rewarded with procurement contracts unless donor companies are prohibiting from bidding for tenders.<sup>3</sup> It is the form of the so called “pay-to-play” practice.

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2. Companies Act 2006, Pt 14.

3. 74 % of the OECD countries ban donations from corporations with government contracts or partial ownership with political parties.

Donations from companies which are bidding for public procurement contracts may be liable to prohibitions during the time period of the procurement (Serbia, Spain). In the United States a contractor who provides goods and or services to the Federal Government or any affiliated department can't make any contribution to any political party, political action committee or candidate in connection with a federal election. In Chile a ban applies to companies where the amount of the contract represents more than 40% of the annual revenue of the corporation. But donations after the conclusion of the public procurement can be equally tricky from favorism point of view and tend not to be regulated. It is the reason why a "cooling-off period" for donations from private companies after the conclusion of the public procurement is advisable. A general ban on donations from companies which have signed contracts with the Government would be a stricter regime, provided that it also covers entities directly or indirectly linked to a political party.

***Supervisors should therefore pay attention to possible benefits through contracts and licenses that may be associated with individual donations. This applies both to situations where such donations are being made before and after the contracts/licenses had been awarded. Evidence for such transaction requires deep investigations.***

#### *3.2.1.2.6 Donations from foreign companies*

The most frequent rule is that political parties and candidates cannot be influenced by foreign interests. In situations when a donation is made through a national subsidiary of a foreign parenting firm, it is not very easy for a supervisory entity to assert that the subsidiary acted completely independent from the foreign parenting company. Risk of undue influence of foreign entities may also occur when donations are made to entities related to political parties, such as party foundations and think tanks, where such donations are not regulated. Supervisors should take note of such practices.

***Ambiguous statutes on donations from foreign companies could pose a problem for supervising enforcement of a prohibition of such donations due to legislative loopholes that allow for circumventing the rules.***

#### *3.2.1.2.7 Donations from public companies and public bodies*

There are many variations in relation to regulatory prohibition of donations from public corporations. This can be explained by the fact that semi-public bodies such as state or local-owned companies, or semi-public institutions such as think tanks or state supported non-profit organizations may also have a stake in electoral campaigns. Therefore, Austria, for example, prohibits donations from corporations if the state holds at least 25% of the shares in it. In Austria and Germany, public funds to parliamentary groups cannot be transferred to political parties. Depending on the legal setting, these matters need to be considered by supervisors.

***Supervisors have to keep an eye out for possible engagement of public entities or semi-public entities in electoral campaigns. Donations from public companies to candidates and to political parties which are a form a political endorsement have to be prohibited.***

### 3.2.1.2.8 *In kind donations*

Provisions of services, equipment and goods in kind to political parties and election candidates are often not regulated. A supplier who supports the electoral campaign of a candidate may give him goods or services at a reduced value or pay for leaflets and manifestos on behalf of the candidate. Monitoring bodies have to identify them and ensure that they are properly recorded, at their market value, in the financial statements of the political parties and of election candidates. It requires investigations to identify the services rendered and their value. For that purpose, investigators have to collect information on what similar providers charge for the same goods or services.

In addition to commercial discounts that could be available for both regular clients, such as companies, and election candidates, non-commercial discounts could also be given by suppliers close to certain candidates. This refers to any special rate which is not available on the market. Internet is a good way for finding out market rates of goods and services. For instance when a self-employed web designer designs the website of a candidate and does not charge for this service, this is a non-monetary, in kind, contribution. Its commercial value is equal to the amount the provider would regularly charge for the same kind of service. In Latvia, services provided to a political party have to be declared to the Monitoring Committee within 15 days of their receipt. In the United Kingdom, free of charge or special discount services are regarded as a donation.

***Supervisors have to ensure that all goods and services provided in kind to candidates and political parties are properly identified and comprehensively recorded at their market value.***

### 3.2.1.3 Loans

Loan of money or credit facilities may be an important source of funding for political parties and for election campaigns of candidates (Poland, Spain). Such loans must be reported in their financial statements. Monitoring bodies need to make sure that loans granted to actors of political life are reimbursed within the terms under which they were provided. This means that information about the lender, including his name/title and address, and loan conditions, such as its value, the date it is due to be repaid, and the interest rate, have to be known. The purpose of this monitoring is to ensure that such loans don't deviate from the general conditions on the open market, that they are not partially or totally written off, and therefore could be considered as donations (Andorra, Russian Federation, Poland, Serbia and Spain), which has led to a high degree of indebtedness of political parties vis-à-vis banks.

The experience of the United Kingdom shows that loans may be used or result in inappropriate political funding. To finance general election campaign of the Labour party in 2005, loans have been made in return for the promise of a peerage. Indeed four of the lenders were nominated for peerages without the House of Lords Appointments Commission being informed of the loans.

Monitoring of the terms of the loans has to be carried out by auditors who certify financial statements and by the supervision body. More generally, in systems where

loans are not forbidden (e.g. Turkey), it is the task of supervisors to check if the debts are covered by financial statements of the candidates or of the political parties. In Italy candidates to Parliament and regional councils have to include the debts incurred for campaigning in the accounting reports and elections statements they provide to the Board of Controllers. Interest incurred on a loan is an expense irrespective of whether it is paid or accrued.

***Supervisors have to ensure that the loans to candidates and to political parties are reported and do not circumvent the rules on political financing.***

#### 3.2.1.4 Sponsoring

Sponsoring refers to different forms of support which may be given to political parties or to election candidates. This support helps them to meet the costs of events such as congresses, rallies, production or distribution of publications or studies. In certain countries, such as Germany, sponsoring is valuable insofar as it is considered by tax authorities as an advertising expense and is eligible for tax deduction. On the contrary, in the United Kingdom sponsors are not eligible for such tax deductions on any commercial value or the benefit.

Identification of sponsoring requires careful supervision from monitoring bodies. In doing so, supervisors have to take into account the form of the sponsorship. Advertising payments which do not help meet the costs of an event or a publication may not be considered as sponsorship. On the other hand, an event or a party hosted by an organization or a company, for instance, to meet the costs of a party event might be treated as sponsorship.

Amount of sponsorship has to be also taken into consideration. In the two European countries where this type of support is permitted (Austria and the United Kingdom), sponsorship has to be reported if the amount exceeds a threshold set forth by law. This means that sponsoring above the legally prescribed threshold has to be disclosed and treated like in kind contributions, i.e. these services should be evaluated and assessed at their commercial value.

***Supervisors should look into the practice of sponsorship of election campaigns of candidates and political parties and recommend regulating this use if it is not the case.***

#### 3.2.1.5 Candidates' own sources

Practice has shown that activity funding from one's own sources gives rise to two questions. When majority of this funding stems from the candidate's own sources, such as loans or any aid to a party, it is relatively easy for a monitoring body to identify these sources. However, if such own sources mostly refer to savings, it will be much more difficult to clearly identify through any kind of investigation the actual source of such funding which could also involve irregular financing.

If regulation limits donations and in-kind support to candidates for certain elections, the candidates may enjoy the privilege of having no limits for contributions to their "own funds" (e.g. Presidential election in Ukraine). This may lead to exposure to undue influence and corruption, namely in case of independent candidates. As OSCE

noted, unlimited funding of one's own campaign carries the risk that a few wealthy individuals will be able to spend unlimited amounts in election campaign. Similar concerns were raised by the Venice Commission and OSCE/ODIHR concerning Ukraine electoral legislation. If this risk may exist for independent non-partisan candidates, it may equally apply to candidates too who are very well positioned on a party list.<sup>4</sup>

***To avoid any risk of suspicion of influence and corruption, supervisors have to pay attention to risks of unlimited funding of election campaigns by candidates. The setting of a limit to the amount of contributions to a campaign which could come from a single source should be taken in consideration.***

### 3.2.1.6 Benefits to elected representatives

In some cases, donations can be given directly to parliamentarians. If this is the case, plus donations to already elected representatives from unidentified donors are acceptable, such a scenario creates an imbalance between treatment of donations to incumbent candidates and new candidates. The problem with such a scenario is additionally convoluted in countries where corruption of elected parliamentarians is regulated to a limited extent. This was, for example, the case in Germany before the introduction of the criminalization of corruption of MPs in the criminal code in 2014.<sup>5</sup>

Similar problems may occur where rules prohibit gifts to members of Parliament in return for acts performed in connection with their mandate, but allow benefits to them without any counterpart (Belgium). Such distortion poses a problem not only from the standpoint of management of risk from corruption with regard to gifts and other benefits, but also in terms of the effectiveness of the legal framework on political finance.

***Supervisors have to also look to all forms of benefit, material and non-material and to check if they constitute a breach of duty.***

### 3.2.2 Public sources

Issue of abuse of public resources is a matter of political culture. If political parties are operating in a transparent, democratic environment, with a culture of legality, risk of misuse of public resources is weaker than in countries where there is no sharp distinction between the state and the ruling party. A clear line has to be drawn in such cases between official governmental capacities and political campaign and between acceptable and unacceptable use of administrative resources.

The OSCE/ODIHR Guidelines for reviewing a legal framework for elections state that *“the legal framework should ensure that state resources are not misused for campaign purposes and that they are used only with strict adherence to the applicable legal provisions (...)* The legal framework should specifically provide that all state resources used for campaign purposes, such as state media, buildings, property and other resources

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4. Venice Commission and OSCE/ODIHR, Joint opinion on the draft amendments to some legislative acts concerning prevention of and fight against political corruption of Ukraine, October 2015, Available from: [www.venice.coe.int](http://www.venice.coe.int); Accessed on: 19.07.2016

5. Article 108 e Strafgesetzbuch. Bestechlichkeit und Bestechungen von Mandatsträgern. Gesetz 23 April 2014.

are made available to all electoral participants on the basis of equal treatment before the law”<sup>6</sup>. The Guidelines on political party regulation adopted by the OSCE/ODIHR and the Venice Commission state that abuse of state resources is universally condemned by international norms.<sup>7</sup> The ban on donation of state resources to candidates and political parties applies to counteract the risk of abuse of administrative resources.

While there is a natural and unavoidable advantage for incumbents, legislation and practice must be careful not to perpetuate or enhance such advantages. Incumbent candidates and parties must not use state funds or resources to their own advantages. Public resources have to be granted to all election competitors. To allow for the effective regulation of use of state resources, legislation should clearly define what would be considered an abuse. Such clarification would assist in supervision. Supervisors have to pay attention, for instance, to Government spending on advertising for public campaigns before elections during so called “information campaigns”, inaugurations of public services, hiring of civil servants, and awarding contracts through public procurements. Where misuse of public resources during election campaigns is not expressly forbidden, law should remedy this shortcoming.

Abuse of public resources during election campaigns for partisan ends may have different forms:

- ▶ In Austria GRECO noted that during electoral campaign ministries or municipal administrations used to buy advertising space in free newspapers.<sup>8</sup>
- ▶ Misuse of public resources consists of misuse of public buildings, meeting-rooms, vehicles, equipment, printing, machinery, travels, printing during electoral campaign. Public facilities may be used by all elected officials in the National Assembly, as it was noted by GRECO in the case of Bulgaria. Such use of official cars, equipment, secretarial services by sitting officials who were again running for office has been observed in a number of countries, including Georgia, Montenegro, Romania and in the Russian Federation. According to the 2014 EU Progress Report for Montenegro, public companies were instructed to award grants or write off debts related to electricity and water bills to consumers.<sup>9</sup> In Cyprus public entities may provide donations to political parties up to 20 000€, which creates a potential misuse of public funding.

Use of civil servants for electoral purposes is another example of misuse of institutional resources. Commitment of public servants may have other forms: pressure to vote in favor of the ruling political party/ies, incentives to working for them, mobilization to help them, and use of such individuals as candidate election staff. In order to avoid such scenarios, there should be an explicit requirement for public servants to act impartially in election campaigns at all levels. In Albania, Armenia, Ireland, Portugal and Spain public servants cannot campaign.

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6. OSCE/ODIHR, Guidelines for Reviewing a Legal Framework for Elections, January 2001, p. 22  
7. Council of Europe Venice Commission, Updated compilation of Venice Commission opinions and reports concerning political parties, 2016, Available from: [www.coe.int](http://www.coe.int), Accessed on 1.07.2016  
8. After the assessment of the Austrian regulations by the Greco, receipts from advertising space in newspapers have to be disclosed over a threshold in the financial statements of the political parties (Article 7 Parteiengesetz 2012)  
9. European Commission, Montenegro Progress Report, October 2014

Payment of 850 public servants in the Greek National Parliament (300 members) and in the European Parliament (22 members), who worked for the parliamentarians and the political parties and for reelection of the outgoing members of both assemblies has been reported in the past.<sup>10</sup> Distinction should be however made with some situations. A civil servant who is employed as a candidate staff to answer the phone and help with other office duties during his holidays is a volunteer labour and not a contribution. For that service that person is not to be paid.

Rules against abuse of public resources apply in several countries to prevent such risks. In Moldova trustees of candidates who hold public functions may not use public resources for electoral campaigns. In Slovenia pre-election meetings are not allowed in the premises of public entities. French Electoral Code prohibits all public figures and public sector bodies from giving donations or other benefits to a candidate. It is on the supervisory body and for the court considering election issues to assess whether the campaign account report of a given candidate should be rejected, taking into account all the circumstances, and in particular to the value of the benefit, the conditions under which the benefit was acquired, and its amount. For instance, an occasional use of an official vehicle by a candidate given the value, the nature, and the benefit does not justify rejection of the candidate's campaign account report, but use of the entire system of communication within a Town Hall by a Town Hall official running for elections would justify such an outcome.

***Supervisors should check: if state and local public authorities take part in public events organized for electoral campaign purposes and support candidates or political parties with human, financial and material resources; if the civil servants act impartially and independently during the electoral process. If such practices exist, supervisors should recommend implementation of a legal framework preventing the misuse of administrative resources during electoral process.***

### 3.2.3 Third Parties

In Western democracies non-party's campaigners such as campaigning groups, NGO's, associations, and trade unions tend to take part more and more in election campaigns. They may do so for or against political parties or candidates and in relation to campaigns on policies or issues closely linked to a political party or to a candidate. In some countries, like the United Kingdom, third parties are defined by law. They have to be registered and if registered, they may spend money on regulated campaign activity during the election campaigns in order to try to influence voters to vote for or against political parties or candidates. The spending limits on the third parties will depend on which elections they are campaigning in and whether they are registered (for example, if they are registered with the Electoral Commission they will have a higher spending limit). They may organize media events, publish election material, and take part in public events and rallies. Nonetheless, according to the European Court of Human Rights a need to protect e democratic debate and process from distortion by powerful financial groups with advantageous access to

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10. Council of Europe GRECO, Evaluation Report on Greece on Transparency of party funding, Third Evaluation Round, June 2010, Available from: [www.coe.int](http://www.coe.int), Accessed on 1.07.2016

influential media justifies an application of a prohibition of paid political advertising on radio and television on behalf of third parties.<sup>11</sup>

However, in majority of Western countries third parties are not subject to registration and their participation in the public debate may hence give rise to abuse and create an unbalance between political forces in election campaigns. Last parliamentary elections in Estonia (2015) may serve as an interesting example. A foundation for defense of family supported incumbent candidates who voted against a law about same sex partnership and called the voters to vote against those candidates who voted for this law. Estonian legal framework on political finance prohibits donations from legal entities to candidates but in such cases the authors of the expenditures, i.e. the foundation in this case, would be accountable. For the Estonian Police authority the foundation had covered all political parties and therefore this campaign was not considered as campaign advertising.

***Supervisors should verify if third-parties are covered by law and if third-party campaign financing is regulated, particularly when there is a spending ceiling for candidates and parties. If not, supervisors should consider expanding parties' reporting obligations to include contributions to electoral campaigns by third parties.***

### **3.3 Transparency of electoral expenses**

Unlike the United States, spending limits in many member states of the Council of Europe are viewed as limits on incentives for undue influence and corruption of political stakeholders. When electoral funding system has a threshold of electoral expenditures, an excess of electoral expenses above the ceiling raises a few questions related to the definition of these expenses, the volume of the excess, and their scope.

#### **3.3.1 Definition of electoral expenditures**

The nature of the expenses is an important criterion. Where there is a ceiling for electoral expenditures, rules have to define campaign expenditure. Some costs are not automatically electoral expenses. Supervision therefore has to distinguish between electoral expenses which have to be included in candidate's spending's and personal expenses. For instance, make up before a broadcast or computer equipment for personal use shouldn't be counted towards spending limits. Public meetings opened to just party members are not considered as electoral expenses and their exclusion may not necessarily represent an irregularity (e.g. France and the United Kingdom). On the other hand, electoral expenses for primaries opened to any voter should be regarded as electoral expenditures (France).

For example, political advertisements are an important part of electoral expenses when they are permitted. Paying for political advertisements on traditional radio and/or television may be prohibited (France, Ireland, Malta, Spain, and the United

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11. ECHR Animal Defenders International v. the United Kingdom [GC] - 48876/08 Judgment 22.4.2013. Yves-Marie Doublet, *Revue trimestrielle des droits de l'homme*, 2014/483

Kingdom) or limited (Denmark, Sweden, Switzerland). In certain cases, length and frequency of such paid broadcasts is regulated (Bosnia-Herzegovina).<sup>12</sup> Irregularities in this realm have to be reported. When limitations on paid advertising apply, equal opportunity should be given to parties and candidates through free and equal access to broadcast media. If paid advertisements are accepted, equal access and treatment should be granted.

***It falls to supervisors to identify what constitutes electoral expenditures in view of the law and of practice.***

### **3.3.2 The excess of electoral expenditures**

The amount of the excess has to be taken in account when considering sanctions. If the excess is very significant, sanctions may apply. In Austria the conservative party OeVP exceeded the statutory threshold by 4 million € in 2013 parliamentary elections and was fined. In France, an excess of election expenditures for legislative constituencies of 9 % results in disqualification for the candidate. In Belarus on the other hand, an excess of 19 % will not result in disqualification of a candidate running for presidential election, while in Mexico federal and local elections will be annulled if candidates exceeded the ceilings of campaign expenditures by 5 % or more.

When constituencies are of reasonable size (local and parliamentary elections), it is not so difficult to make sure that a candidate did not exceed the ceiling. If the constituency encompasses the entire territory, as for a presidential election, with widespread sources of income and expenses on the whole territory of the country, it will be much more difficult to detect sources of potential fraud. If an excess of expenses is reported, candidates have to inform on the type on the expenditure, its value, and the date when the expenditure occurred.

### **3.3.3 Scope of electoral expenditures**

One of the main tasks of the above-mentioned financial agents is to cover candidate expenditures during the election period. For instance, in the United Kingdom the agent must keep invoices or receipts for any payments made of £ 20 and above. In France, according to electoral judges, the candidate could settle personally 3,6% of the electoral expenses, without having to go through his financial agent.

The scope of the allowed spending is a challenge. In Denmark, Estonia, Finland and Germany no limits are placed by law on the amount a candidate or a political party can spend. In Spain and in the United States there are spending limits for political parties but not for candidates. In France, Iceland, Ireland and Japan, spending limits apply to candidates but not to political parties. Accordingly, financial flows stemming from political parties in the election campaign, particularly at a national level, may reduce the real impact of the spending ceiling for the candidates. When different rules on expenditure ceilings apply, the danger is that they may be used to circumvent the ceiling of expenditures.

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12. The European Platform of Regulatory Authorities, Available from: [www.epra.org](http://www.epra.org)

French political parties were not required to file campaign accounts (except for referendums) until 2016. As a result, neither the French supervision body nor the general public had an overall view of the financial investment of political parties in election campaigns, which naturally limited the scope of the provisions relating to transparency and supervision, since it was not possible to cross-check candidates' and parties' campaign accounts. Since 2016, report on expenses of political parties has to be enclosed to the campaign accounts of candidates for presidential elections.<sup>13</sup>

The election expenditure ceiling may be, on the face of it, respected, but in practice this may imply that other structures close to a party may be taking care of such expenditures. For instance, in 2015 the German Audit Office, which is responsive for scrutinizing the finance of political groups in the Bundestag, revealed that between 1999 and 2006 Bundestag political groups funded 67 actions linked to election campaigns: 28 times on behalf of the SPD, 16 times on behalf of the CDU/CSU, 13 times on behalf of the Greens, and 10 times on behalf of the Liberal party (FDP). Such expenditures made by parliamentary groups are strictly forbidden by the German Act on Political parties.

In 2012, during the French presidential election, Nicolas Sarkozy exceeded the ceiling of expenses for the presidential election by €11 million. The Supervision Committee and the Constitutional Council estimated that he had to include in his campaign accounts costs of public meetings he held as part of his mandate as incumbent president despite the fact that some of them were held before his candidacy. His party covered this excess, but a subsequent investigation revealed that the party itself spent in addition to this amount €13 million for his presidential campaign.<sup>14</sup>

***When limits on expenditures have been set, supervisors have to ensure the effectiveness of these limits and to identify expenditures regarding what counts as an election spending and what does not.***

### 3.3.4 Buying votes

Number of Council of Europe member states prohibit offering or giving money, employment offers, and other types of favors, aimed at getting signatures to support candidates, for voting in favor or against a candidate. These include Albania, Bosnia-Herzegovina, Denmark, Greece, Ireland, Italy, Latvia, Montenegro, Serbia, Sweden, Spain, United Kingdom and Ukraine. Introduction of such a prohibition clarifies the position regarding such practices and facilitate sanctioning.

## 3.4 Disclosure of financial statements

Disclosure of information on funding of candidates and political parties promotes transparency and makes scrutiny easier. It helps supervisors assess to what extent candidates and political parties have complied with the regulations and if their income and expenses have been properly disclosed. It is also a way for candidates

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13. Article 7 of the Institutional Act 2016 - 506, 25 April 2016

14. See case 9.7

and political parties to raise and spend money in a manner acceptable for voters and serves as a deterrent against undue influences.

Supervision has to also ensure that the deadline for publication of financial statements of candidates and political parties is respected. Disclosure is of course not only a matter of meeting a deadline. In order to be able to analyze the content of such financial reports they need to be consolidated in a standardized format and made easily accessible to the public within a given deadline provided for by law. Financial statements may be disclosed on the websites of political parties, in print media or in the official gazettes (Italy), or on the websites of the monitoring bodies (Canada, Estonia, France, and the United Kingdom). These rules have to apply to all political parties and candidates.

An option of several reports submitted at different time exits. For example, in the US, a pre-election report is to be filed by the principal committees of a congressional candidate 12 days before any election in which that candidate takes part; post-election report is released 30 days after the general election; and a quarterly report is to be submitted during an election year. In other calendar years, a quarterly report is to be submitted. In Azerbaijan, parties and candidates have to submit an initial financial report, a second financial report 10 to 20 days prior to the day of elections, and a final financial report 10 days after official publication of the final results at the latest.

The challenge with provisional reports before the official deadline for presentation of the campaign account and a reports published immediately after is the degree of their reliability as such information has not been certified by an auditor. As a rule, campaign account reports being verified by a supervisory body or an electoral court, have to be certified and represent a final accounting document.

Another option is a requirement to publish after the official results of the elections. In the Former Yugoslav Republic of Macedonia, political parties have to submit their reports one day after an election has been officially concluded; in Slovakia within three days, in Belarus within five days, and in Armenia six days after an election. It is very difficult for a candidate or a party, to collect all information related to the funding of an electoral campaign and to get invoices for electoral expenses in such short periods of time and this is likely to reflect on the efficiency of the supervision.<sup>15</sup> Supervisors must be aware of this fact.

***Supervisors have to make sure that the relevant information on election campaign and party funding is disclosed in a timely manner and is easily accessible to the public.***

***A reasonable deadline allows stakeholders to have more time to consolidate data and make reports more accurate.***

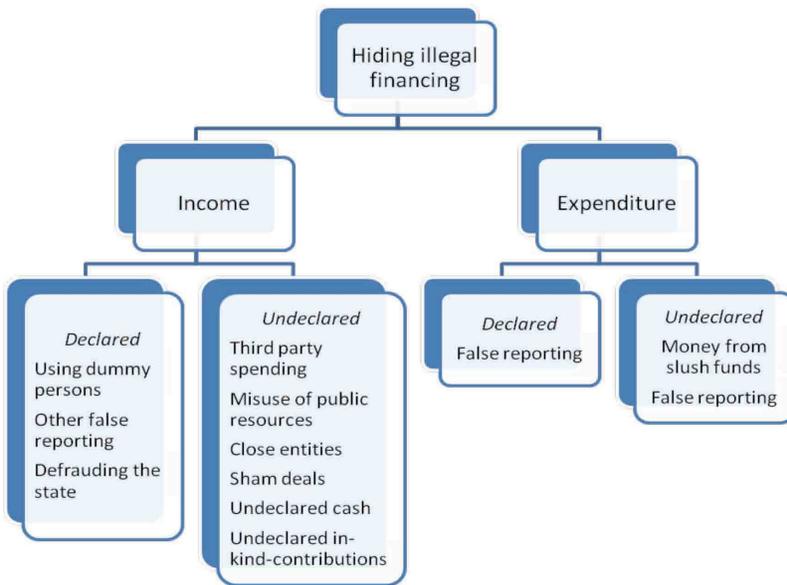
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15. The OSCE/ ODHIR and the Venice Commission recommend the deadline for political party post-election reports should be "no more than 30 days after the elections".



# 4. Hiding irregular financing

Keeping the above issues in mind, analysis of political financing reports should focus, broadly speaking, on two major categories: income and expenditure. From that perspective, the following ways of hiding irregular financing are possible:



There are essentially two ways of hiding irregular funding: a) simply not declaring the income or expenditure, or b) declaring the income or expenditure, but misrepresenting the true origin or destination. This section provides a number of practical examples of each of the four options.

Cash-flow	Shown	Hidden
Declared	Amount	Context
Undeclared	-	Amount, context

**Declared cash-flows:** providing false information about where the money came from or what it was spent on but the amount of cash-flow is properly reported. However, the relevant surrounding circumstances of the declaration are not properly identified (for example, a donation is reported as membership fee or under a different name).

Amount reported?	How is illegality hidden?
Yes	Disguise true background of cash flow

**Undeclared cash-flows:** hiding the fact that extra money is earned or spent in a parallel “shadow” world of political financing which does not appear in any financial report (for example, party money is kept and spent from a secret deposit box for some unreported purpose, such as unauthorised advertising).

Amount reported?	How is illegality hidden?
No	Disguise existence of cash flow as such

The above two ways of hiding illegal financing exist on both sides of the calculation: the income and the expenditures.

In addition, parties might defraud the state of subsidies in order to – illegally – increase their income (e.g. by inflating donations which are matched by state subsidies):

Financing reported?	How is illegality hidden?
Yes	Lying about entitlement to subsidies

## 4.1 Hiding irregular income

There are essentially two ways to hide illegal income when it comes to political financing:

- ▶ **Disguising** the true origin of income: the amount of money received is properly reported, but the information on where it comes from is not correct.
- ▶ **Shadow** income: the income is not reported at all.

Type	Reported?	Amount correct?	Origin true?
Declared	Yes	Yes	No
Undeclared	No	(Yes)	(Yes)

### 4.1.1 Declared income

The amount of income can be fully declared, but can still be illegal. This is the case when the true origin of the income is disguised in the financial report.

This option is chosen whenever the true source of the income or donation makes it illegal, for example:

- ▶ Under political finance laws:
  - The private donor has already reached an annual donation limit;
  - The income source is forbidden in general, such as:
    - Donations from public companies and state entities;
    - Foreign subsidies;
    - Large amounts of cash from unknown sources;
    - Income from business activities; or
    - Donations collected by commercial donation-collectors.
  - The income source is not relevant for calculating state subsidies and is thus reported as income that would not “generate” such subsidies.
- ▶ Under company laws:
  - The donation is a forbidden capital drain; or
  - The donation is not properly approved by the board or shareholders.

- ▶ Under tax laws:
  - The donation stems from untaxed (slush funds); or
  - The donation is used for illegal tax privileges (channelling via tax-privileged charity organisations).
- ▶ Under criminal law:
  - The donation stems from laundered money or other criminal activity; or
  - The donation stems from slush funds and is laundered as small cash-donations into seemingly legal party income.

Even when the true source of the income or donation is not illegal, it can be an attractive option in the following circumstances:

- The donor wants to remain anonymous but the size of donation would require full transparency; or
- An artificial increase in donations (at the expense of other income) would increase the party's claim to state subsidies which are matched with donations (see below at 4.3).

#### 4.1.1.1 Using dummy persons

Dummy persons can be citizens or legal organisations. Both can be used for basically any purpose of disguising the true original of income. The following is an example of the use of a natural person as a dummy:

##### *Example 1*

*In 1999, the owner "C" of a construction company had previously donated €60,000 to the conservative party of the German town Wuppertal. However, in the campaign for mayor's office in Wuppertal, the front-runner was a member of the social democratic party. Therefore, C intended to donate €250,000 to the campaign of the front-runner. He did not want the full donation to be published, possibly in order to not alienate the conservative party. He managed to convince three natural persons to be named as dummy donors of €25,000, €50,000, and €100,000. The remaining €75,000 C donated himself. The local chapter of the social democratic party reported the donations to the party's federal headquarter. According to standard procedures, the auditors of the party contacted the dummy donor of the €100,000 in order to verify this large donation. Eventually, with some adjustments, the donations were registered under two of the dummy donors. After C implemented several construction projects after the election of the front-runner, the donations became subject of a lengthy criminal appeals procedure. However, he was eventually acquitted of bribery in a highly contested case.<sup>16</sup> The party receiving the dummy donations had to pay a fine twice the size of the contested donation.*

16. Final judgment: Federal Supreme Court [Bundesgerichtshof], Decision 3 StR 212/07 of 28 August 2007, Available at <http://lexetius.com>, Accessed on 24 July 2015.

Whenever the donor is a party member, special attention should be paid, as the money could stem from hidden cash donations to the party member, as the following case illustrates:

#### *Example 2*

*Between 1996 and 2002, the chairman of the regional chapter of the liberal party in Germany donated €2.2 million to his party. The party treasurer, who received the donations in cash or in kind, later alleged that he had no doubts that the money stemmed from private funds of the party's chair. The treasurer allocated the money to natural persons and this way camouflaged them as donations. Where the money really came from was never fully investigated, even though the scandal resulted in a criminal investigation on tax evasion and political finance offences against the chairman in 2003. Thirty minutes after the parliament lifted his immunity on 5 June 2003, the party chairman embarked on a private parachute flight that ended with him jumping to death under unclear circumstances. There were suspicions that the money originated back to the many Arab contacts he had fostered during 20 years as chairman of the German-Arab Society and through his consultancy firm specialising in the Middle East.<sup>17</sup>*

Also legal persons can serve as dummies, as illustrated by the alleged facts of this example:<sup>18</sup>

#### *Example 3*

*In 2013, the Conservative Party of Romania notified the National Anti-corruption Directorate (DNA) and the Permanent Electoral Authority that the Hungarian government and several companies owned by the Hungarian State had funded the Hungarian People's Party of Hungarians in Romania with more than three million euros. A number of organisations, associations and foundations are believed to have been doing this to funnel the money from Hungary to the Romanian political party, thus violating declaration requirements as well as the ban on foreign donations.*

The use of dummy persons is indicated by the following non-exhaustive list of factors:

- ▶ An equivalent amount of money flowing from the dummy to the party flows to the dummy within a short period of time;
- ▶ The dummy has not enough means for transferring the sum in question to the party;
- ▶ There is a pattern of cash-flows to the party indicating the use of dummies orchestrated by the same source behind.

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17. The Economist (12 June 2003), A mysterious death – Why did one of Germany's most controversial politicians die?, Available at [www.economist.com](http://www.economist.com), Accessed on 24 July 2015.

18. Amos News (18 April 2013), PC and DNA alerted SRI concerning illegal financing of the Hungarian People's Party of Romania, [PC a sesizat DNA și SRI cu privire la finanțarea ilegală a Partidului Popular al Maghiarilor din România], Available at [www.amosnews.ro](http://www.amosnews.ro), Accessed on 24 July 2015.

### 4.1.1.2 Other false reporting

Examples of other forms of false reporting include:

- ▶ Illegal large cash donations are broken down into several small (“legal”) cash donations;
- ▶ Forbidden donations (for example foreign subsidies) are reported as legal donations (for example business revenue);
- ▶ Donations are reported as revenue.

One form of false reporting is the defrauding of state subsidies presented below (see 4.3), whenever the financial report is the basis for receiving state subsidies.

The following is an example of possible donations reported as revenue:

#### *Example 4*

*One party in Germany offered to corporate sponsors a package consisting of renting an exhibition booth at the annual party congress (€14,000) and a private meeting with the region's prime minister (€6,000). Some of the most prominent law professors on political finance argued that there was no real service by the party for the money so that it had to be reported as a donation in the financial reports. If that is true, that party's financial report would be wrong as it did not list the purchase payments as donations. The federal oversight body did not see a discrepancy, though, between the package and the money paid. Still, the President of the German Parliament called this practice of members of his own party “incredibly stupid”<sup>19</sup>*

#### *Example 5*

*In 1983, the regional chapter of Hesse of the conservative party in Germany transferred €10 million to Switzerland. The party wanted to prohibit this money from becoming visible to the public under new political finance legislation coming into force. The money was put into bonds and the revenue from interest channelled back to Germany via a charity trust. The political party falsely declared them as “other income” and as “inheritances from Jewish citizens”<sup>20</sup>*

An example of a possible foreign (cash) subsidy which is instead reported as a domestic donation is included in Example 2 at chapter .

### 4.1.1.3 Defrauding the state

In this pattern, the money is reported, and it is clear where it comes from; however, it is obtained by fraud from the state. The basis for allocating state subsidies is normally the financial report of a political party. In order to obtain more funding than entitled

19. German Parliament (25 March 2010), News release, Available at [www.bundestag.de](http://www.bundestag.de), Accessed on 24 July 2015.

20. Administrative Court Berlin, Decision 2 A 25/00 of 31 January 2001 (not final).

legally, some numbers in the financial report need to be tuned. In this sense, defrauding the state of subsidies is actually a subcategory of false reporting (see above at ).

Type	Reported?	Amount true?	Origin true?	Defrauded?
Disguise origin	Yes	Yes	<b>No</b>	No
Shadow income	<b>No</b>	(Yes)	(Yes)	No
Defrauding the State	Yes	Yes	Yes	<b>Yes</b>

How do political parties defraud the state of money? The patterns will vary from country to country depending on which basis the subsidy is calculated:

- ▶ Political finance laws might limit subsidies to the equivalent total amount the party is receiving from private funding. In this case, the party would have an interest, for example, to declare income from its business as donations and thus raise the limit of its state funding.
- ▶ “Matching subsidy” mechanism. Under this system, private donations raised by parties would be matched by subsidies from the state up to: a) a certain size of donations; and b) a certain maximum total subsidy per party.

#### Example 6

*In 1996 and 1997, the German right-wing party “NPD” was issuing fake receipts for donations that it never received. The staged donations amounted to between 6-10% of its total of received donations. Thus, it managed to apply for and receive higher state subsidies in 1997 and 1998, which by law match private donations. In 2006, the oversight body investigated the irregularities and claimed back all state subsidies for both years (€870,000). As a consequence, the NPD had to dismiss its entire full-time staff.<sup>21</sup> The case was triggered by a criminal investigation against the party’s treasurer. After the police looked into allegations that the treasurer had embezzled €740,000 from party funds, they discovered in confiscated party records that he had issued fake receipts for years.<sup>22</sup>*

#### Example 7

*In 1999, the Chair of a local chapter of the conservative party in Germany accepted anonymous donations of €33,000. He intentionally misstated in the financial report that the money was from anonymous sources. The Federal Supreme Court clarified in 2011, that the Chair had committed all elements of crime offence of embezzlement and fraud, but questioned the existence of damage for the party. The case is currently being retried at first instance.<sup>23</sup>*

21. N24 (4 April 2013), Shortage of money forces NPD to dismiss staff [Geldnot zwingt NPD zu Entlassungen], Available at [www.n24.de](http://www.n24.de), Accessed on 24 July 2015.

22. PNN (18 September 2008), Convicted treasurer leaves NPD, [Verurteilter Ex-Schatzmeister kehrt der NPD den Rücken], Available at [www.pnn.de](http://www.pnn.de), Accessed on 24 July 2015.

23. German Supreme Court, Decision 1 StR 94/10 of 13 April 2011, Available at <http://openjur.de>, Accessed on 24 July 2015.

## 4.1.2 Undeclared income

In this scenario, income is not declared for the same reasons as disguising the true origin of declared income (.). In addition, undeclared “shadow” income is an interesting option from the perspective of spending:

- ▶ Shadow income can be used to orchestrate internal party power through a war chest;
- ▶ Shadow income can be used for other discreet, possibly illegal spending purposes.

### 4.1.2.1 Third party spending

Third party spending is any unreported coverage of a party’s or a candidate’s expenses. It can be for one of the following party or campaign expenses:

- ▶ Opinion polls and other market research;
- ▶ Communication services (mailing, design, strategy, billboards, airtime, etc.);
- ▶ Renting offices or campaign space;
- ▶ Human resources;
- ▶ Purchasing or renting campaign and office equipment;
- ▶ Utilities (electricity, water, heating); and
- ▶ Transportation and accommodation.

#### *Example 8*

*In preparation of the 1998 national elections, the chairman of the regional liberal party contracted a communications company to put up 531 placard boards showing politicians of his party. Both sides agreed on a service fee of €175,000. The fee was paid from an account in Lichtenstein controlled by the party’s chair.<sup>24</sup> The source of money on this account is unknown. There were several more payments covering these type of expenses (for printing flyers, publishing ads, etc.) that, eventually, the political finance oversight body in Germany reclaimed about €3.5 Million in state subsidies from the liberal party.*

Restricting third party spending might conflict with free speech as, for example, in the Phyllis Bowman case before the European Court of Human Rights:

#### *Example 9*

*Mrs Phyllis Bowman is the executive director of the Society for the Protection of the Unborn Child (“SPUC”). In the period immediately before the parliamentary elections in April 1992, Mrs Bowman arranged to have some 1.5 million*

24. Administrative Court of Appeals Berlin Brandenburg, Judgement OVG 3a B 2.11 of 28 November 2011, Available at <http://openjur.de>, Accessed on 24 July 2015.

leaflets distributed in constituencies throughout the United Kingdom, including, in the constituency of Halifax, 25,000 copies of a leaflet which read as follows:

*“We are not telling you how to vote, but it is essential for you to check on Candidates’ voting intentions on abortion and on the use of the human embryo as a guinea-pig”.*

*Terry Martin, Conservative.*

*Mr Martin has publicly declared his firm commitment to defending the unborn child. If elected, he would vote to tighten the grounds for abortion to stop abortion on demand. He would vote to stop abortion after 24 weeks, as the law currently allows abortion up to birth for handicapped babies and on other grounds. Would vote to stop the creation and use of human embryos as guinea-pigs for drug testing.*

*Alison Mahon, Labour.*

*Mrs Mahon is a leading pro-abortionist. As an MP she voted to allow abortion up to birth for handicapped babies. She voted for the compulsory enrolment on a published register of doctors with a conscientious objection to abortion despite warnings that it could be used as a blacklist. She also voted to allow human embryos to be used as guinea-pigs in programmes including the testing of drugs and other experiments. [...]*

#### *THE SOCIETY FOR THE PROTECTION OF THE UNBORN CHILD”*

*On the reverse side of the leaflet, together with a picture marked “an unborn baby ten weeks after conception”, was printed a description of the first weeks of life of an unborn child.*

*Mrs Bowman was charged with an offence under the Representation of the People Act 1983 (“the 1983 Act”), which prohibits expenditure of more than five pounds sterling (“GBP”) by an unauthorised person during the period before an election on conveying information to electors with a view to promoting or procuring the election of a candidate. The ECtHR ruled that her conviction violated her right to free speech under Article 10 of the Convention.<sup>25</sup>*

Third party expenses might also, in some circumstances, include (possibly legal) use of publically controlled funds, in other words, social security benefits:

#### *Example 10*

*Following a monetary sanction for illegal financing, the German right-wing party “NPD” had to dismiss its entire full-time staff in 2009.<sup>26</sup> The (former) staff applied for unemployed benefits from the social security agency and allegedly continued to work for the political party on a “pro bono” basis.*

25. ECtHR, Decision in *Bowman v. The United Kingdom*, 24839/94, 19 February 1998, Available at <http://hudoc.echr.coe.int>, Accessed on 24 July 2015.

Sometimes the line between third party and undeclared cash can become very fine:

#### *Example 11*

*After a trial lasting three and a half years, a court ruled that the former Prime Minister of Romania, Mr Năstase, illegally raised €1.6m (\$2.1m) during his 2004 election campaign, when he ran for president. The case, nicknamed “The Quality Trophy”, refers to a conference organised by a state agency at which companies and institutions donated money. From here, the money went further to a company providing various services in the presidential campaign of the Social Democrat leader.<sup>27</sup> One could argue in this case that the services from the company are third party spending; or, one could argue that the money was under party control from the very beginning and thus undeclared income.*

#### 4.1.2.2 Misuse of public resources

Incumbent candidates and parties have a natural and unavoidable advantage over challenging candidates. However, as noted in the previous section, if they use state funds or resources to the advantage of their own party or campaign, this constitutes income. As it is generally forbidden, it is normally not found in financial reports. Among the public resources abused are:

- ▶ Office space;
- ▶ Office equipment;
- ▶ Transportation;
- ▶ Staff;
- ▶ State media.

#### *Example 12*

*President Clinton was accused, in 1997, of having converted the White House into a roadhouse for campaign contributors. According to a list released by the White House, 938 guests stayed overnight in “The Lincoln bedroom”. They had contributed \$10,176,840 to the Democratic Party, an average of \$10,849, although many gave nothing. Guests reported that the mattress was lumpy, but the ambiance was tough to beat. The White House argued all along that the rich donors who stayed the night, were there as Clinton friends, not as contributors.<sup>28</sup>*

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26. N24 (4 April 2013), Shortage of money forces NPD to dismiss staff [Geldnot zwingt NPD zu Entlassungen], Available at [www.n24.de](http://www.n24.de), Accessed on 24 July 2015.

27. The Economist (21 June 2012), A bloody sentence, Available at [www.economist.com](http://www.economist.com), Accessed on 24 July 2015.

28. New York Times (19 July 1998), Lincoln Bedroom, Still Open, Available at [www.nytimes.com](http://www.nytimes.com), Accessed on 24 July 2015.

### Example 13

*Between 2006 and 2008, the Bavarian government (under the conservative party) financed a so-called "Feedback-Study". The Study of 2007, for example, contained the recommendation, to focus the political contest on the social democratic and green parties. The three Studies cost the government €108,000, and were not declared in the conservative's party financial report.<sup>29</sup> The Bavarian Court of Auditors investigated the matter and concluded that since 2000 the government had commissioned surveys for a total of €558,302.51. The Court stated: "Questions of political parties are not a matter of the government and must not be subject of surveys commissioned by the government. Such activities are of the responsibility and at the expense of political parties."<sup>30</sup>*

### 4.1.2.3 Close entities

Similarly, as discussed in the previous section, under this pattern, money or other resources are moved from entities closed to political parties or campaign candidates. This concerns mainly:

- ▶ Political youth organisations;
- ▶ Political foundations;
- ▶ Parliamentary groups.

### Example 14

*Parliamentary groups in Germany receive public funding for their work. It is forbidden to use the money for any other purpose, such as for party expenditures. In May 2001, two parliamentary groups of a regional parliament engaged in a public mud fight.<sup>31</sup> A half-page ad in a newspaper by the parliamentary group of the conservative party reminded the prime minister of the social democratic party that he had no "right to laziness" given the "brain-drain, poor education, and youth unemployment" in the region. The parliamentary group of the social democrats answered with a counter-ad, describing the conservatives as "ignorant and complacent", characterised by "political finance scandals" and by "dead birds in parliament". Finally, the prosecutor intervened by notifying both factions that he investigated them for embezzlement of public funds: in his view, the ads were paid by funds of the parliamentary group, but were in fact financing a political campaign of the respective political parties.*

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29. Merkur (4 August 2010), Heavy accusations against CDU party: using tax money for campaigns [Schwere Vorwürfe gegen CSU: Steuergelder für Wahlkampf benutzt], Available at [www.merkur-online.de](http://www.merkur-online.de), Accessed on 24 July 2015.

30. Bavarian Court of Auditors (January 2011), Expertise contracts by the governor's office for surveying public opinion [Gutachtens- und Beratungsaufträge der Staatskanzlei zur Erforschung der öffentlichen Meinung], Available at [www.orh.bayern.de](http://www.orh.bayern.de), Accessed on 24 July 2015.

31. Focus (22 April 2002), United in fighting [Vereint im Streit], Available at [www.focus.de](http://www.focus.de), Accessed on 24 July 2015.

*The case never proceeded any further, as the parliament refused to lift immunity of the deputies in question, making it one of the unfortunate incidents where German parliamentarians abused their immunity.<sup>32</sup>*

#### *Example 15*

*Political foundations are a “popular” target of donations. In 1986, the Final Report of the Inquiry Committee on illegal donations in Germany came to the following conclusions: between 1975 and 1980 the Flick-Holding paid €1.4 Million to the Friedrich-Ebert-Foundation (of the social democratic party). In the years before almost no donations are recorded. The increase in donations since about 1975 can only be explained with tax favours provided by the government (of social democrats) to the Flick-Holding between 1975 and 1980.<sup>33</sup>*

There are many ways as to how political foundations can spend money for other party purposes:

- ▶ Human resources;
- ▶ Expertise;
- ▶ Research;
- ▶ Organisation of conferences and workshops;
- ▶ Office equipment;
- ▶ Libraries and archives.

#### *Example 16*

*The German liberal party sold its archive to its political foundation. In addition to the €200,000 as price money it saved the money for subsistence of the archive, but kept the same access to all the archived data.<sup>34</sup>*

### 4.1.2.4 Sham deals

Sham deals are used to give income a legal appearance. The income can be:

- ▶ Cash from natural or legal persons (see below example 9);
- ▶ Cash from illegal activities, for example tax evasion by corporations;
- ▶ Cash from illegal sources, for example foreign entities.

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32. Hoppe T. (2011), Public Corruption: Limiting Criminal Immunity of Legislative, Executive and Judicial Officials in Europe, 5 Vienna Journal on International Constitutional Law 2011, 538, Available at <http://tilman-hoppe.de>, Accessed on 24 July 2015.

33. German Parliament, Document BT Drs. 10/5079, page 275 (no. 430).

34. Die Zeit (4 February 1983), Green Party suing [Die Klage der Grünen], Available at [www.zeit.de](http://www.zeit.de), Accessed on 24 July 2015.

*Example 17 (see the Flick-scandal Example 15)*

*In the 70s, the German conservative party held a subsidiary company in the “tax haven” Lichtenstein, called “European Business Consultancy Institute”. A German corporation orders an expertise at Institute for a fee of €75,000. Both sides agree that the expertise is not really needed, so that neither timely delivery nor exactness of the expertise is the matter. In addition, the expertise has already been sold several times to other companies. The fee flows to the conservative party. The case comes to light, when tax authorities audit the corporation and become suspicious of the deal.<sup>35</sup>*

Sham deals are not always concluded directly with the political party as a contractor. This is, for example, the case for third party spending:

*Example 18*

*During regional elections campaigns in Germany in 2000, a company A invoiced €35,000 to a company B, which was owned by the chairman of the liberal party. The invoice was for an “Expertise on mid- and long-term shift of oil and gas in the energy mix of OECD-countries, geostrategic impact and security policy consequences”. Such an expertise was never drafted. Instead, the money was paid as a salary to a campaign manager for the liberal party.<sup>36</sup> The head of company A was later convicted of embezzling money from company A.<sup>37</sup> The chairman of the liberal party could not be brought to trial as he died after what appeared to be a suicide following the discovery of the scandal.*

#### 4.1.2.5 Undeclared cash

Instead of trying to introduce the cash-flow in the report under the flag of legal income, it is subject to a second, secret bookkeeping. Undeclared cash regularly comes from the following sources:

- ▶ Cash from natural or legal persons;
- ▶ Cash from illegal activities, for example tax evasion by corporations (see below Example 10);
- ▶ Cash from illegal sources, for example foreign entities (see below Example 11).

*Example 19 (see the Flick-scandal Examples 15 and 17)*

*A tax privileged German charity organisation called “State Citizens Associated – SV” collected money from the corporation R. By donating the money to SV, R received a tax benefit it would not have generated if it had donated the money to a political*

35. Bundestag Document BT-Drs. 10/5079, page 71.

36. Administrative Court of Appeals Berlin Brandenburg, Judgment of 28 November 2011, OVG 3a B 2.11, Available at <http://openjur.de>, Accessed on 24 July 2015.

37. District Court Düsseldorf, 28 June 2006, 80 Js 735/03.

party. A small part of the money was used to cover administrative costs of the SV and to donate some money to charity causes in order to fabricate a pro bono cause of SV for the tax authorities. The money flowed from SV to Swiss and Lichtenstein accounts. In Switzerland and Lichtenstein, the treasurer of the conservative party withdrew the money and brought it back to Germany in a suitcase full of cash. There, he deposited it into a variety of party accounts. Representatives of R claimed in the ensuing criminal trials alleged that they did not know that SV – as a dummy person – was channelling the money to the conservative party. In 1986, the court rejected this version as unrealistic.<sup>38</sup>

### Example 20

A scandal began 1999 in Germany with the emergence of a series of undeclared contributions given to Helmut Kohl's Christian Democrat party, the CDU, by arms dealer Karlheinz Schreiber when Mr Kohl was German chancellor.<sup>39</sup> Mr Kohl admitted that he ran a network of secret CDU accounts containing a stash of anonymous donations controlled by a former party official nicknamed "the Postman".

According to German law, political donations of more 10,000 € must be declared, while this funding scandal involves millions of dollars' worth of secretly donated funds. Mr Kohl repeatedly refused to name any of the secret donors, saying he could not break the promises he made to them. The most serious allegation was that the donations were kept secret because they influenced key government decisions. In January, auditors investigating the finances of the CDU said that they had failed to trace the origin of nearly \$6m paid to the party in secret campaign donations. German company law does not foresee publication of donations in company's annual reports to shareholders. The political finance oversight body, the Parliament, ordered the party to pay back about \$21m in state financing as punishment for flouting the country's strict political funding rules. The CDU was also fined \$3m. German media reported that former French President Francois Mitterrand arranged payments of about DM 30m (\$15.7m) to the CDU, through a French oil company in order to secure investments in Eastern Germany. Mr Kohl admitted receiving himself about \$1m in secret donations, but denied corruption. Party functionaries could not be punished for the fraudulent accounting, as there were no equivalent penal provisions back then. As a consequence, penal provisions were introduced into German political finance laws.

In the following years, German criminal courts of different instances and in different trials concerning different aspects of the scandal took differing views as to whether party executives committed embezzlement by accepting secret donations and running a secret bookkeeping system. The Court of Appeals of Frankfurt took

38. District Court Hamburg Decision 17/85 of 6 March 1986.

39. BBC (29 June 2000), Q&A: Germany's party funding scandal, Available at <http://news.bbc.co.uk>, Accessed on 24 July 2015.

*the position that the secret administration of cash was embezzlement if it entailed additional costs for the party, if competent party organs could not disburse the money, or if the secret cash-system caused the risk of monetary sanctions to the party.<sup>40</sup> The prosecutor terminated the criminal procedure against Mr Kohl in exchange for a quasi-fine payment by Mr Kohl of 300.000 DM (€150.000).<sup>41</sup> The court, which approved the termination, pointed to the unclear legal situation.*

#### *Example 21*

*As a consequence of the Flick-scandal in the 70s (see above Example 15 and 17), the treasurer of the social democratic party in Germany had accumulated millions of cash money for the party. After the scandal came to light, and the treasurer had died in 1983, the party did know anything other than to report the money as a donation of the treasurer to the party.<sup>42</sup>*

#### *Example 22*

*In October 2011, the Croatian State Attorney's Office for the Suppression of Corruption and Organised Crime (USKOK) for the first time opened an investigation into a political party. The Democratic Union (HDZ) is accused of funnelling money from public companies to a slush fund between 2003 and 2009.<sup>43</sup> The slush fund is reported to amount up to a total of €9.3 million, money that was siphoned off from state-owned companies.<sup>44</sup>*

### 4.1.2.6 Undeclared in-kind-contributions

AS noted above, in-kind-contributions can be any of the following:

- ▶ Free media time;
- ▶ Offices, staff, transportation, communication, energy etc.;
- ▶ Property (IT, vehicles, etc.).

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40. Appeals Court Frankfurt a.M., Decision 3 Ws 1106/02 of 12 January 2004.

41. District Court Bonn 27 AR 2/01 of 28 February 2001.

42. German Parliament, Document BT-Drs. 10/5079, page 276.

43. Freedom House, Country Report Croatia 2012, Available at [www.freedomhouse.org](http://www.freedomhouse.org), Accessed on 24 July 2015.

44. BNE (23 March 2012), Croatia gears up for landmark graft case, Available at [www.bne.eu](http://www.bne.eu), Accessed on 24 July 2015.

### *Example 23*

*In the 2013 national elections in Germany, the contender Peer Steinbrück of Chancellor Merkel received support by an internet-blog created solely to support his campaign. The blog is created by six businessmen each allegedly donating a five digit sum to the blog. The oversight body for political financing has started an investigation into the matter. For the outcome, it will be decisive whether the blog is an independent media body, or a one-sided campaign vehicle. The question is delicate as it touches on the constitutional right of free press.<sup>45</sup>*

### *Example 24 (see above example 18)*

*During regional elections campaigns in Germany in 2000, a company paid a campaign manager for the liberal party.<sup>46</sup>*

### *Example 25*

*The parliamentary staff of lawmakers in Germany is paid by state subsidiaries to lawmakers and to parliamentary groups. By law, the subsidies may only be used for parliamentary purposes. However, the parliamentary staff is in reality the “organisational backbone of political parties“, according to political scientists.<sup>47</sup>*

### *Example 26*

*The right-wing party “NPD” is currently under investigation for in-kind contributions from its group in parliament. Allegedly, the parliamentary group was financing public relation expenditures of the party. The case is still under investigation.<sup>48</sup>*

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45. Wiwo (6 February 2013), Suspicion on hidden party financing [Verdacht auf verdeckte Parteienfinanzierung], Available at [www.wiwo.de](http://www.wiwo.de), Accessed on 24 July 2015.

46. Administrative Court of Appeals Berlin Brandenburg, Judgment OVG 3a B 2.11 of 28 November 2011, Available at <http://openjur.de>, Accessed on 24 July 2015.

47. Tagesspiegel (1 July 2012), Unconstitutional [Ein Verstoß gegen das Grundgesetz], Available at [www.tagesspiegel.de](http://www.tagesspiegel.de), Accessed on 24 July 2015.

48. Die Welt (20 November 2014), Parliament and Party NPD fight about money at Constitutional Court [Landtag und NPD streiten vor Landesverfassungsgericht um Geld], Available at [www.welt.de](http://www.welt.de), Accessed on 24 July 2015.

## 4.2 Hiding illegal expenditures

There are basically two types of hiding expenditures in political finance:

- ▶ **Disguising** the true object of the expense: the amount of money spent is properly reported, but the information on what it is spent is not correct.
- ▶ **Shadow** spending: the spending is not reported at all.

Type	Reported?	Amount true?	Object true?
Disguise object	Yes	Yes	<b>No</b>
Shadow expense	<b>No</b>	(Yes)	(Yes)

### 4.2.1 Declared spending

The amount of expenditures can be fully declared, but the expenditure can still be inappropriate. This is the case when the true object of the expenditures is disguised in the financial report.

This option is chosen whenever the expense is in fact illegal, in particular:

- ▶ **Under political finance laws:**
  - Spending limits have been already reached (as for example under Armenian Law, see above);
  - The expenditure constitutes an improper use of state subsidies or party funds;
- ▶ **Under criminal law:**
  - The expenditure constitutes embezzlement, as competent party organs did not sanction it.

#### Example 27

*The governor of the Italian region of Lazio resigned in 2012 amid a scandal over the alleged embezzlement of public funds for his political party, which were reportedly used to buy cars, holidays and expensive dinners.<sup>49</sup> Franco Fiorito, a former top official of Berlusconi's Freedom People party in Lazio, is prosecuted on suspicion of embezzling €1.3 million in public funds granted to his political party and declaring the expenditures as expense claims to the party's accounts. The prosecution has pled for a five-year imprisonment term and a life-long debarment from public office.<sup>50</sup>*

#### Example 28

*The Mayor of Toronto (Canada), Rob Ford, is suspected of having exceeded the legal spending limit in his 2010 campaign for office. According to an auditing report, the campaign exceeded the \$1.3-million spending limit by \$40,168, or about 3 per cent. The complaint against Ford was filed in 2011 by two citizens, one lawyer,*

49. The Guardian (25 September 2012), Lazio governor resigns amid scandal, Available at [www.guardian.co.uk](http://www.guardian.co.uk), Accessed on 24 July 2015.

50. La Gazzetta Del Mezzogiorno (20 March 2013), Politician at center of Lazio funds scandal risks 5 years, Available at [www.lagazzettadelmezzogiorno.it](http://www.lagazzettadelmezzogiorno.it), Accessed on 24 July 2015.

*and one left-leaning activist and former vice-chair of the library board. They now lead a group called Fair Elections Toronto. Rob Ford's response to the allegations has changed over time. He first said he had "nothing to hide" and did not plan to appeal the decision by the city's compliance audit committee to order an audit (the committee is composed of three non-politician experts). He then filed an appeal; his lawyer argued he had not broken the law. Finally, in April, he withdrew the appeal and softened his position, saying in a statement that "everything during the campaign was done in good faith with the intention of complying fully with election law."<sup>51</sup>*

#### **4.2.2 Undeclared spending**

Expenditures are not declared for the same reasons as in the case where the true object of the expenditures is disguised (). Apart from this, undeclared "shadow" expenditures are simply the "natural" consequence of undeclared income. As undeclared income is kept in shadow bookkeeping, it also has to be spent outside official channels.

##### *Example 29*

*As a mirror image to the illegal income generated by Helmut Kohl's Christian Democrat party in the 1990s (see above Example 20), the money was also spent on undeclared purposes. The money was used for example for financing a mailing campaign to all party members costing €400,000 in 1988. The final report of the parliament's inquiry committee on the scandal lists for example the following undeclared expenses from the party slush funds (1 DM equaling about 0.5 €):*

*"Campaign costs, 1996, regional chapter Rheinland-Pfalz 75,325 DM*

*Campaign costs, 1996, regional chapter Schleswig-Holstein 89,182 DM*

*Campaign costs, 1994, regional chapter Saarland 33,330 DM*

*Campaign costs, 1996, regional chapter Schleswig-Holstein 126,881 DM*

*Campaign costs, 1994, regional chapter Mecklenburg-Vorpommern 147.200 DM*

*12 Posters, 1994, invoice to federal headquarter, 81.506 DM*

*Campaign costs, 1996, regional chapter Rheinland-Pfalz 70.725 DM*

*Campaign costs, 1996, regional chapter Schleswig-Holstein 89.700 DM [...]*

*Unclear purpose of the following cash-withdrawals:*

*07.03.1989, 100.000 DM*

*30.04.1989, 130.000 DM*

*24.07.1990, 50.000 DM*

*24.07.1990, 100.000 DM*

*05.10.1990, 600.000 DM<sup>52</sup>*

51. The Star (1 February 2013), Mayor Rob Ford exceeded election spending limit, audit suggests, Available at [www.thestar.com](http://www.thestar.com), Accessed on 24 July 2015.

52. Bundestag Document BT-Drs. 14/9300, page 132.



# 5. Red flags

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The following is a list of factors that indicate a possible violation of political finance regulation. It should regularly cause an oversight body to look more deeply into the financing of the concerned party of the candidate. There are two kinds of red flags:

- ▶ Implicit red flags: a particularity in a case that would compel an attentive observer to assume a possible irregularity, for example, a contradiction in a financial report.
- ▶ Explicit red flags: a direct allegation of a wrongdoing, for example, a media report alleging the use of dummy persons for donations.

## 5.1 Implicit red flags

### 5.1.1 Red flags in financial reports

Financial reports by political parties, by candidates, parliamentary groups, or lawmakers often already contain first indications of illegal cash-flows. However, one should keep in mind that they can mostly only show cases where the true origin of income or the true object of spending is disguised (see above and ). The whole world of shadow income and spending takes place outside financial reports and is mostly related to red flags outside financial reports (see below ).

#### 5.1.1.1 Income

On the income side of financial reports, the following are common examples of red flags for hidden illegal financing:

Membership fees:

- ▶ A shift of amount from the line for membership fees to the line of donations (indication for tuned up donations to be matched with state subsidies).
- ▶ Unusual high total of donations from natural persons (indicating tuned up donations to be matched with state subsidies).
- ▶ Donations from different branches of a corporation that altogether would reach a donation, reporting, or publication limit.

Donations (financial data):

- ▶ A high amount of cash transactions.
- ▶ There are sudden surges in the amount and/or number of donations immediately preceding the election, with a number of people typically making donations close to the legal limit.<sup>53</sup>
- ▶ Donations from party members (indicating tuned up donations to be matched with state subsidies).
- ▶ Same particular amount of donation by different donors at the same day.

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53. Reed Q. (2005), Open Society Institute, Monitoring Election Campaign Finance – A Handbook for NGOs, page 91, Available at [www.opensocietyfoundations.org](http://www.opensocietyfoundations.org), Accessed on 24 July 2015.

### Donations (personal data contained in the annex to the financial report):

- ▶ A high number of natural persons donating the same amount of money just below the publication threshold (possible indication for dummy persons).
- ▶ Individuals who donate large amounts of money but do not have the appearance of corresponding wealth.<sup>54</sup>
- ▶ Companies that, based on their revenue, profits, paid taxes, and tax liabilities, did not appear likely to possess the funds to donate to a political party.<sup>55</sup>
- ▶ Connections among different individual donors, as well as among individual and corporate donors.<sup>56</sup>
- ▶ Politician: donating himself (sign for shadow income/cash donations from his side).
- ▶ Donations by charitable organisations (possible indication for a donor abusing the tax privilege of the charity by channelling the donation through the organisation).
- ▶ A party member donating money (possible indication for cash donations of third parties to the party member falsely declared as donation by the party member).
- ▶ Frequent donations interconnecting by amount, date, address, etc.
- ▶ The appearance of many senior employees of the same corporation among the donors to a specific party may indicate that salaries have been increased to create room for a “routed” corporate donation.
- ▶ Legally separate companies donate and are economically controlled by one entity.

### Business revenue:

- ▶ Income from typical sham deals (consultancy contracts, expertise, etc.).
- ▶ Income from highly profitable businesses with little or no registration, tax or auditing regime (as an “easy” pretext for other undeclared income).
- ▶ High revenues from business with typically low profits (e.g. selling flowers, collecting mushrooms in the forest, etc.).

### State subsidies:

- ▶ A rise in donations leading to a rise in subsidies.
- ▶ A rise in the number of members or membership fees leading to a rise in subsidies.

### Other income:

- ▶ “Income from inheritances” is sometimes a disguise for income from other undeclared sources
- ▶ Campaign spending of a party that appeared on the political scene just a few months prior to the elections and that is comparable to that of more established parties, raising questions regarding the rapid acquisition of significant funds.<sup>57</sup>

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54. Ibid.

55. Ibid.

56. Ibid.

57. Ibid.

- ▶ Alienation of assets considerably above acquisition price.
- ▶ Windfalls (any income without quid pro quo: casino or gamble wins, gifts, inheritances, etc.).
- ▶ Considerable increase in income from one financial report to another (which is not due to a compelling reason, such as an increase in state subsidies based on election results).

### 5.1.1.2 Expenditures

On the expenditure side of financial reports, the following are common examples of red flags for hidden illegal financing:

- ▶ Suspiciously low levels of overall expenses.
- ▶ Expenditures just below spending limits.
- ▶ Unusually high expenditures in certain categories, for example personal expenses of party members for travelling etc. (possibly used for other purposes than declared).
- ▶ Expenses below market conditions (low service fees, office rents, etc.), indicating undeclared in-kind income.
- ▶ Loans disbursed without compelling reasons (indicating a possible disguise for expenditure).
- ▶ A considerable increase in expenditures from one declaration to another.

### 5.1.1.3 Relation of income and expenditures

The relation of income and expenditures can also be an indicator for hidden illegal financing:

- ▶ If the spending exceeds declared income, this is a clear indication that parties are concealing income or failing to report it accurately.
- ▶ Implausible balance of income and expenditures: more or less all income is spent on campaign expenses, leaving no room for necessary daily expenses of a political party (party offices etc.), indicating hidden income and expenditures for subsistence.

### 5.1.1.4 Assets/liabilities

In the assets/liabilities sheet of a financial report, the following factors are examples of possible red flags:

- ▶ A considerable increase in assets from one declaration to another without compelling explanation.
- ▶ Unusual/excessive loans received (being donations under the flag of a loan).
- ▶ Unpaid liabilities remaining for a longer period of time indicating a de facto donation (waiver of liability).
- ▶ Asset deals with close entities (political foundations), especially if done under favourable conditions, indicating undeclared in-kind income.

## 5.1.2 Red flags outside financial reports

- ▶ Tax offences by third parties in connection with donations.
- ▶ Incidents of embezzlement at a political party, which are normally covered up by falsified bookkeeping, raising the probability of other irregularities in accounting.
- ▶ Unusually high amount of advertising expenditure obviously exceeding declared income or declared expenses.
- ▶ Donors providing suspiciously similar explanations when asked about their donations.
- ▶ Donors, when asked by the oversight body in interviews, make note of the questions with the probable intention of informing other possible dummy donors on what they will expect as questions.
- ▶ Connections between party members and charities/NGOs.

## 5.2 Explicit red flags

### 5.2.1 Open and anonymous complaints

Any open complaint (i.e. the complainant revealing his/her identity) that is not obviously arbitrary or abusive should trigger an investigation.

Anonymous complaints generally carry the risk of being abused for intentionally harming people, for example political competitors. However, unlike a criminal investigation, an audit into a financial report is nothing an honest political party or candidate has to be afraid of. In addition, an audit might take place without the party or the public getting notice of it; thus, there is little if any disadvantage to the party from a full audit.

From the perspective of law enforcement though, anonymous complaints are often the most useful and successful resource for uncovering irregularities. Therefore, international standards on whistleblowers recommend the “availability of anonymous reporting”.<sup>58</sup> As a consequence, anonymous complaints that are not obviously arbitrary or abusive should be included as a trigger for a full audit.

### 5.2.2 Media reports

Media reports are in fact a major source of information for political finance oversight bodies. Investigative journalists often have informal access to data that would – legally – not be available to the oversight body. In addition, media reports are often launched from inside the political sphere with the aim of eliminating competitors. As tax evasion of natural persons is often reported by estranged family members, so is illegal political finance often reported – via the press – by estranged political partners.

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58. G20/OECD (2011), Compendium on Protection of Whistleblowers, Recommendation 3, p. 31, Available at [www.oecd.org](http://www.oecd.org), Accessed on 24 July 2015.

*Example 30 (see already Example 8)*

*On 30 October 2002, one month after national elections, the press published a report on an alleged financing scandal at the liberal party in Germany. The political party launched an internal audit, complemented by an external audit by the oversight body for political finance at the parliament's administration. The oversight body, followed by court decisions in three instances<sup>59</sup> led to the reclaiming of about €3.5 Million in state subsidies from the liberal party. At the centre of the illegal financing of the party was its chairman, who by that time was already highly controversial for alleged Nazi-remarks and for a lost national election. The scandal resulted in a criminal investigation on tax evasion and political finance offences in 2003. Thirty minutes after the parliament lifted his immunity on 5 June 2003, the party chairman embarked on a private parachute flight that ended with him jumping to death under unclear circumstances.<sup>60</sup> It is not clear to what extent political rivals within the party have pushed facts about the illegal financing to the press in order to rid the party of its chairman.*

There are two sorts of Media reports around declarations:

- ▶ Reports, which “only” rely on the financial report and presenting it as implausible or “hard-to-believe”.
- ▶ Reports, which rely on additional data including informants.

It is obvious that the second kind of reports should regularly be a trigger for a full audit.

But even reports which only construe financial reports as being hard-to-believe should normally trigger a full audit: It supports the perceived credibility of the oversight body if it looks into cases of heightened public interest.

### **5.2.3 Information from other authorities**

Tax investigations are a frequent cause for triggering political finance inquiries. Any cash-flow outside political finance regulations is normally also outside tax regulations.

*Example 31 (see already Example 15)*

*One of the biggest scandals in German political party financing involved the German industrialist, Friedrich Karl Flick, one of the world's richest men – and came to be known as the Flick Affair.<sup>61</sup> In 1981, tax inspectors discovered that Flick had been secretly donating at least €13 million to all leading German political parties. In return for the donations, Flick allegedly bought his business political favours worth €420 million. As donations, the cash-flow would not have been tax exempt or privileged.*

59. See for example Administrative Court of Berlin, Decision 2 K 126.09 of 8 December 2009, Available at [www.gerichtsentscheidungen.berlin-brandenburg.de](http://www.gerichtsentscheidungen.berlin-brandenburg.de), Accessed on 24 July 2015.

60. The Economist (12 June 2003), A mysterious death – Why did one of Germany's most controversial politicians die? Available at [www.economist.com](http://www.economist.com), Accessed on 24 July 2015.

61. Der Spiegel (7 August 2009), Germany's Schreiber Affair: The Scandal that Helped Merkel Become Chancellor, Available at [www.spiegel.de](http://www.spiegel.de) (English), Accessed on 24 July 2015.

*Therefore, part of the money was channelled via tax-privileged charity trusts. Tax investigations into one of the charity trusts unrolled the whole scandal and led to a search of Flick's headquarters. There, a hidden cash-journal was found documenting millions of shadow donations. Eventually, three men were brought to trial – Flick's business manager, one former and one sitting economics minister (both from the liberal party) – and were convicted of tax evasion or assisting tax evasion; the conviction was upheld through all instances up to the Constitutional Court.<sup>62</sup> However, bribery charges had to be dropped even though the court expressed substantial doubts about the innocence of the defendants.*

*The whole scandal was only uncovered by one stubborn tax investigator from the former German Capital Bonn who acted against resistance of his superiors. As "gratification" for his determination and integrity, he was transferred against his will to another tax department. After unsuccessfully challenging the transfer in court, he continued as a tax lawyer in private practice.<sup>63</sup> Another tax investigator involved in the investigation was put on forced leave after a psychiatrist paid by the government attested him paranoia. The psychiatrist was later convicted for "intentional wrong expertise" because of this attestation. A civil suit for damages brought by the tax investigator against the state is still pending.<sup>64</sup>*

Another major source is criminal investigations by the police or prosecutors on embezzled money that somehow ends up with a political party:

*At the start of the affair, nobody had any idea that it would blow up to become a grand scandal on the scale of the Flick Affair.<sup>65</sup> It all started on 4 November 1999, with the issue of an arrest warrant for the conservative party's treasurer by the district court in Augsburg, Bavaria. The court suspected him of tax evasion in relation to a €500,000 donation by a well-known arms lobbyist and businessman, who had recently been arrested after he fled to Canada. The donation was transferred in cash on a parking lot in Switzerland. It is reported to stem from the arms producer Thyssen for facilitating the approval of exporting 36 tanks to Saudi Arabia. Allegedly, the (illegal) cash donation never reached the party but was shared among three party members. The scandal eventually uncovered a multi-million financing scandal and led to the resignation of Chancellor Kohl, a change of government, and a comprehensive reform of political finance regulations.*

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62. German Constitutional Court BVerfG, Decision 2 BvR 385/87 of 15 October 1990.

63. Tagesspiegel, (8 October 2006), One man and power [Ein Mann und die Macht], Available at [www.tagesspiegel.de](http://www.tagesspiegel.de), Accessed on 24 July 2015.

64. Capital (21 January 2013), How the State silences uncomfortable tax investigators [Wie der Staat unbequeme Steuerfahnder kaltstellt], Available at [www.capital.de](http://www.capital.de), Accessed on 24 July 2015.

65. Der Spiegel (7 August 2009), Germany's Schreiber Affair: The Scandal that Helped Merkel Become Chancellor, Available at [www.spiegel.de](http://www.spiegel.de), Accessed on 24 July 2015.

Bribery allegations are another example where criminal investigations can trigger a political finance inquiry: often donations are suspected to buy influence and will first lead to criminal investigations that, in a second step, uncover often unrelated violations of political finance (see above the bribery case under ).

The oversight body should ensure that tax and law enforcement authorities inform it about investigations into the official (through a memorandum of understanding or a respective legal provision).



## 6. Monitoring

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In the field of political finances, efficiency of legislations is best judged in terms of its application and the associated monitoring system. It will only be effective if well implemented and efficiently supervised. Political financing monitoring refers to the auditing system and to public monitoring and raises several questions: the independence of the audit and monitoring, the means available to a public monitoring body to exercise adequate substantive supervision, and the powers of investigation available to a public monitoring body.

### 6.1 Independence of the audit and the monitoring

Auditing brings up the question of the real independence of the auditors entrusted with certification of campaign and party accounts and of the members of the public supervisory bodies. Auditors must not be placed in situations that represent conflict of interest. Accordingly, auditors should not be members of the party they audit and should not be auditors of the companies which made donations to the party they audit. In small countries where the number of auditors is limited, this risk of conflict of interest may occur.

Independence from political influence of the public supervisory bodies is also crucial. It may become an obstacle for investigating financial irregularities related to government candidates and parties. A partisan membership in the monitoring body either close to the parliament (Azerbaijan, Belgium, Denmark, and Germany) or to the executive branch (Japan and Latvia) does not provide all guarantees of independence. Length of tenure also raises a question of independence. Confidence in independence of members of the supervisory bodies tends to be greater if they are not subject to reappointments.

### 6.2 Financial and material resources of the monitoring body

Independent and substantial monitoring requires adequate powers and resources to effectively supervise implementation of rules on political financing. A single body vested with a clear mandate, adequate powers, and resources can ensure more substantial and proactive monitoring than a fragmented system which includes different authorities vested with different bodies (e.g. commissions against corruption, tax authorities, court of auditors, and electoral authority).

### 6.3 Powers of investigation of the monitoring body

Very often the monitoring bodies do not go beyond the data provided by political parties (Croatia, Cyprus, Finland, France, Poland, Slovakia, and Slovenia) and the monitoring may be limited to the legality of the books rather than the real money flows (Hungary). In this landscape the British Electoral Commission's powers to monitor and secure compliance are an exception. It has the power to visit premises of parties and candidates. Investigatory powers of the Commission also cover persons who are suspected of having committed an offence under the rules on political financing and the Commission can require the production and the provision of documents. In Estonia, the Supervision body investigates suspected violations or complaints and may demand additional evidence from political parties or third parties and everyone else covered by the investigation.

Even if a supervisory body has human and financial resources to perform its duties, it may focus its resources on what it views the most significant breaches of political finance laws and for that purpose it may introduce an objective rating system. For instance the above-mentioned UK Electoral Commission considers its enforcement actions, including the use of investigatory powers and sanctions, where it is necessary and proportionate to do so in order to meet its enforcement aim and objectives. The French monitoring body focused its 2015 investigations on loans of political parties. Spot checks focused on risks of fraud may be used in such a compliance policy.

If a monitoring body does not have the resources to carry out audits, random checks of the accuracy of financial reports may be deterrent.<sup>66</sup> If a monitoring body can assign a staff member to a candidate for presidential elections, for instance, with risk of significant spending, who would follow daily electoral expenses of the candidate through his meetings, his travels and his advertisements, it will be in a better position to compare these expenditures with subsequently declared electoral expenses. For instance, field supervisors of the Serbian Anti-Corruption Agency collect election campaign data. They attend public events, record distributed election material, make notes of activities that could represent costs, and document them with photo or video material.<sup>67</sup> Gathered data is presented in the form of reports to coordinators on a weekly basis and forwarded then to the secretariat of the Agency.

Judicial authorities are also a valuable source for detecting possible fraud. They may by coincidence come across suspicious transactions connected to building licenses, for instance, that may be associated with political funding fraud. Many political scandals of this kind have been discovered through justice sector investigations in France, Italy and Spain. Vigilance has to be exercised also by mass media, political competitors and voters. External complaints by individuals or groups allowed under law may feed the work of supervisory bodies if they provide sufficient, substantial, and reliable evidence. This would naturally it implies data cross-checks from various sources: official sources such as financial statements and bank accounts, but also

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66. Magnus Ohman, Political Finance Oversight Handbook, International Foundation for Electoral Systems, 2013 page 80

67. Venice Commission, CDL-EL (2014) 004 11th European Conference of electoral management bodies

information gathered on the spot by natural or legal persons. For instance in order to support political spending oversight in Argentina, the local branch of Transparency International recorded the number of advertisements in the newspapers, on television and radio, and the number of posters in a given geographic area.<sup>68</sup>

Where supervisors cannot impose sanctions in case of suspicion of serious wrongdoing themselves, they have to ensure reports of suspected offences to enforcement authorities. For instance the Austrian Court of Audit (ACA), which audits the statements of account of the political parties and the campaigning parties, has the right as any citizen to inform the prosecution authorities of any wrongdoing. In Romania the Electoral Authority reports suspicions of criminal offences to the competent criminal justice authorities. The same applies in France. Contrary to that, in neither Austria nor Liechtenstein are supervisory authorities clearly allowed to forward the cases where there is a suspicion of criminal offences to the competent authorities.

In all circumstances, monitoring bodies should fulfill their duties by carrying out investigations of alleged financing irregularities in a close cooperation with other enforcers and law enforcement authorities.

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68. Magnus Ohman Ibid. page 124



# 7. Investigation

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## 7.1 Investigative powers

Political finance oversight bodies will have differing powers. Some will have no investigative powers at all; others will have access to certain databases, will be able to request any documentation related to the financial activities of parties, and be able to interview persons involved. In any case, oversight bodies can cooperate with other agencies, including law enforcement. The following is a picture of what can be achieved by looking deeper into a concrete case of political financing, either if triggered by a complaint or red flag, or, if done as a regular or sample check.

Depending on an oversight body's analytical and investigative powers, it could always request information from the political parties concerned or from third parties based on their consent. In addition, the oversight body could always decide to submit any evidence collected so far for notifying any law enforcement authority with further powers of obtaining evidence (for example, tax authorities).

## 7.2 Investigative strategy

### 7.2.1 Without concrete suspicion

When looking into a case without knowing what to look for, one has to ask the following strategic questions, in order to target possible irregularities:

- ▶ What are the weak points of the political finance system?
- ▶ For example, loose reporting or auditing requirements; high thresholds for reporting donations; allowance of large cash amounts, etc.
- ▶ Where does it create incentives for cheating?
- ▶ For example, state subsidies being linked to membership fees or private donations.
- ▶ Where does the tax system offer advantages for political parties or third parties?
- ▶ For example, donations being not tax deductible but donations to charity organisations, which creates an incentive for channelling donations through such organisations.

Any of the above mentioned are possible entry points for violations and require particular attention.

Apart from a concrete suspicion, the analysis will look at the financial report of a political party, campaign candidate, parliamentary group, or lawmaker from the following angles:

1. "Verifying the amount of income;
2. "Verifying expenditures;
3. Verifying the relation of income and expenditures;
4. Verifying assets and liabilities.

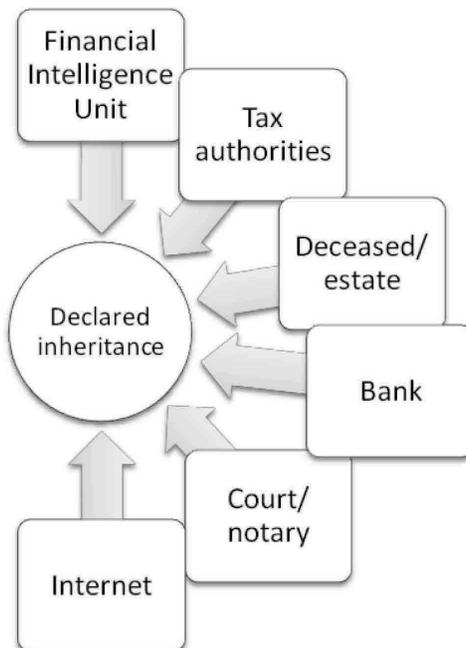
The verifications are done by using data from third sources, such as from databases indicated below ( ).

### 7.2.2 Following a concrete suspicion

The following three strategic questions provide the next steps:

- ▶ Are there possible **weak**/suspicious points in the financial report to start with?
- ▶ Where does data connected to the suspicion leave **traces**? Are there legal requirements for documentation? Or are there typical patterns of voluntarily providing information (e.g. internet)?
- ▶ What information could possibly substantiate or **contradict** the suspicion, and where does it leave traces?

As a first step, it is helpful to draw a chart of stakeholders and evidence possibly involved for any financial position identified. For example, the following sources might be relevant for looking into a suspicion around a large donation from an unknown corporation being hidden as coming from an inheritance:



In a second step, for each stakeholder, a list of possible leads/questions is drawn up:

- ▶ **Deceased/estate**
  - Is there a written will?
- ▶ **Financial Intelligence Unit**
  - Was the payment to the political party reported to the FIU by the involved banks?
  - Are there any reports to the FIU about money being channelled into the deceased's estate (in cash or as wire)?
- ▶ **Tax authorities**
  - Do tax statements support the deceased's alleged wealth?
  - Is the inheritance properly declared to the tax authorities?
- ▶ **Courts**
  - Is the inheritance recorded in court or notary documents?
- ▶ **Internet**
  - Is there data on the internet contradicting or verifying the death and wealth of the deceased?
- ▶ **Banks**
  - Where does the wealth of the deceased come from according to bank statements?

## 7.3 Written information

An investigation by a political oversight body or cooperating law enforcement authorities would use, in particular, the following sources of information:

### 7.3.1 Financial reports

Financial reports by political parties, each annual report in itself, and several reports combined, can provide clues and evidence as shown under chapter .

### 7.3.2 Databases and files

#### 7.3.2.1 State

One can cross-check in particular the following databases to verify data provided (or not) in the financial report:

- ▶ Tax authority.
  - Tax declarations are for example useful when checking the plausibility of donations and other cash flow from third parties: Do their tax declarations support sufficient means for transferring the alleged amount of money to the parties?
- ▶ Motor vehicles registry.
  - Does data confirm the date of acquisition of a vehicle?

- ▶ Land registry.  
Does data match declared data on land owned by political parties?
- ▶ Civil registry.  
Does the data on donors, testators, members, etc. match civil registry's data?  
Are several donors registered in the same household?
- ▶ Business registry.  
Does the data support declared income from parties' business activities?
- ▶ Register of bank accounts.  
Is the bank beneficiary owner of any bank account not reflected in the financial report? In some jurisdictions exist central registers for all bank accounts, or banks have to keep each a register to which a supervisory authority like the central bank has automated access. The register contains only the account number, and the name and birthday of its holder.<sup>69</sup> It thus allows public welfare agencies or tax authorities to verify whether citizens have bank accounts on which they did not provide information.
- ▶ Patents and licenses registry.  
Does data on licensed material (books etc.) match data in the financial reports?
- ▶ Financial Intelligence Unit.  
Is there any data at FIUs confirming reported large bank transfers or cash-flows?  
Financial Intelligence Units usually observe two kinds of financial patterns in order to detect cases of money laundering:
  - ▶ Transactions with suspicious specifics, as for example regular money transfers to a tax haven.
  - ▶ Transactions above a certain threshold, for example 10,000 €.

All financial institutions (and certain non-financial businesses and professions) in the country have to report any of the two types of transactions to the FIU. The FIU records and analyses the Suspicious Transaction Reports (STR) and Cash Transaction Reports (CTR) for possible further investigation. Those reports are an invaluable source for verifying financial declarations by public officials. Any STR or CTR on a public official could easily not be aligned with his/her declaration. For example, such reports could show cash transactions beyond the means declared, or transactions to foreign destinations which do not appear in the declaration. Conversely, a lack of a CTR should raise questions if the official has purchased a valuable asset and has apparently done so with large amounts of cash. Equally, the official might claim to have received a loan from a friend, but there is no CTR reflecting the alleged bank

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69. See § 24c of the German Banking Act [Gesetz über das Kreditwesen (KWG)], Available at [www.bundesbank.de](http://www.bundesbank.de), Accessed on 24 July 2015.

transfer. Another standard question for the FIU is, whether there are any cross-border transactions related to the public official.

- ▶ Immigration and customs authorities: information on border passing of persons and goods. For example, a cash donation by a person might be contradicted by that person's being out of country at the time of the cash donation according to customs information.

### 7.3.2.2 Private

- ▶ Company reports;  
Is there a mirror image of donations in company reports? Does data from companies' financial support match with reported donations?
- ▶ Banks;  
Do account statements support the wealth of donors and the declared cash-flows?

### 7.3.3 Internet search

There is a myriad of information available on the internet for cross-checking the plausibility of financial reports and transactions with third parties, such as:

- ▶ volume of campaign expenditure;
- ▶ campaign staff;
- ▶ offices;
- ▶ donors;
- ▶ members; and
- ▶ businesses.

### 7.3.4 Media reports

An analysis of media reports, where the name of the party or names of the persons involved in a case are mentioned can be a good starting point for collecting information.

### 7.3.5 Trash runs

Law enforcement agencies often search the suspect's discarded trash for evidence: this technique can be an effective way of obtaining leads to assets and cash-flows, as well as help develop probable cause for more coercive measures and evidence for use at trial. Suspects frequently discard evidence, including financial records and correspondence that may be valuable to a financial investigation.<sup>70</sup>

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70. FATF Report (June 2012), Financial Investigations Guidance, Available at [www.fatfgafi.org](http://www.fatfgafi.org), Accessed on 24 July 2015.

## **7.4 Video recordings**

Video recordings can link real donors with dummy donors. In Latvia, for example, party members would address people outside banks to deposit money for them as donations to a party account. Video footage could prove that this scheme took place in several cases.

## **7.5 Observations**

Direct observations by representatives of the political oversight body can be useful for checking campaign expenditures, allegations of abuse of administrative resources, party business, etc.

## **7.6 Interviews**

### **7.6.1 Experts, witnesses, donors**

The oversight body can always ask witnesses to provide voluntary information, such as the executor of an estate, the creditor of a loan, the seller of a car, etc. Whenever compulsory means are necessary, a law enforcement agency needs to be involved. For this to be possible, a provisional claim of a suspected offence would have to be made.

When dummy persons are involved, they are sometimes instructed by the real donors to provide standard answers during the interviews. Asking new and surprising questions can uncover the scheme. Interviews should normally be done in person in order to be able to confirm the identity of the person. They should also be done outside the interviewee's home or else the interview might catch unwanted media attention.

### **7.6.2 Party representatives**

In any case, party officials, such as a party's treasurer, are often the most knowledgeable source of information. However, one should carefully weigh the pros and cons of questioning a party member: it would warn an unfaithful party and might provide the opportunity to tamper with the evidence if the party is aware that an irregularity has been detected.

Another option might be to inform law enforcement authorities. If they have exploited all means of investigation, the relevant party officials could be interviewed.

## **7.7 Data of foreign entities**

Throughout the process, a foreign country's sovereignty must be treated with the utmost respect. State authorities have no right to pursue their own investigations in the territory of a foreign country. In some jurisdictions, even communication inquiries (by phone, letter or email) fall under the territorial sovereignty. In order to obtain information from foreign state or private parties, the oversight body would need to go through the channels of mutual legal assistance, usually located with the General

Prosecutor and/or the Ministry of Justice. A rather informal way of cooperating with foreign law enforcement is to go through an FIU (see above at ).

## **7.8 Obtaining evidence through other agencies**

Indications of illegal income might not point towards a specific crime such as bribery or embezzlement, but illegal income almost always entails the criminal offences of money laundering and/or tax evasion, in addition to administrative or criminal violations of political finance laws.

Based on suspicious initial evidence, the following law enforcement authorities can use compulsory and secret measures of obtaining evidence:

- ▶ Tax police;
- ▶ General Prosecutor;
- ▶ Secret service.

In addition, FIUs can obtain financial data from other jurisdictions.



## 8. Sanctions

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**S**anctions ensure credibility of the legal framework on political finance. Article 16 of the Council of Europe Recommendation calls member states to require the infringements of rules concerning the funding of political parties and electoral campaigns to be subject to effective, proportionate and dissuasive sanctions. Sanctions are clearly connected to detection of irregularities. If regulations do not provide for sanctions in case of violation of law, supervision will lose in strength and supervisors may not have sufficient incentive to detect various irregularities. Five conditions have to be met for sanctions to be considered appropriate to serve their main purpose.

First, sanctions have to cover all non-compliance aspects and be stipulated by law. For instance in its first assessment of the Irish regulations on party and election campaign finances, GRECO noted that not all legal obligations were coupled with effective sanctions in case of non-compliance. For example, the law was silent as to sanctions for failure to comply with a request by the Standards Commission to provide information or documentation (including by third parties) or failure to open a political donation account or the prohibition to use funds from the exchequer for electoral purposes.<sup>71</sup>

Secondly, disclosure and public reporting are the cornerstones of enforcement of rules on political financing. This means that financial information on candidates and on parties has to be made public in a coherent and comprehensible manner.

Third, sanctions have to be appropriate. GRECO evaluation of legislations of a number of Council of Europe member states revealed that infringement of political funding rules were not accompanied by adequate sanctions. For instance, sanctions in Italy are limited to infringements made by political parties and persons employed by the parties, but no such review has taken place in regards to sanctions for election campaigns and election candidates. The 2008 GRECO evaluation for Slovenia showed that if a party were to obtain funds from a prohibited source or received donations in excess of ten average monthly salaries, the fine which would have been imposed would have in fact been lower than the received benefit.

An efficient and appropriate legal framework of sanctions presupposes a wide range of sanctions. Serious breaches of law should not be punished lightly while minor offences should not be liable to too severe penalties. While criminal sanctions should be reserved for significant violations, small administrative fines may be sued for minor infringements, encourage voluntary compliance, and encourage efficient work of supervisors. This is also a recommendation from GRECO, which calls upon a system of flexible sanctions, such as administrative ones or fines, which could serve as warnings, which would precede termination of state support and criminal sanctions. Loss of a seat for violation of political funding regulation is applicable in Armenia, in France (except for presidential elections), and in the United Kingdom<sup>72</sup> and may be a highly dissuasive tool.

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71. GRECO, Third Evaluation Round, Compliance Report on Ireland, 9 December 2011, Available from: [www.coe.int](http://www.coe.int); Accessed on 18/07/2016

72. The Representation of the People Act 1983 disqualifies candidates for corrupt and offences relating to donations.

The enforcement approach of the British Electoral Commission is worth considering when talking about flexible sanctions. The Commission can issue compliance notices, restoration notices, and stop notices. Compliance notices refer to actions that must be taken by the person/entity who/that has broken the rules. Restoration notices refer to actions that must be taken by the person or organization that has broken the rules to restore the position that could have been obtained hadn't the rules been broken. The purpose of the stop notice is to prohibit beginning or carrying activities until steps set out in the notice are taken. The Commission can also impose fines. In Croatia money collected or spent by parties, lists, or candidates in a manner contrary to the provisions of the law is to be seized and transferred to the state budget. In many cases, infringement of the rules leads to loss of the right to public funds for a specific period of time. It may be short (four months in Belgium), which is not necessarily sufficiently dissuasive because during that period of time a party may borrow money to compensate the loss. It can also be longer (one year in France, Norway and Poland), which serves as more of deterrent.

Fourth, sanctioning must cover all stakeholders involved in the process of party and election funding, thus not only parties and candidates but also individual donors and entities linked to parties. This point has been raised in the Netherlands, in Serbia and in Spain by GRECO. Remedying such shortcoming will help supervisors in their tasks. Liability for infringements may be shared between the candidate, his financial agent and/or the treasurer of the party. Sometimes it is not clear who should be held accountable for the violation of the law on political funding: will it be the treasurer? The leader of the party? Shall they enjoy immunity if they are members of Parliament? May the party be prosecuted as a legal person?

Five, an efficient system of enforcement is required. A loophole in the legal framework may however impede this. For example, discretionary powers of bodies (not) to impose sanctions, such is the case with the Ministry of Justice of Azerbaijan, erode the effects of a sanctioning regime.

As a last note, the statute of limitation regimes have to be construed so as not to impede conduct of investigations/inquiries and sanctioning for violations. For example, if a report of a monitoring body is released with a long delay after an infringement took place, while the statute of limitation is short, it will inevitably impede the supervisory body to conduct further enquiries and investigate properly. In some countries the statute of limitations was very short (Armenia, Moldova and Romania) and was extended for this purpose.

# 9. Case studies

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The following are case studies illustrating real life examples.

- ▶ how the illegal financing was unsuccessfully hidden (Chapter 4);
- ▶ how the investigation was triggered (red flags – Chapter 5);
- ▶ what investigative means were used to uncover the scheme (Chapter 7).

## 9.1 No. 1 – Latvia: “NGO for Freedom of speech”

### The Legal Background

In 2006, the election to the Saeima (the Latvian Parliament) took place. Pursuant to the law *On Financing of Political Parties and Organisations*<sup>73</sup> and the law *On Campaigning for the Saeima and the European Parliament Elections*<sup>74</sup>, the parties putting forward candidates were subject to the following limitations in the run-up to elections:

- ▶ the start date for the 2006 Saeima election campaign was 270 days before the election day, i.e. from 10 January 2006 to 7 October 2006;
- ▶ a party's election campaign expenses would be limited to LVL 278,345, or EUR 394,760. The eligible expenses included the following:
  - placement of election campaign ads;
  - postal services;
  - production of election campaign ads;
  - planning, arranging, and managing the election campaign;
  - wages and other payments related to the planning of the election campaign;
  - rental of movable and immovable property required for the election campaign;
  - production of booklets, magazines, etc., and
  - sponsorship during the election campaign.
- ▶ the total of monetary contributions from one individual should not exceed LLV 10,000, or EUR 14,180.

At the time, the law *On Campaigning for the Saeima and the European Parliament Elections* did not define the so-called “third parties” leaving a gap in the law whereby these third parties were allowed to express their opinions and support for political parties and such support would not be counted as in-kind contribution.

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73. Latvian Law on Financing of Political Parties and Organisations as amended on 18 May 2006 [Grozījumi Politisko organizāciju (partiju) finansēšanas likumā], Available at [www.likumi.lv](http://www.likumi.lv), Accessed on 24 July 2015.

74. Latvian Law on Campaigning for the Saeima and the European Parliament Elections as amended on 15 September, 2005 [Grozījums likumā “Par priekšvēlēšanu aģitāciju pirms Saeimas vēlēšanām un Eiropas Parlamenta vēlēšanām”], Available at [www.likumi.lv](http://www.likumi.lv), Accessed on 24 July 2015.

## Identifying the Violation

A group of persons used a loophole in the existing legislation and registered the NGO named *For Freedom of Speech* on 20 February, 2006. The mission of the NGO was, supposedly, to promote civil society and human rights in Latvia. NGOs are not subject to control by the KNAB. The NGO was founded by J.Liepnieks and K. Roļšteins who had previously been directly linked to the People's Party and managed several election campaigns for the party.

In the run-up to the Saeima election, a promotion campaign was launched on television where various renowned people spoke positively of the cabinet, the People's Party, and the members of the cabinet representing the People's Party. At the time, the head of the Latvian cabinet was Aigars Kalvītis who was also a member of the People's Party.

The promotion campaign was very dynamic and extensive. Video advertisements were broadcast on all Latvian TV channels. The KNAB received many complaints against the People's Party allegedly trying to circumvent the election campaign spending limits established by the law *On Financing of Political Parties and Organisations*. The campaign violated the principle of equality of political parties in the run-up to the election and thus significantly undermined the democratic and equal election process. As of 2006, the campaign spending limit was LLV 278,345 or EUR 394,760. According to the People's Party's income and expenditure statement for the 2006 Saeima election campaign, the party had spent the total of LLV 138,914 or EUR 197,013 on its election campaign.<sup>75</sup>

On the other hand, the NGO *For Freedom of Speech* had spent the total of LLV 564,149 or EUR 800,097 on its promotion campaign in the run-up to the election. The advertisements could be broken down into four groups:

- ▶ positive thinking (see below screenshot 1),
- ▶ the Latvian cabinet (see below screenshot 2),
- ▶ the members of the cabinet representing the People's Party (see below screenshot 3), and
- ▶ the People's Party (see below screenshot 4).

(1) An example of an opinion about positive thinking



75. KNAB, Declaration by "Tautas Partija" of 22 March 2005, Available at [www.knab.gov.lv](http://www.knab.gov.lv), Accessed on 24 July 2015.

Ēriks Stendzenieks:

“Whether third parties may campaign or not is a non-issue. There are countries where it is totally legitimate and there are countries where it is prohibited. All this is perfectly normal. The politicians may be the most underappreciated members of our society. Usually it might seem deservedly so, but by and large, it is not. Really, it’s not like the only food you can buy in a grocery store is margarine and only the cheapest, shabbiest cars are in the streets. Some things have definitely changed, and some of the changes are good.”

(2) An example of an opinion about the cabinet



Leons Briedis:

“This cabinet will surely go down in history as one of the more efficient cabinets, possibly the most efficient since Latvia’s independence, for the real effort it puts in with little fanfare.”

(3) An example of an opinion about a member of the cabinet representing the People’s Party



Kristīne Opolais:

“She is always happy to compliment people, always so radiant, which is very nice of her, and she encourages herself and others to do their best to please people. There is nothing better than to get encouragement, both official and informal, from a member of the cabinet. She is a very kind-hearted person. I often see her cry and I know that it really comes from her heart. She’s a very sophisticated person, she knows a lot about music, and she’s always interesting to talk to. All this means a lot to the people of art. I hope it stays that way.”

(4) An example of an opinion about the People’s Party



Nina Pleša:

“There is still a crisis within the health care system but the progress already achieved is obvious. Until now, none of the political parties have ever focused on the problems faced by hospitals in remote areas. However, the situation improved after the People’s Party took over the Ministry of Health. We, the staff at the hospital of the town of Balvi, do feel the positive impact.”

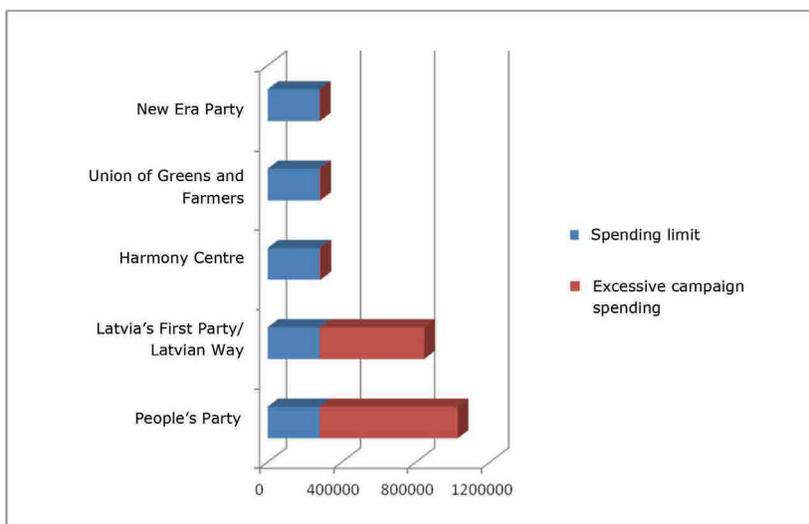
### **The Issues Encountered**

As mentioned above, the law *On Campaigning for the Saeima and the European Parliament Elections* did not define the third parties and their rights.

The goal of the KNAB was to prove that the election campaign run by the People’s Party and the promotion campaign run by the NGO *For Freedom of Speech* had effectively the same aim of campaigning for the People’s Party’s parliamentary candidates who at the time were members of the Latvian cabinet.

After the election, it was stated that all five political parties that had entered the Saeima had exceeded campaign spending limits, the absolute worst offender being the People’s Party (“Tautas partija” in below diagram).

**Diagram 1. The actual campaign spending vs. the spending limit, EUR**



Source: KNAB

The diagram shows the excessive campaign spending of all five parties that had entered the Saeima.

### Summary of the Knab Audit

The **initial audit** included the visual assessment of the promotion campaign entitled *You Have the Right to Know This Point of View!* that had been run by the NGO *For Freedom of Speech* (i.e. Campaign 1).

According to the definition provided in the law *On Campaigning for the Saeima and the European Parliament Elections*, election campaigning means a direct appeal to vote for or against a political party or a parliamentary candidate.

Campaign 1 did in fact meet the criteria set by the above definition as it featured an appeal to vote for the People's Party and the parliamentary candidates nominated by the party.

The KNAB also examined the registration documents of the NGO *For Freedom of Speech* and found that, according to the registration documents, the NGO's mission and objectives did not specify any cooperation with political parties or participation in election campaigns. Nevertheless, it was established that the founders of the NGO were two PR managers who had previously organised several election campaigns for the People's Party.

Based on the results of the initial audit, on 10 July 2006, the KNAB initiated an **in-depth audit** to verify the legality of Campaign 1. The aim of the audit was to find out whether the NGO *For Freedom of Speech* had been acting in an effort to assist the People's Party in circumventing the election campaign spending limits as applicable to political parties pursuant to the law *On Financing of Political Parties and Organisations*.

Additionally, on 20 December 2006, the KNAB started the verification of the People's Party's income and expenditure statement for the 2006 Saeima election campaign.

In the initial phase, the KNAB requested all documents related to the registration and financial operations of the NGO *For Freedom of Speech* as well as used its powers to request all of the NGO's bank transaction printouts.

Based on the analysis of the financial operations of the NGO *For Freedom of Speech*, it was established that during the planning and organisation phases of Campaign 1, the NGO *For Freedom of Speech* had received the total of LLV 566,310 or EUR 803,163 in donations. The largest donations had come from the following sources:

- ▶ LLV 330,000 or EUR 468,019 had come from Mr. A.Šķēle who was a founder, unofficial leader, and member of the People's Party.
- ▶ LLV 107,300 or 152,177 EUR had come from the JSC *Shipping Company of Latvia*.
- ▶ LLV 80,000 or EUR 113,460 EUR had come from Mr. J.Liepnieks who was a member and PR manager of the People's Party.

**Diagram 2. Campaign 1 funding scheme**



Source: KNAB

The audit revealed that the donations to the NGO had come directly from the People's Party. That was one of the reasons why Campaign 1 could not qualify as a public expression of opinion since it had all of the characteristics of election campaigning.

According to the law *On Campaigning for the Saeima and the European Parliament Elections*, election campaigning means promoting political parties, alliances of political parties, or parliamentary candidates nominated by political parties provided that such advertising directly or indirectly appeals for voting for or against a political party, an alliance of political parties, or a parliamentary candidate nominated by a political party.

It was established that every video advertisement had at least some characteristics of election campaigning. Additionally, it was established that the messages had not been neutral. The people involved in Campaign 1 had been biased towards one political party and its members despite the fact that Campaign 1 had allegedly been aimed at promoting positive thinking in the society.

During the audit, the KNAB interviewed the participants of Campaign 1 as well as its sponsors and donors.

The Radio and Television Oversight Council also provided its own assessment of Campaign 1 based on claims by radio and television companies that the majority of the broadcast Campaign 1 advertisements were part of election campaigning.

Campaign 1 was in fact election campaigning, the KNAB faced another problem, namely whether to qualify Campaign 1 as a campaign financed by a third party (scenario 1) or a campaign promoting the People's Party (scenario 2).

#### Scenario (1)

As of 2006, the law *On Campaigning for the Saeima Elections* did not define the so-called third parties and their rights and obligations. Had the NGO been recognised as a third party, no sanctions would have applied because of the major loopholes in the law.

#### Scenario (2)

The law *On Campaigning for the Saeima Elections* and the law *On Financing of Political Organisations* put strict limitations upon the amount of money an individual may contribute to a political party within one year and the amount of money a political party may spend on election campaigning. Donations from legal entities were prohibited.

Based on the findings of the audit, the KNAB opted for scenario 2 and found a direct connection between Campaign 1 and the election campaigning for the People's Party. The body of evidence was collected and consolidated in the following stages:

1. The initial audit which included identifying the problem and formulating the objective.
2. The in-depth audit which included gathering the information from audit reports, publications, aggregate statistical data, re-audit, interviewing everyone involved, etc.
3. The internal discussion within the KNAB involving legal professionals, auditors, and the KNAB management.
4. Based on the available evidence, the KNAB formulated its opinion on Campaign 1 and qualified the identified violation in accordance with the existing law.
5. The decision was adopted.

## 9.2 No. 2 – Latvia: “Ice hockey in politics”

### The Legal Background

In 2010, the election to the Saeima (the Latvian Parliament) took place in Latvia.

Pursuant to the law *On Financing of Political Parties and Organisations*<sup>76</sup> and the law *on Campaigning for the Saeima and the European Parliament Elections*<sup>77</sup>, the parties

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76. Ibid.

77. Ibid.

running their candidates were subject to the following limitations in the run-up to elections:

- a. the length of the 2010 Saeima election campaign was 120 days before the election day, i.e. from 05 June 2010 to 02 October 2010.
- b. a party's election campaign expenses would be limited to LVL 571,211, or EUR 807,707. The eligible expenses included the following:
  - ▶ placement of election campaign ads;
  - ▶ postal services;
  - ▶ sponsorship during the election campaign;
- c. the total of monetary contributions from one individual would not exceed LLV 18,000, or EUR 25,400;
- d. on the day of the election and the day prior, it is prohibited to place election campaigning materials in the public space or in the media.

During this period, there were no obvious loopholes in the laws regulating financing of political parties and their election campaigns.

### **Identifying the Violation**

At this election, the party union named "For a Better Latvia" (ZHL) was registered, and it actively conducted its election campaign in the media and in the public space throughout the campaigning period. This political party ran for the election as No.8 on the list.

This union was made up of two parties, "Latvia's First Party" and "Latvian Way", whose Chairman A.S. was the leader of the union and number one on its list of candidates for the Parliament.

For this election, the costs of campaigning material were limited. For example, while the previous most expensive election campaign had been conducted when no limits on campaign spending were in effect and cost approximately EUR 2,000,000, at this election a party could spend no more than EUR 806,567 on placement of campaigning materials and on charity events.

In total, thirteen lists of party candidates were submitted for the election. In the process of implementing control measures (independent monitoring, studies of the concluded contracts, cross-checks, and complaints consideration), it was concluded that none of the parties exceeded the ceiling of spending on election campaigning and organised charity events on the eve of the election.

The day before the election, when election campaigning was banned for everyone, advertising of the hockey club "Dynamo Riga" appeared in the public space. The skipper of the hockey club's team who also plays as number 8 featured in the advertisements. On the photographs, he was holding his hockey uniform, and the slogan of the advertising company was "FOR A BETTER HOCKEY" and "FOR A BETTER DYNAMO".

On the very first day after the advertisement was placed in the public space, KNAB received more than 50 calls from the public all of whom viewed the advertisements

as campaigning for ZHL. Most of the people calling read the slogan of the club as the name of the party FOR A BETTER LATVIA!

(1) Examples of the party's election campaign:



“FOR A BETTER LATVIA!”



(2) Examples of the hockey club's advertising:



## Issues Encountered

The law *On Campaigning for the Saeima and the European Parliament Elections* defines the third parties and their rights.

The main goal of KNAB's audit was to prove that the campaign run by the hockey club was election campaigning. The next step was qualifying the advertising as election campaigning by a third party or proving that the hockey club's promotion campaign the day before the election and on the election-day was a component of ZHL's election campaign.

The hockey club "DYNAMO RIGA" did not position itself as a third party and insisted that its advertisement campaign was not related to the upcoming election. The hockey club explained the advertisement campaign as promotion of the club linked to the upcoming arrival of the hockey club "PHOENIX COYOTES FLY" for a friendly NHL match.

## Summary of the KNAB Audit

The **initial audit** included visual assessment of the campaign conducted by the hockey club "DYNAMO RIGA" (Campaign 2).

Based on the definition in the law *On Campaigning for the Saeima and the European Parliament Elections*, election campaign is a direct or indirect appeal to vote for or against a political party or a candidate.

KNAB concluded that Campaign 2 included the criteria that define an election campaign, as it manifested a direct appeal to vote for ZHL since identical colors and slogans had been used, and the number in the picture was identical to ZHL's list of candidates number.

Overall, in the course of the audit, KNAB analyzed the following:

- ▶ the list of founders and board members of the hockey club;
- ▶ separately, it analysed the visual similarity of the two campaigns, and
- ▶ it took into account the timing of the hockey club's advertisement campaign and advertising venues.

Based on the results of the initial audit, KNAB initiated an **in-depth audit** to verify the legality of Campaign 2. The aim of the audit was to find out whether the hockey club's promotion campaign one day before the election and on the election-day was part of the election campaign of ZHL, or whether that was an election campaign of the hockey club as a third party.

KNAB studied all the documents related to the timing of organizing and placing of the hockey club's advertisement campaign (bank accounts, and contracts for all transactions). Explanations were requested from all individuals associated with the organisation, with development and placement of the hockey club's advertising campaign.

As a result of the audit undertaken, it was discovered that:

- ▶ there was visual similarity between the two campaigns;
- ▶ advertising posters of the hockey club were placed in exactly the same places where ZHL campaign materials were previously placed;

- ▶ in its campaign, ZHL used the sports theme as one of its items, referring to the hockey club “DYNAMO RIGA”;
- ▶ hockey player Sandis Ozolinsh, seen on promotional materials of the hockey club, also appeared in ZHL election campaign materials, and
- ▶ three shareholders of the hockey club G.U., G.S., and G.R. were also members of the ZHL board. Moreover, G.U. was also a candidate on the ZHL list, but since G.U., G.S., and G.R. did not make the decision on placement of the hockey club’s advertisement campaign, not enough evidence was collected to recognise the hockey club’s advertising as a continuation of the ZHL party election campaign.

Therefore, the actions of the hockey club that placed the advertisements on the day before the election and on the election-day were classified as a third party’s election campaign. The limit on placement of election campaign materials was exceeded by EUR 14,027. They also breached the ban on campaigning on the day before the election.

The hockey club was fined under administrative procedures for placing election campaign materials in the period when this was prohibited. The resolution led to the payment of the amount exceeding the limit on a third party’s election contributions, in total EUR 14,027, to the national budget.

### **9.3 No. 3 – United Kingdom “Foreign donations”**

#### **The UK Electoral Commission investigation into donations to the Liberal Democrats reported as being from 5<sup>th</sup> Avenue Partners Limited**

##### **1. About the Electoral Commission<sup>78</sup>**

The Electoral Commission (‘the Commission’) is an independent regulator established by the UK Parliament. One of its core objectives is ensuring the transparency of party and election finance, with high levels of compliance.

Political parties are a central part of democratic politics. They set out competing views and policies for voters to choose from at elections. Parties need money to campaign and develop their policies, and to communicate with voters. It is important that the public knows where money is coming from, and has confidence that it comes from permissible sources.

The Political Parties, Elections and Referendums Act 2000,<sup>79</sup> as amended, establishes controls on donations and loans to, and spending by, political parties and some other regulated organisations and individuals. Regulated organisations and individuals include ‘third party’ organisations campaigning at elections, campaigners in

78. The following text is taken in large parts from the Commission’s website, with some slight editing, and an additional comment (see below No. 6): The Electoral Commission (20 November 2009), News release – Donations by 5th Avenue Partners Limited to the Liberal Democrats: statement, Available at [www.electoralcommission.org.uk](http://www.electoralcommission.org.uk), Accessed on 24 July 2015.

79. United Kingdom, Political Parties, Elections and Referendums Act 2000, Available at [www.legislation.gov.uk](http://www.legislation.gov.uk), Accessed on 24 July 2015.

referendums, and other 'regulated donors' (which include members of political parties, holders of elective office, and associations mainly consisting of party members).

The Commission is responsible for ensuring that these organisations and individuals comply with the requirements of PPERA.

Under PPERA, political parties and some other regulated organisations and individuals have to:

- ▶ report to the Commission on the donations and loans they receive and send it their accounts, so that the Commission can publish that information;
- ▶ make sure that they only accept donations and loans from 'permissible' sources such as individuals on the electoral register; and
- ▶ stay within spending limits during election and referendum campaigns, and report to the Commission on what they have spent.

The Commission's regulatory role is to ensure that the organisations and individuals that it regulates follow these rules.

## **2. Trigger of the Case**

In the following case an allegation was made to the Commission by a Member of Parliament who had received information from a constituent concerning the provenance of the donations. A national newspaper (The Times) also published articles concerning the donations claiming the party had used a 'loop hole' in the law in May 2005. The initial investigation by the Commission was suspended while the police conducted a criminal investigation into Michael Brown, the owner of 5<sup>th</sup> Avenue Partners Ltd. The Electoral Commission investigation resumed in November 2008 after Mr Brown was found guilty of a number of criminal offences (not related to political finance). The Commission considered a substantial body of evidence: evidence from the criminal proceedings against Michael Brown; documents obtained from the City of London Police, including analysis by forensic accountants; and evidence provided by the Liberal Democrat party.

It should be kept in mind, though, that the Commission at that time had no power to require potential witnesses to attend for interview. Furthermore, it was only able to require the provision of documents from regulated entities and officers of regulated entities – in other words, from the party and its officers – but not from reported donors or others. Since 2010, the Commission's powers are amended and it is able now, for example, to require information from donors as well as from those that receive donations.<sup>80</sup>

## **3. Basic Facts**

The Commission investigated donations made to the Liberal Democrats and reported as being from 5<sup>th</sup> Avenue Partners Limited, to determine whether those donations were within the rules for political donations under the Political Parties, Elections and Referendums Act 2000.

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80. United Kingdom, Political Parties and Elections Act 2009, available at [www.legislation.gov.uk](http://www.legislation.gov.uk); The Electoral Commission (21 October 2010), News release – New powers for party funding regulator, Available at [www.electoralcommission.org.uk](http://www.electoralcommission.org.uk), Accessed on 24 July 2015.

Enquiries concerning the donations began in May 2005 but were suspended in March 2007 at the request of the City of London Police. The Commission was only able to resume its investigation at the conclusion of the criminal proceedings in November 2008, at which time Michael Brown, the sole director (and founder) of 5<sup>th</sup> Avenue Partners Limited, was convicted of theft, furnishing false information and perverting the course of justice (for maintaining some kind of financial snowball scheme defrauding several private clients).<sup>81</sup>

During its investigation the Commission has made a number of enquiries and obtained and considered a large volume of documents, including evidence used in the criminal proceedings against Michael Brown. Those documents became available to the Commission in May 2009, sometime after the investigation was resumed.

Having carefully examined the evidence and the applicable law, the Commission has concluded that 5<sup>th</sup> Avenue Partners Limited met the permissibility requirements under the Political Parties, Elections and Referendums Act 2000, and therefore was a permissible donor. The Commission also considers that there is no reasonable basis, on the facts of this case and taking into account the relevant law, to conclude that the true donor was someone other than 5<sup>th</sup> Avenue Partners Limited.

No evidence emerged during the investigation to change the Commission's previously expressed view that it was reasonable for the Liberal Democrats, based on the information available to them at the time, to have regarded the donations as permissible.

The donations reported as being from 5<sup>th</sup> Avenue Partners Limited are as follows:

- i. 10 Feb 2005, £100,000.
- ii. 25 Feb 2005, £151,000.
- iii. 22 Mar 2005, £1,536,064.80.
- iv. 30 Mar 2005, £632,000.
- v. 06 May 2005, £30,000 for use of aircraft for 5 days.

#### **4. Legal Framework for Political Donations**

There are a number of rules under PPERA in relation to what donations can be accepted by political parties.

Parties can only accept donations from 'permissible' donors. A permissible donor is, in the case of an individual, someone who is registered on the electoral register. In the case of a company, a permissible donor must be registered under the Companies Act 1985; incorporated within the United Kingdom or another member State; and carrying on business in the United Kingdom at the time of the donation.

If a party receives a donation from an impermissible source it should return the donation within 30 days. Where a party has accepted a donation which it was prohibited from accepting, or accepted a donation despite being unable to establish

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81. BBC (28 November 2008), Top Lib Dem donor stole millions, Available at <http://news.bbc.co.uk>, Accessed on 24 July 2015.

the permissibility of the donor, the Commission may seek a court order that an amount equal to the impermissible donation be forfeited.

## **5. Key issues in the Investigation**

The investigation focused on the two key issues of the case, set out below:

### **1. Was 5<sup>th</sup> Avenue Partners Limited a permissible donor?**

5<sup>th</sup> Avenue Partners Limited was registered under the Companies Act 2005 and was incorporated within the UK, as required by the Political Parties, Elections and Referendums Act 2000. The issue to be determined was whether it was carrying on business in the UK at the time of the donations.

The evidence indicates that 5<sup>th</sup> Avenue Partners Limited undertook a number of actions consistent with carrying on business, including opening business bank accounts with a major high street bank, opening trading accounts with a financial services broker, contracting for staff/services and passing company resolutions. In February 2005 it deposited a substantial sum of money into one of its trading accounts, which was then used for options trading and in March 2005 the company entered into a lease for offices. During February and March 2005 it also spent substantial sums on office furniture and equipment. Some of these activities occurred shortly after the initial donations were made; a number of others were undertaken in advance of the donations.

Based on the evidence, the Commission has concluded that 5<sup>th</sup> Avenue Partners Limited met the permissibility requirements under the Political Parties, Elections and Referendums Act 2000 and was, therefore, a permissible donor.

### **2. Was 5<sup>th</sup> Avenue Partners Limited the true donor?**

The Commission considered whether there was a basis for concluding that either Michael Brown, as an individual, or 5<sup>th</sup> Avenue Partners GmbH, a company incorporated in Switzerland and which was the parent company of 5<sup>th</sup> Avenue Partners Limited, was in fact the true donor. Neither Michael Brown nor the parent company would have qualified as permissible donors under the Political Parties, Elections and Referendums Act 2000: Michael Brown was residing in Majorca, Spain, at the time of the donation, and was not registered to vote in the United Kingdom; the parent company was incorporated in Switzerland and thus a foreign entity.

The Commission considers that there is no reasonable basis taking into account the facts of this case and the relevant law to conclude that the true donor was anyone other than 5<sup>th</sup> Avenue Partners Limited. The Commission looked at the relevant evidence and considered that there was no reasonable likelihood that a court would find that 5<sup>th</sup> Avenue Partners Limited acted as an agent on behalf of either Michael Brown or 5<sup>th</sup> Avenue Partners GmbH when making the donations. The Commission also considered whether company law allowed the actions of 5<sup>th</sup> Avenue Partners Limited to be treated as the actions of Michael Brown or 5<sup>th</sup> Avenue Partners GmbH. The Commission considered that there was no reasonable likelihood that a court would remove the usual protection provided by the veil of incorporation.

There is no credible evidence that any of the donations came from Michael Brown's own money rather than from one of his companies. For three of the donations (the

donations of £100,000, £151,000 and £632,000), the evidence indicates that money in relation to these came from money transferred into 5<sup>th</sup> Avenue Partners Limited by investors.

For the other two donations (the cash donation of approximately £1.54m and the non-cash donation of £30,000) the movement of funds was different, in that the parent company was involved.

The source of funds for the donation of approximately £1.54m can be traced as having originated with investments into the parent company. Funds were transferred from the parent company bank account to the UK company bank account. E-mails prior to the transfer confirmed that the transfer was for the purpose of onward transfer of those funds to the Liberal Democrat Party. The sum of €2,250,000 was transferred to 5<sup>th</sup> Avenue Partners Limited. Shortly thereafter €2,225,000 was transferred from 5<sup>th</sup> Avenue Partners Limited bank account to the Liberal Democrats. The money arrived in one of the Party's accounts on 22 March 2005 having already been converted into Sterling in the sum of £1,536,064.80.

The Commission considered whether the transfers amounted to an agency arrangement. An agency arrangement is a form of agreement that one person acts on behalf of another. An agency arrangement would not arise purely because a holding company made funds available to its subsidiary. It is commonplace for holding companies to transfer funds to subsidiaries.

The Commission considered whether the transfer amounted to agency, whereby 5<sup>th</sup> Avenue Partners GmbH arranged for 5<sup>th</sup> Avenue Partners Limited to act on its behalf. The facts do not support such a conclusion. There is no evidence of an express agency agreement. Additionally, there is no evidence of a motive for the parent company to use the UK Company to make the donation on its behalf. Any benefit from making the donations appeared to relate primarily to the UK company rather than its parent, which did not support a conclusion that the UK company was merely acting as a conduit for its parent. There is also no evidence that the manner of transfer of funds was intended to conceal the true source of the donation or to evade the requirements of the Political Parties, Elections and Referendums Act 2000.

The cost of the non-cash donation of £30,000 in relation to flights was originally met by 5<sup>th</sup> Avenue Partners GmbH. The Liberal Democrats provided documents to indicate that the cost of the donations was ultimately met by 5<sup>th</sup> Avenue Partners Limited. This evidence included an inter-company recharge invoice from 5<sup>th</sup> Avenue Partners GmbH to 5<sup>th</sup> Avenue Partners Limited and a statement from Michael Brown confirming that the cost of the flights was met by 5<sup>th</sup> Avenue Partners Limited. Whilst there was concern about the reliability of these documents there was insufficient evidence to contradict the information provided by Michael Brown and 5<sup>th</sup> Avenue Partners Limited. On the facts of this case the Commission was of the view, in relation to this non-cash donation that there was no reasonable likelihood that a court would find that that 5<sup>th</sup> Avenue Partners GmbH was the true donor rather than 5<sup>th</sup> Avenue Partners Limited.

## 6. Comment

The case illustrates the need of a political oversight body for sufficient investigative powers to be realised. It is possible, or even likely, that the Commission would have reached a different result if it could have tapped data resources other than simply the provision of documents from regulated entities and officers of regulated entities – in other words, from the party and its officers – but not from reported donors or others. Further witness statements, banking data, Financial Intelligence Unit analysis, etc., could have drawn a different picture. From a legal point of view, it should be pointed out that in many jurisdictions the donation of 5<sup>th</sup> Avenue Partners Limited (UK) would be evaluated as a donation by 5<sup>th</sup> Avenue Partners GmbH (Switzerland), because the money was transferred from the parent company to 5<sup>th</sup> Avenue Partners Ltd with the purpose of making a donation to the Liberal Democrat Party.

## 9.4 No. 4 – Canada “Kick-backs”

### Kick-backs to the Canadian Liberal Party<sup>82</sup>

#### 1. Political Finance Overview in Canada

Canada receives fairly high marks for transparent and effectively monitored procedures for private and public party financing and electoral campaign financing, and for the ways in which infringements are subject to sanction. The Canada Elections Act requires registered parties or electoral-district associations to issue income tax receipts for contributions, and to make public reports on the state of their finances. Furthermore, the act requires registered parties to report and make public all contributions of more than CAD 5. Elections Canada provides access to the full database online for public use.

#### 2. The Sponsorship Programme

The Sponsorship Programme was a federal government advertising campaign. Each year federal, provincial, territorial, and municipal governments in Canada spent hundreds of millions of dollars on various forms of advertising and publicity. Spending intensified over the unsuccessful trial of the Canadian province of Quebec to gain independence from the Federal Republic of Canada in 1995.

#### 3. Trigger of the Case

The Sponsorship Scandal began with allegations of there being conflicts of interest in the management of the federal sponsorships. In 2000, Alfonso Gagliano, then Minister of Public Works and Government Services Canada (PWGSC), and also the minister responsible for the Sponsorship Programme, came under fire when it was revealed that sponsorship contracts had been awarded to advertising firms that had sub-contracted their printing business to a company linked to Gagliano's son. Opposition

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82. This case study is largely based on or cited from the following source: Mapleleafweb (1 January 2006), Gomery Commission of Inquiry & Sponsorship Scandal, Available at [www.mapleleafweb.com](http://www.mapleleafweb.com), on which further information on the scandal can be found. Information on the political finance system is drawn from: Mapleleafweb (21 July 2009), Federal Campaign Finance Laws in Canada, Available at <http://mapleleafweb.com>, Accessed on 24 July 2015.

parties called for Gagliano's resignation, suggesting that it was inappropriate for a cabinet minister to be overseeing government contracts that benefited his family. The Federal Ethics Counsellor, Howard Wilson, later cleared Gagliano of breaking any conflict of interest rules.

Concerns with the Sponsorship Programme later intensified over irregularities found in sponsorship contracts given to Groupaction Marketing, Inc., a Montreal-based advertising firm. In the late 1990s, Groupaction had been awarded three contracts for advertising-related services designed to increase the visibility of the federal government. The contracts were valued at \$500,000, \$550,000, and \$575,000 respectively. In March 2002, Public Works and Government Services Canada (PWGSC) reported that one of the Groupaction reports, worth \$550,000, had not been delivered.

#### **4. Further Procedure**

Don Boudria, then Public Works Minister, immediately asked the Auditor General of Canada to investigate the three Groupaction contracts totaling \$1.6 million. In May 2002, then Auditor General, Sheila Fraser, released her Groupaction Report, revealing severe shortcomings at all stages of the contract management process, as well as a failure on the part of Groupaction to fulfill the services for which it was contracted and paid to perform.

The Auditor General referred the Groupaction matter to the Royal Canadian Mounted Police (RCMP) for further investigation. In September 2002, the RCMP raided the Montreal offices of Groupaction in a search for evidence relating to their sponsorship contracts.

In addition to referring the Groupaction matter to the RCMP, the Auditor General announced that her office would undertake a government-wide audit of all advertising and sponsorship activities since 1997. In her report, released in February 2004, the Auditor General found a persistent pattern of mismanagement in government sponsorship contracts that had cost Canadian taxpayers millions of dollars.

Her revelations led to the Martin government establishing the Gomery Commission<sup>83</sup> to conduct a public inquiry and file a report on the matter. The official title of this inquiry was the Commission of Inquiry into the Sponsorship Programme and Advertising Activities.

#### **5. Basic Facts**

Besides the mismanagement of public money for the "sponsorship programme", the inquiries found the following political finance violations:

- ▶ sponsorship money awarded to advertising firms in return for little or no work, with these firms instead maintaining Liberal organisers or fundraisers on their payrolls, or donating back part of the money to the Liberal Party;

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83. The Canadian Encyclopedia (21 September 2006), Sponsorship Program and Advertising Activities (Gomery Inquiry), Commission of Inquiry into, available at [www.thecanadianencyclopedia.ca](http://www.thecanadianencyclopedia.ca); Commission of Inquiry (1 February 2006), Phase 2 Report, Available at <http://epe.lac-bac.gc.ca>, Accessed on 24 July 2015.

- ▶ an audit found that sponsorship contract recipients donated a total of \$801,000 “back” to the Liberal Party of Canada;<sup>84</sup>
- ▶ in addition, one of the advertising firms’ executives made \$1.8 million in “indirect” or unaccountable donations. The audit was unable to determine how much of that money actually went to the party;
- ▶ party officials have confirmed receiving envelopes full of cash but forensic experts say the “actual amount is unknown.”

## 6. Evidence used

The findings relied in particular on the following evidence:

- ▶ documents from a search by the police of the Montreal offices of the advertising firm Groupaction;
- ▶ witness testimony in the public Gomery inquiry.<sup>85</sup> In the most explosive testimony at the Gomery Commission, one of the advertising executives, Mr. Brault, testified that he participated in several schemes to defraud the federal government and funnel money to the Quebec-wing of the Liberal Party of Canada. Under these schemes, Groupaction received preferential treatment in obtaining sponsorship contracts and was allowed to submit false invoices to the federal government for services it never rendered. In return, Mr. Brault provided money and support to the activities of the Liberal Party in Quebec. Mr. Brault testified that, in one scheme, he agreed to provide Jacques Corriveau, a Liberal Party organiser in Quebec and friend of Prime Minister Jean Chrétien, with a percentage of the commissions that Groupaction received from sponsorship contracts. Mr. Brault also testified that he repeatedly arranged large cash donations to the Liberal Party, in addition to placing Liberal election workers on his payroll, even though they were working exclusively on Party business;
- ▶ an audit report by a panel of three forensic accountants tasked by Justice John Gomery.<sup>86</sup>

## 7. Outcome

Two stakeholders in the scheme were tried in criminal court – a government official responsible for the sponsorship programme and one advertising executive. They were sentenced for fraud and other offences to fines and imprisonment of up to three-and-a-half years.

Even though the Gomery-Commission found that two successive Executive Directors of the Liberal Party were directly involved in illegal campaign financing, there was not enough ground for criminal indictment. Similar is true for many Party workers who accepted cash payment for their services when they should have known that such payments were illegal under the Canada Elections Act.

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84. Commission of Inquiry (18 May 2005), The “Kroll Lindquist Avey Report”, Available at [www.cbc.ca](http://www.cbc.ca), Accessed on 24 July 2015.

85. Commission of Inquiry (1 February 2006), Phase 2 Report, Phase 1A, Available at <http://epe.lac-bac.gc.ca>, Accessed on 24 July 2015.

86. Commission of Inquiry (18 May 2005), The “Kroll Lindquist Avey Report”, Available at [www.cbc.ca](http://www.cbc.ca), Accessed on 24 July 2015.

However, the revelations from the unraveling scandal would cost the Liberals dearly in the election of June 28, 2004: their majority evaporated and – for the first time in 25 years – Canada had a minority government.

After the parliamentary election on Jan. 23, 2006, the Liberals found that for the first time in 12 years, they did not have enough seats in the House of Commons to govern. The Conservatives picked up 10 seats in Quebec, prompting the new Prime Minister, Stephen Harper, to say the scandal had inflicted “enormous damage to the image of federalism” in Quebec.

Harper’s government introduced the Accountability Act in April to crack down on unethical actions and make government transparent.

## **9.5 Estonia: Misuse of public resources for an election campaign<sup>87</sup>**

### **1. Basic facts**

On a video in November 2014 made by the ruling Reform party, the Prime minister of Estonia Taavi Roivas chief of this party was shown walking on the runway of an air force base, the Amari Base, with a NATO fighter plane above his head. This video was released before Parliamentary elections in March 2015. The picture of the plane flying over the head of Mr. Taavi Roivas was a montage. The Estonian Prime minister declared in that video “*Firmly Forward*”.

This promotional video was regarded by the press and by the public opinion as an abuse of state resources. The official policy of Defence Forces was opposed to this intervention but Defense forces declared other political parties could have access to this military territory provided it does not damage security but within the following limits: “*Even so, the Defence Forces requests that the openness be not used for political aims*”. The Defence Forces confirmed that the Prime minister’s office contacted the air forces and the air force granted permission to film, while not specifying who exactly did that. In practice it has been said afterwards that the idea to shoot the prime Minister had been suggested by an advertisement agency. An advisor to the Prime minister had contacted the air force base and a production company entered into an agreement with the air base.

At a press conference focused on NATO and the European security, Mr. Taavi Roivas stated later: “*As a Prime Minister, chairman of a party and an Estonian patriot I am proud of the Amari Base. I am proud of the Estonian Defence Forces and I will do all in my power to help them defend us even more. I understand your interest to find an intrigue but I find that Amari has become a might symbol of Estonia’s defence. As Prime Minister, as chairman of a party, I am always focused at us doing all in the name of defending ourselves even more*”.

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87. See Prime Minister drags Defence Forces into politics, Available from: <http://m.postimees.ee>; Accessed on: 9.07.2016

## 2. Considerations and outcome

The president of Estonia, Toomas Hendrik Ilves considered that defence forces and security-related agencies had to be kept separate from election campaigns: *“issues related to security of the Estonian state are obviously part of our political debate but defence forces and other agencies related to security are depolitized, as befitting a democratic state and thus they need to be kept separate from election campaign”*. The case was challenged too within the Estonian party funding supervision committee. It took the view that the idea of filming the prime minister on this air base came from the producer hired for the video and there was no evidence of any influence of the cabinet of the prime minister on the decision but the committee made a reproach to the officials of the air base for having permitted this film.<sup>88</sup>

## 9.6 Spain: Dual financial statements of political parties

### 1. Basic facts

In March 2015, the Spain’s High Court has ended an inquiry into the slush funds of the country’s ruling party Popular Party which were removed from the legal economic circuit around to the country. They were used to pay for election campaigns and another party business including the 1.6 € million refurbishment of national party headquarters. The 190 pages report of the investigating judge considered that the party between 1990 and 2008 used to operate *“through various account systems that recorded monetary inflows and outflows outside the official accounting declared by the party and files with the Audit Court during the 18 years in question”*. This financing system breached the requirements and conditions laid down by the law. This money was provided by some of the biggest construction tycoons in Spain. The affair originated in 2009 as a judicial investigation into alleged kickbacks involving members of the Popular Party and construction companies (OHL, FCC, Sacyr Vallehermoso).

### 2. Considerations and outcome

The investigating judge called for Luis Barcenas, treasurer of the Popular Party at that time and senator to stand trial on charges of tax fraud and embezzlement and referred the case to the state prosecutor.<sup>89</sup> Mr. Barcenas admitted that a list of alleged illegal payments within the party which was published in the El Pais newspaper was in handwriting. Mr. Barcenas said later he had made numerous bonus payments in cash to Mr. Mariano Rajoy, the Prime Minister, chief of the Popular Party and other senior party members out of the party slush fund of donations by business. Mr. Barcenas avoided admitting that some donations were directly linked to granting of public contracts. Such an admission would risk a conviction of bribery which

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88. See Guardian, “Spain’s ruling party ran secret fund for 18 years, investigating judge finds”, Available from; Accessed on: 9.07.2016

89. Mr. Barcenas resigned in 2009 after being indicted in the early stages of an investigation into a scheme of kickbacks and illegal payments. When he resigned Mr. Barcenas took with him nine boxes of documents from his offices. Mr. Barcenas is also involved in the Gürtel kickbacks-for-contract case.

carries a heavier penalty than other offences committed in the case and remains punishable even after 10 years have elapsed.

Mr. Mariano Rajoy admitted making a mistake by putting trust: *"in someone who we now know did not deserve it. But he denied" committing the criminal offence of covering up for someone who is alleged to be guilty*".

These scandals show three kinds of irregularities:

- ▶ Construction companies appear to have made large illegal donations to one of the two most important political parties in Spain;
- ▶ The annual financial statements of election campaign and party's activities of the Popular Party between 1990 and 2008 were not reliable;
- ▶ The party maintained parallel accounts with off-the-books accounts.

## **9.7 France: Significant excess of the spending limits for a Presidential election<sup>90</sup>**

### **1. Basic facts**

The spending ceiling for the French 2012 presidential election was 16,851 million € for the first ballot and 22,509 million for the second one. Expenses are considered as electoral expenses liable to a flat reimbursement in the limit of the ceiling of expenditures when they aim at obtaining votes and be engaged by the candidate or within his agreement within the legal electoral campaign period which started for this election one year before the first day of the month in which the election takes place.

### **2. Considerations and outcome**

In the first instance on the 19 December 2012 the supervision body rejected the campaign account of Nicolas Sarkozy, candidate to the 2012 presidential election. It took the view that he exceeded at 363,615 € the threshold of electoral expenses, which meant 1,61% of the limits of electoral expenses. Nicolas Sarkozy had to reconstitute the lump sum advance of 153,000 € too he received as a candidate. This decision was challenged by him within the Constitutional Council. It confirmed on the 4<sup>th</sup> July 2013 the rejection of the campaign account of Nicolas Sarkozy by the monitoring body and considered after a review of the case that expenditures of Nicolas Sarkozy exceeded 2,1% of the threshold of the electoral expenditures. Nicolas Sarkozy lost his public reimbursement which amounted to 10,8 million €. The Constitutional council reintegrated into his campaign account different expenses the candidate considered as related to the preparation of the presidential election or to the following legislative elections. The relevant expenditures were expenses for the organization of political meetings and public conferences, printing of leaflets, services of public relations agencies and candidate's website. According to the Constitutional council the total exceeded the authorized limit by 466,118 €. His political party (Union pour un mouvement populaire) paid for him the public reimbursement of 10,8 million €, which was around the third of the annual budget of the party.

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90. See Independent, "Nicolas Sarkozy 'exceeded campaign spending limits'", Available from: <http://www.independent.co.uk>, Accessed on: 09.07.2016

This excess of ceiling of electoral expenses did not stop here. In February 2016, Nicolas Sarkozy was placed under formal investigation by the justice on preliminary charges of illegal overspending during the 2012 presidential election campaign. Thirteen people including executives at a PR company and aides close to Nicolas Sarkozy have been placed formal investigation in that case.

On one hand the PR company closed to the political party of Nicolas Sarkozy was suspected of false accounting. This company was in charge of thematic events over 18 million € which never existed or were overestimated. So the case was initially not about the election campaign's accounts of Nicolas Sarkozy but about a fraud system which was supposed to have enriched the leader of the party, Jean-François Copé.

On the other hand the political party of Nicolas Sarkozy has been suspected of covering spending that illegally exceeded the limit set by law. A senior official of the party admitted that the costs of the election exploded and these expenses had been made by the party and had not been integrated in the campaign's accounts of Nicolas Sarkozy. They should have been added to the excess of the ceiling of expenditures recorded in 2012 and 2013 by the monitoring body and the Constitutional council. This supplementary excess was estimated in February 2016 at 13 million €, while 10 million € have been declared officially for the funding of the presidential election by the party in its annual financial statement 2012. These 10 million € should have been reimbursed to the party by the candidate with the flat reimbursement he lost. A judicial procedure is ongoing.

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