

Part 1

Summary of the Main Issues

Earlier this year I was asked by the Prime Minister to review our system of party political funding and to try to reach as much agreement as possible between the parties on a way forward. I have been asked to report by the end of this year.

This interim assessment sets out the main issues as they appear to me, and the choices which face the public and the political parties.

The purpose of publishing this assessment now is to stimulate and inform public debate, so that I can hear public and party reaction to the issues outlined here, and take this into account as I enter final discussions with the political parties.

The role of parties

For many people party politics is a turn-off. Party membership has substantially declined. There is widespread disenchantment with politicians. Yet everyone knows that parties are essential to democracy and there is no mature democracy anywhere in the world in which political parties do not play a vital role. People also know that party politics, and the abilities of those who choose to enter it, are of central importance to the quality of leadership, and the prosperity and the reputation of our country. We elect a Government through a Parliamentary democracy which is not about voting on single issues but about a wide range of important choices and priorities. Party politics is a competition to serve the public interest: that is its purpose.

There is widespread disenchantment with party politics, not only in the UK but in many other democracies. Turnout at elections has fallen. So has membership of political parties. In the 1950s one in 11 people belonged to a party: now it is one in 88. When it came to power in 1997 the Labour Party had around 400,000 members. Now it has around 200,000. The situation is similar for the Conservative Party as well, which has seen a long-term decline in its number of members.

Trust in politicians at a national level and trust in political parties are both low, and have been subject to a long-term decline. Polling research indicates that people feel distant from parties, and they feel that parties are only interested in them at election times. According to research undertaken by Ipsos MORI for the Committee on Standards in Public Life, trust in “your local MP” is relatively high at 48%, especially where the MP is seen as being active in the constituency, while trust in “MPs in general” is at 29%.

While membership of political parties has fallen, membership of single-issue groups has risen. This voluntary activity is of course welcome, but it cannot be a substitute for party politics. Parties have to balance out competing claims upon government. That is why no modern democracy has been able to do without political parties. A healthy democracy needs healthy political parties.

Tackling party funding alone will not resolve the problem of cynicism about party politics. The central challenge is for the politicians themselves across a much wider front. However, any changed system of party funding should try to bolster public confidence and help recapture the true mission of party politics as serving the public.

The funding of parties and regulation

Some views put to us in the course of the Review so far reflect a belief that political parties are or should be on the whole unregulated bodies, like social or sports clubs. But that position has gradually been eroded. The leader of the main opposition party has been paid out of public funds for 70 years; candidates in elections get free mailshots; parties receive free broadcast time at election time; and parties have received money from public funds for representational activity for many years. Those parties represented in Westminster now receive grants for policy development as well. Parties were recognised in statute and regulated in law by the *Registration of Political Parties Act 1998* and the *Political Parties, Elections and Referendums Act 2000*. It is somewhat misleading, therefore, to continue to speak of parties as if they were entirely unregulated bodies. There is a public interest in the political parties. Healthy opposition is as essential to democracy as government.

The number and nature of political parties have also changed. We have devolved administrations functioning in Scotland and Wales, and a latent devolved administration in Northern Ireland, as well as a plethora of different voting systems. The funding system needs to reflect the reality of this changed political situation and the needs of smaller parties, and enable entry to the political arena.

In recent elections we have seen the growth of smaller parties. In the 2005 general election parties and candidates other than the three main parties won more than 10% of the vote. In comparison, in 1979, the share of the vote was less than 6%, and in 1955 less than 2%.

Despite the existing contributions from public funds, the finances of most parties are fragile. The Labour Party remains dependent on trade union affiliation fees (though not as much as 20 years ago), and the three main parties have had to rely increasingly on donations or loans from a small number of very rich individuals. After the recent controversies about these, that source may well dry up, possibly of its own accord, even without any new step to cap the amount individuals or organisations can give.

Nonetheless, in spite of these problems there is a case to be made for making little change to the present system. The simplest argument for this is that the parties have got into trouble by themselves and they should sort themselves out. But this may miss the underlying challenge to party financing. It certainly misses out the public interest in financially healthy political parties, and what parties can do in the public interest.

A more sophisticated argument for avoiding major change now is that some of the problems which have arisen may be the result of the new regulatory regime of transparency: donations, and now loans, have to be disclosed; there is a limit to what parties can spend to campaign at elections; and some public funding is available for defined purposes. Change should be avoided, so the argument goes, as the problems that have arisen so far show in fact that the system is working.

This minimalist approach would leave people free to give what they want to parties, and it could involve some changes to the role of the regulator – the Committee on Standards in Public Life is looking into that – to help increase its effectiveness. But the problem about doing little or nothing is that it does not address the underlying fragility of party finances nor does it do anything about public confidence in parties.

Limit spending

At general elections, there is an existing limit on what parties can spend on campaigning based on an allowance of £30,000 per constituency contested. This results in a ceiling of almost £19 million for the three main parties, depending on the number of seats contested (the three main parties tend not to contest all the seats in Northern Ireland). In the 2005 general election their respective expenditure was £17.85 million for the Conservative Party, £17.94 million for the Labour Party, and £4.32 million for the Liberal Democrats.

Reducing the ceiling further may help close the gap between income and expenditure. It might also encourage more local campaigning and greater engagement of voters in the communities in which they live. It would respond to the perception that parties spend far too much on campaigning and could force parties to spend with a clearer eye to value for money in what they do to persuade the voter.

However, it has been put to me that lowering the ceiling further implies that “campaigning” is somehow a bad thing, ignoring the part it plays in informing the electorate. Running a professional campaign which meets modern communications expectations and complies with the rules is expensive.

If the expenditure limits are decreased there are two consequential decisions. First we need to agree the new ceiling – some have suggested £15 million, others £10 million or £12 million.

Second, a view needs to be taken on the period over which campaigning expenditure needs to be capped. There are many more elections than ten years ago. The campaigning cycle extends well beyond the annual period currently set for a general election. Considerable sums are spent in marginal seats outside the controlled period. The logic of this pattern might be to cap national and local campaign expenditure all the time. The question is whether this is proportionate and whether parties, especially locally, can manage the practical demands of greater accountability; and whether the cost of compliance on small parties is too great.

Limit donations

One of the most common responses to the charge that large donations to political parties buy influence is to say that the law should limit the amount any individual or organisation can give. Other countries, for example the USA and Canada, have such limits. On the face of it this would be a direct response to recent criticism and concern. Indeed it can be argued that if the limit is set relatively low (what that may be is a pretty subjective judgement) then it would have the further benefit of obliging parties to search for more small donations and therefore engage more people.

Before anyone ticks this box in an automatic way four things must be thought through.

The first is where this would leave the main parties financially. If you assume that existing donation patterns and sources continue, and that Trade Union affiliation fees are caught by any cap, the arithmetical consequence is a shortfall for the main parties in the following range:

	Limit/Cap £100,000 – £5,000
Conservative Party	£3.1 – 7.2m
Labour Party	£6.9 – 12.6m
Liberal Democrats	£0.6 – 1.3m

Of course, these precise levels are not likely to occur because parties and donors will change their behaviour, but in ways that are difficult to predict. (A detailed analysis of the possible range of shortfalls is in Annex G.)

The second is the risk of evasion or avoidance, such as channelling donations through others, for example, giving amounts up to the cap to friends to donate; or alternatively through funding other organisations which campaign in the interests of a particular party without giving it the funds directly. Of course some of this risk can be dealt with by closing off obvious loopholes in law, although this adds to the complexity and bureaucratic weight of regulation.

The third is the consequence for the constitution of the Labour Party in which historically some trade unions and socialist societies are, by virtue of affiliation fees, “corporate” members. It has been put to me with some force that a change in funding arrangements should not be constructed so that it forces a change in the way in which a political party chooses to organise itself. Others argue, with equal force, that a major political party should have both the resilience and flexibility to sustain the constitution it wants despite new financing requirements.

The fourth is that it may not be sustainable to set a limit on donations without some increase in public funding if the financial health of parties, and not just the large ones, is to remain stable.

Public funding

Adding to the amount of public funding which parties receive is not popular, but there are clear arguments in favour of it as well as against it. Simply put it would help ensure financial stability and underline the real public interest in healthy political debate. If allocated according to votes cast at one or more previous general elections, and in relation to elections for the devolved administrations, it would, depending on the threshold set, assist smaller parties and not just the big battalions. It could also encourage voter turnout in safe seats. A significant amount of public funding is a settled component in the Westminster-style democracies of Canada, Australia and New Zealand; and also in many continental European countries.

Resistance to more public funding comes in a number of forms. Some oppose this as a matter of principle, although the principle has been breached in practice for some time. Others argue that they do not want “their” money going to a party with whose views they disagree; others that it would actually lead parties to engage with voters less, especially if it led to greater centralisation and less local activity. It is possible to point to examples from abroad where significant public funding of parties has not removed the risk of abuse or perceived abuse.

It is quite clear that public funding should not be dismissed out of hand, but serious consideration given to both the merits as well as the drawbacks. Some commentators and some reports and research have suggested two ways in which more public funding might flow to parties other than as a general subsidy.

One way would be to reward membership, and encourage parties to attract more members or more small donations, by some scheme of matched funding. It is argued this would provide an incentive for parties to engage more directly and regularly with voters, particularly if funds were to flow to local parties as well as to the centre. However, it would be important to take account of the cost of administering and regulating a system which might cover thousands of small donations or small sums of matched membership fees.

Another suggestion would be to provide more public funds for defined activities which are in the long-term interest of developing a better informed relationship between parties and voters. The existing public funds are designed to assist parties to discharge their Parliamentary duties such as representing constituents, and formulating policy. Any increase in public funds might further

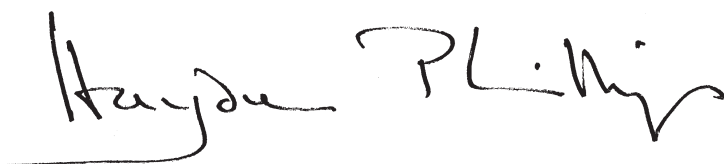
support these activities and others which are clearly in the public interest. Any such increase could cover research, training and educational activity, for example, leaving the parties to find other sources for general administration and campaigning.

Conclusion

I have tried in this introduction to bring out the central issues although beneath them lies much technical complexity. Much of that detail can be found in the rest of this assessment.

Finding a consensus on a new way forward for party funding will not be easy. The reform of party funding is not an end in itself, but a means to achieve the wider benefit of improving the quality of democracy. From the reaction the Review has received so far, I believe that the achievement of a good measure of cross-party agreement would be welcomed by the public. For that reason alone the process of the Review must be openly explained and not perceived as a private agreement only in the interests of the established political parties. Achieving agreement will require not just facilitation but an act of political will, including a readiness to accept that no one party will necessarily be able to achieve all of its objectives.

I have been asked to report to the Prime Minister by the end of December. I now want to take public reaction to the issues set out in this interim assessment into my discussions with the political parties.



October 2006

The Structure of the Interim Assessment

The interim assessment consists of two parts, the first part setting out what the key issues are and where choices may need to be made, and the second part providing more of the factual detail and analysis in a series of Annexes.

In the first part, the above summary set out the key issues, without going into particular detail on any of the options. The next section gives an overview of what the current arrangements are for political parties, in terms of the regulations that exist regarding their income and expenditure.

Following that overview is a section setting out a number of possible scenarios or packages of measures which can be envisaged for a changed system of party political funding.

The Annexes can be split into three main sections. The first section provides information about the Review, including its processes and objectives; the second section provides background information on the current system of party funding in the UK; and the third section provides more detailed analysis of some of the issues discussed in the scenarios.

Existing Arrangements

Historically, political parties were private organisations, largely unregulated as far as their finances and organisation were concerned. It is only with the changes introduced in the *Political Parties, Elections and Referendums Act 2000*, following the Fifth Report of the Committee on Standards in Public Life (the Neill Committee), that their financial activities became substantially regulated. Parties now have to register with the Electoral Commission if they wish to put forward candidates for an election. Parties also have to submit annual accounts to the Electoral Commission, which publishes them on its website.

Parties are primarily funded by donations and membership fees. They also receive some public funding, including support in kind. There are strict rules about what parties and candidates can spend at elections.

Income and expenditure

The average income of the Conservative Party over the last five years has been in the region of £20 million per year, while the average expenditure has been £27 million. For the Labour Party these figures are respectively £28 million and £32 million, and for the Liberal Democrats both are in the region of £5 million.

The amount of funding a party receives fluctuates and is linked to popular support, with more donations being received when the party's popularity is greater, and also in the build up to a general election. Overall expenditure is also obviously higher for the year in which a general election takes place.

In 2005, according to the annual statement of accounts, the total expenditure, including campaign expenditure, for the three main parties was as follows, with campaign expenditure then shown separately. As different criteria are used for the annual statement of accounts compared to the campaign expenditure return these figures differ slightly from those quoted earlier.

	Total expenditure	Campaign expenditure
Conservative Party	£39.2 million	£15.7 million
Labour Party	£49.8 million	£15.2 million
Liberal Democrats	£ 8.8 million	£ 4.9 million

The average annual expenditure for the Conservative and Labour parties, excluding campaign expenditure, is in the region of £20 million. This includes costs such as accommodation, IT, servicing their membership, as well as activities such as developing policy.

According to the annual statement of accounts, as of 31 December 2005, the Conservative Party had total net liabilities of £18.0 million, and the Labour Party £27.2 million. The Liberal Democrats had total net assets of £298,000.

Donations

The majority of the three main parties' income, somewhere between 50–80%, comes in the form of donations. There are currently no limits on the amount that political parties can receive from any one individual or corporation. This has led to some disquiet about large donations and loans accepted from high net-worth individuals.

Donations are subject to regulation to make the system fair and transparent. The rules cover the reporting of donations and the identity of donors. This applies across the whole of England, Scotland and Wales, but Northern Ireland is currently exempt from some aspects of the donation reporting requirements due to the particular situation that exists there. It is due to come into line with the rest of the UK over the course of the next few years.

Any donation to a political party of over £200 must come from a “permissible donor”. This is anyone on the UK electoral register, companies or organisations registered and carrying on business in the UK, trade unions, and unincorporated associations.

If a public listed company wants to give money to a political party the company has to ask its shareholders for their approval. Other companies are free to donate according to their own internal rules, as long as the companies are active and registered in the UK.

Trade unions have to ballot their members every 10 years on whether the union should have a political fund. If the membership votes in favour of a political fund, each member pays a certain amount into that fund. The union may then decide to affiliate to the Labour Party, and would then pay the affiliation fee, currently £3 per member per year. Twenty-nine unions currently have political funds, of which 17 affiliate to the Labour Party.

Any donation of over £5,000 made to the main political party offices must be reported to the Electoral Commission, as must donations of over £1,000 to constituency or local party offices. Parties must report any such donations to the Electoral Commission every three months or, in a general election campaign period, every week. The Electoral Commission then publishes this information on its website.

Loans now come under the same rules as donations, and have to be reported in the same manner.

Expenditure

There are limits set on the amount parties and candidates can spend at certain elections on items and activities directly related to getting candidates elected. Limits on what candidates can spend on campaigning at elections, introduced in 1883, were intended to stop election results being bought. Limits on what a party could spend on campaigning nationally at an election, introduced in 2001 following a recommendation by the Neill Committee, were also intended to stop excessive spending at elections. For a general election the candidate limit comes into effect five to six weeks before an election, while the national party limit comes into effect 365 days before an election. Both limits cover only money spent on campaigning and not routine expenditure.

The national campaigning limits for a party apply at general elections, European Parliamentary elections, Scottish Parliamentary elections, National Assembly for Wales elections, and Northern Ireland Assembly elections. Limits do not apply to parties at local elections.

At a general election a party can spend £30,000 multiplied by the number of seats the party contests. So for a party contesting the elections nationwide the limit is in the region of £19 million.

Generally, money spent on campaigning nationally, such as billboard campaigns, and aimed at promoting the party, counts as national expenditure, no matter where the activity takes place or where it is delivered.

The limits on what candidates can spend are based in general on the number of electors in any constituency. These limits apply at all elections where electors can vote for individual candidates, but not to candidates on a party list.

A candidate at a general election can spend around £10,000 to £13,000, depending on the number of people who can vote in each constituency. This is separate from what parties can spend. Lower limits exist at local and devolved elections.

Public funding

In addition, there is already some public funding available to parties and candidates, both direct funding, in terms of grants, and indirect funding, in terms of benefits provided in kind. More detail is provided in Annex E.

Eligible parties in the House of Commons receive direct funding in the form of grants to support their Parliamentary activities and to support their development of policy. A similar scheme exists in the House of Lords.

Eligible parties represented in the devolved administrations also receive support for their representative activities, although they do not receive any money for policy development.

Indirect funding mainly supports campaigning activities. For example, each candidate at a general election is entitled to free postage for one election mailing to each elector in the constituency.

In addition, political parties do not have to pay for the airtime they obtain for party political broadcasts. In general, party political broadcasts are available to all parties that stand candidates in approximately one-sixth of the contested seats.

Incumbency

There are also benefits that a party or elected representative receives due to having been elected. Such incumbency benefits include special advisers for the government of the day, who are paid for out of public funds to provide political advice to cabinet ministers.

Benefits that MPs receive include the Incidental Expenses Provision available to meet costs they incur in the course of their Parliamentary duties, but not on party political activities or campaigning. This might include, for example, reimbursement for part or all of the cost of sending a newsletter to constituents.

There are further incumbency benefits for parties in local authorities in Great Britain, where the three largest party groups in each local authority are entitled to political assistants, paid for out of public funds.

The Funding of Political Parties: A Survey of the Main Choices Involved

There are a number of possible scenarios or packages of measures which can be envisaged for a changed system of party political funding. Each of the measures has drawbacks or risks as well as advantages. Some hard choices have to be made and, if a good measure of consensus is to be achieved, the political parties will have to make some compromises about their own preferences. Questions are posed at the end of each scenario as I want to hear what the public thinks about each one and encourage discussion of these different choices.

Four scenarios or packages of measures are presented on the following pages. These are not intended as discrete options from which a choice must be made but as ways of illustrating the nature of the choices and the arguments involved. These are presented in terms of increasing degrees of change over the present arrangements.

Scenario 1: Minimal change

The first consideration should be whether to keep things as they are now, and to start by evaluating the merits of the current system.

Is there a case for change?

When compared to other jurisdictions, the British political system, taken as a whole, has been remarkably free of abuse. Examples of abuse are the notable exception to the general rule.¹

The Electoral Commission has some of the widest-ranging powers of any electoral regulator around the world available to it to investigate and enforce the law relating to political party finances.² Whether these powers are the right ones is an important regulatory issue.

The current system for regulating party funding is relatively new. The scale of these changes should not be underestimated. Recent events may be the growing pains of the significant changes that have taken place as transparency has taken effect. For the first time, the public has been able to find out who donates what to political parties, and how much.

It may be too early to assess the impact of these changes and therefore too soon to make any changes. Implementing changes to the system would cost the parties and the regulator both time and money. Any benefit from changing the system would need to outweigh these costs.

The *Electoral Administration Act 2006* now requires loans to be reported in the same way as donations. It could be argued that as one of the prime concerns over political party funding has now been addressed, no further changes are needed.

The Committee on Standards in Public Life is currently reviewing the role of the Electoral Commission. Their recommendations, if accepted, might provide a basis for some further regulatory changes without changing the way parties are funded. Suggestions have also been made to the Review of areas where minor change may be needed, for example eligibility for policy development grants. Making these small adjustments coupled with any recommended changes to the Electoral Commission may be sufficient change.

There are, however, three significant reasons for changing the system. Firstly, to respond to the suspicion and concern the public have. Public confidence in political parties and specifically their

financing arrangements continues to decrease. Public expectation and press comment suggest minimal change would be inadequate.

Secondly, politics is changing. The pattern and rhythm of elections have changed rapidly. The long-term decline in participation in party politics is still continuing. This has had implications that the Neill Committee could not have foreseen back in 1998. Since then, the Electoral Commission, thinktanks such as the New Politics Network, the Hansard Society and the Institute of Public Policy Research (ippr), and others have argued that party funding needs to be addressed.

Lastly the parties themselves are recommending changes, and there is an opportunity to work with them to create a consensus. There is no guarantee that this opportunity would present itself again at a later date.

Do you think the current system (with a few minor changes) needs further time to bed in before thinking of more radical change?

Scenario 2: Increased transparency and greater expenditure control

Scenario 2 builds on existing transparency (section A) and existing expenditure control (section B). By enhancing these measures it may be possible to improve public confidence in party funding and ensure that political parties compete on the basis of policy and competence rather than their funding.

2A Donations controlled through increased transparency and public scrutiny, with no caps on donations

The existing system for the funding of political parties introduced in 2001 seeks to regulate donations through transparency. Transparency provides the public with the information on the finances of political parties and lets them draw their own conclusions.

Possible areas where transparency could be increased include:

- For donations over a certain amount, further information about the donor could be made publicly available listing the donor's financial, commercial or other interests. This could be similar in its coverage to the information required in the House of Commons Register of Members' Interests.
- Corporate donors or individual donors holding senior positions in companies could be required to declare any government contracts the company has or is seeking.
- The frequency of reporting could be increased to allow "real time" scrutiny by the public.
- The transparency of trade union political funds could be increased. In addition to the information they are required by law to publish and distribute to members on the balance of the political fund, they could also be required to publish a breakdown of how the political fund was spent.
- Donations from unincorporated associations (i.e. organisations not registered as companies) could be made more transparent. They might be required to disclose their sources of income and the identity of their directors.
- All companies, whether public or private, could be required to reveal any donations or loans made to political parties in their annual accounts.

Advantages

Increased transparency would help public scrutiny become more effective. The requirement for further information about donors giving large sums may make giving sizeable donations less attractive. It concentrates on the root cause of concern over party funding, that is the perception that donors are trying to buy influence. Rather than relying on the media to investigate possible conflicts of interest, more information would be available for all to come to their own conclusions.

Transparency as opposed to a cap on donations would still allow individuals to spend their money as they choose. It avoids using a financial mechanism to change the behaviour of political parties and is more in keeping with the voluntary tradition of political parties.

Greater transparency would be easier to enforce than a cap on donations (this is discussed further under scenario 3). Transparency may be seen as a way the public impose their own views on what is acceptable. It may therefore be more flexible to specific circumstances.

Disadvantages

The main disadvantage is that increased transparency alone may not be sufficient to increase public confidence in how political parties are funded. Following the recent public concern about the unacceptability of large donations and loans, specific measures such as a cap on donations may be needed.

Evidence from other jurisdictions suggests that greater transparency can result in public confidence decreasing; greater disclosure may prompt more stories in the media alleging impropriety.³ While deterring wrongdoing and uncovering it when it does occur are the major benefits of greater transparency, there is a danger that there may be unrealistic expectations that allegations of abuse will be removed. Further rules could suggest there is something fundamentally wrong with our system when this is not actually the case.

Some feel that donors should have a right to privacy, particularly as publicity around a donor may be out of proportion with the amount they have given. Requiring companies to declare they are bidding for a contract could affect them commercially. As a result, transparency may discourage some people or organisations from donating to political parties.

It would be difficult to enforce a register of donors' interests or companies involved in government contracts, as the information in it would be difficult to verify independently. Setting a timeframe in which donors had to declare this additional information would be difficult, as allegations may relate to donations made years before any alleged benefits gained.

2B Reduce the amount parties can spend on campaigning at elections

With the benefit of five years' experience of operating national limits on election campaign spending, it can be argued that national limits do seem to have worked in practice. While some specific operational concerns have been raised around definitions of national and candidate expenditure and the definition of an election period for candidate expenditure, no one seems to be arguing for the removal of the expenditure limit.

There are still, however, areas of concern about campaigning at elections. Public confidence remains low, with research suggesting that campaigning through mass marketing does not engage the public.⁴ The public felt that parties spent some of their money frivolously while campaigning at the 2005 election. Therefore, it is important to look at whether the current limit is the right one.

A strong case has been made to the Review that regulation of party expenditure should try to redress the shift away from local campaigning. Research suggests that the public have higher levels of trust for politicians they know, but low levels of trust for politicians in general.⁵ Local campaigning activities are more likely to encourage people to participate in politics.⁶ The relationships at a local level between political parties and the public seem to be important for democratic engagement. Along with reducing the national limit, the candidate limit could be increased.

Annex F has a more detailed discussion of concerns about how the existing national and candidate limits operate in practice.

Advantages

As expenditure limits were first introduced to help relieve the pressure on political parties to raise substantial amounts of money, an argument can be made that, as this pressure still exists, the limits should be further reduced. Transparency has not yet had the desired impact on how parties raise their income.

Some would also argue that political parties have other functions to carry out as well as campaigning, such as research, policy development, developing leadership skills, education and local civic action.⁷ Over the last 20 years, parties have been concentrating more of their resources, which due to the fall in party membership are mainly financial resources, into campaigning at the expense of these other functions of public benefit.

This may be partly because the number of elections has increased. Elections for the devolved administrations and the London Assembly in addition to local, general and European Parliament elections mean that since the late 1990s in some parts of the country barely a year has gone by without an election being fought. Reducing the amount parties can spend to campaign at elections could encourage them to refocus their resources towards other activities, with possible benefit for local democratic engagement.

There is also a large difference in what the parties are able to spend to campaign in elections. At the 2005 general election, the Conservative Party and Labour Party each spent about six times the total of the Liberal Democrats. Lowering the national expenditure limit for campaigning may help small and new parties to compete with the two principal established parties.

Disadvantages

While reducing the amount parties can spend on campaigning at elections may encourage them to spend more on other activities, this may imply that somehow election campaigning is a bad thing. Campaigning brings many benefits: it informs the public and encourages them to make decisions about their political priorities. An argument can be made that increasing, or at least keeping, the current limits on national party campaign expenditure is positive for democracy.

Parties are under pressure to be professional. Competing for attention with consumer advertising and the mass media has made polished presentation increasingly important. This all requires parties to spend more. Lowering the national campaign spending limit may not reduce the pressure if it does not address the reasons for current spending levels.

While introducing a national limit on campaign spending does not seem to have decreased the central role of political parties in elections, there is a risk that a further reduction might do so, with a detrimental effect on the quality of debate during election campaigns.

Some would argue that concerns over how much parties spend and what they spend it on are for parties to deal with. For as long as parties remain in essence voluntary organisations receiving the majority of their money from private sources, some would argue an expenditure cap is an act of overregulation.

The national expenditure limit has not been adjusted for inflation since it was introduced, so has already been decreasing in real terms. As the national limit is calculated according to the number of constituencies a party has candidates standing in, recent reductions in the number of constituencies have had the effect of reducing the national limit.

Do you favour the specific ideas described in scenario 2 for increasing transparency?

What do you think of the idea of decreasing the amount parties can spend nationally on campaigning?

Do you think the amount that can be spent on local campaigning should be increased?

Scenario 3: Cap on donations in addition to:

greater transparency; and greater expenditure control

This scenario adds in a cap on donations to greater expenditure control and greater transparency. This directly responds to public concern that donors who give large sums gain undue influence. It would increase equity for parties who do not receive large donations but may not be perceived as fair by some parties where particular income streams would be affected.

The purely financial implications for political parties of setting a cap at particular levels are discussed in Annex G. If a cap were applied to organisations as well as individuals then this would have a substantial effect on Labour Party income, and some argue, on the way the Labour Party is constituted. This is discussed in more detail in Annex H.

A Cap on donations, limiting the amount individuals and organisations can donate to political parties

Advantages

The main reasons for introducing a cap would be to remove both the perception and possibility that influence can be bought through donations to political parties. It would stop political parties relying on a small number of high net-worth individuals and have the additional effect of making smaller donations more important to parties. People may be encouraged to donate to political parties if they feel their donation is more likely to be valued. Parties will also have a need to seek donations from a wider range of people and this process will encourage them to engage more actively with voters.

Disadvantages

It would be possible to avoid a cap by making donations through a number of sources that are difficult to trace back to one individual. However, if it were illegal for a party to accept donations knowing that they originated from one individual it is difficult to see how the donor could gain significant influence. Measures could be taken to limit avoidance, such as applying the cap to in-kind donations and loans, although capping in-kind donations is harder as the value cannot be precisely determined.

A cap may give rise to an increase in campaigning by third parties, that is, organisations distinct from political parties who campaign on political issues. Individuals may decide to donate to these organisations if they are restricted in what they can donate to parties. This has been found in some jurisdictions with a cap, such as the USA. However, there are a number of differences between the UK and USA that mean similar effects are not very likely to be found. This is discussed in more detail in Annex I.

It is not immediately obvious where to set a cap. A cap at any given level is open to the charge that it is arbitrary and that it disadvantages one party more than others.

Annex G looks at the impact different levels of cap will have based on current patterns of donations. A cap is likely to change the behaviour of donors and the way parties raise funds and so Annex G also gives examples of how changes in behaviour might affect income for political parties. It is difficult to predict exactly what wider changes would take place should a cap on donations be introduced. But a cap on donations may simply result in parties having insufficient income to function to the extent that a representative democracy requires.

What do you think of the proposal that donations should be capped?

Scenario 4: Greater levels of public funding through a general subsidy, a targeted subsidy, or publicly funded incentives to donate in addition to:

**a cap on donations;
increased transparency; and
greater expenditure control.**

The Review has found in its engagement work with the public that the issue of public funding seems to have generated the most debate and revealed polarised views. This scenario concentrates on setting out the arguments for and against increasing public funding.

There are already a number of ways political parties are given support from public funds. These are described in Annex E.

A general subsidy is a cash grant from public funds allocated in accordance with party popularity. There are various ways it could be implemented, which each have their own advantages and disadvantages. There are other ways of providing support to political parties from public funds, such as providing cash grants for specific functions or giving support in kind, or providing some incentive-based funding scheme. The latter two approaches do not necessarily have to be linked to a scenario which includes a cap on donations.

4A A general subsidy allocated according to voters' preferences

Advantages

A case for a general subsidy can be made on three grounds.

Firstly, it may be required financially to compensate parties for the loss of income through a cap on donations if without it political parties would be unable to fulfil the functions a representative democracy requires of them.

Secondly, some argue as a point of principle that, as parties carry out many activities that are for the public good, it is appropriate for the state to support these public benefit activities.⁸ It could help redress the balance which for some political parties has shifted towards centralised campaigning activities and away from engaging with local communities, education, training future leaders and policy development.

Thirdly, it could help reduce the pressure on parties to raise money and run the risk of compromising themselves in doing so. Any suggestion that political parties reward donors in inappropriate ways or that any donors have undue influence as a result of their donations should be reduced.

Public funding could bring both long-term and short-term financial benefits. A general subsidy could provide political parties with support in the short term and prevent them from facing a sudden, unpredictable drop in income as a result of a cap on donations. Such a drop in income could result in further centralisation and concentration on specific election campaigning activities focused in marginal constituencies at the expense of other activities.

An argument could be made for a general subsidy being phased out over time to oblige political parties to adapt their behaviour and increase the amount of donations they receive. However, some would argue that parties in modern democracies cannot be reasonably expected to raise all the money it is necessary for them to spend.⁹

An additional benefit of a cash grant is that it could be distributed in a way that encourages further democratic engagement. For example, allocating a grant to parties on the basis of share of the vote at elections could encourage supporters to turn out to vote in safe seats even if they felt the fate of their favoured party was certain.

While the criteria used to allocate existing public funding varies, it is based on giving different proportions to parties according to how popular they are. However, other jurisdictions have also taken fair political competition into account when developing eligibility criteria to ensure a level playing field and market entry for new parties. This often results in quite complex formulae that balance these two principles.¹⁰

There is a balance to be struck with any public funding between helping small and new parties but ensuring parties are not set up solely to obtain public funding. Criteria that required a certain level of popular support before becoming eligible for public funding, whether in terms of seats, votes or members, may help achieve this balance.

Disadvantages

Political parties have had an important function as a link with the electorate which could be lost if they become too reliant on public funds. It is argued that if a general subsidy provided a significant share of parties' income, the nature of political parties in the United Kingdom could fundamentally change.

Increased public funding may make political parties less accountable to their members and more accountable to the state, as political parties would have less incentive to represent the views of their members and may be less reliant on them.¹¹

There would need to be a careful balance struck between providing financial stability to parties, allowing parties to budget, and reflecting up-to-date public support. If public funding was distributed on the basis of share of the vote taking into account devolved administration, European Parliament and general elections the amount parties receive could change so frequently that parties would find it difficult to plan ahead.

A sudden stop in public funding, for example following a heavy electoral defeat, could force a party to cut activities which are for the public benefit. More time to prepare for a cut in public funding could allow the party to restructure its finances more appropriately.

Some people feel that public funding should not be given to parties that hold certain values, such as views considered discriminatory, inflammatory or extreme. Some are concerned it may prevent the UK from meeting certain international obligations, such as preventing racial discrimination. The New Local Government Network and the New Politics Network have proposed an additional criterion which would require parties to meet certain democratic standards in order to be eligible for public funding. It would be very difficult to determine what would be acceptable and what would not be acceptable and who should decide. Some parties may stop expressing their views overtly in order to obtain public funding. Some believe that popularity is the best test of what views are acceptable. This is a very tricky issue, but one which any additional public funding would need to address.

Given all the criteria that could be taken into account when determining how to allocate public funding, it could become difficult for people to understand how public funds are distributed and reduce the effectiveness of public accountability. The public's connection with parties could be significantly reduced and the amount of bureaucracy would increase.

4B A targeted subsidy

Additional public funds could be directed towards supporting particular activities, along the lines of the existing policy development grant, to support political parties in carrying out public benefit activities. This could be in the form of direct cash grants and/or indirect funding.

Advantages

This approach would not be designed simply to fill an emerging financial shortfall, but to encourage parties to be more active in areas which are clearly in the public interest. This could cover research, training and educational activities and some forms of community and civic engagement. It builds on existing arrangements which we know have worked in practice and have been in accepted in principle.

Disadvantages

The purposes for which such a grant could be spent might create difficulties in definition and policing; and also arguments about the nature of the threshold that needed to be passed to receive it. Unlike a general subsidy parties would have to account precisely for what the grant had been spent on, adding to their accountability workloads.

4C Introduce a voter-led incentive scheme

Parties might be helped to increase the number of people they get to donate smaller amounts by offering them a financial incentive. The main aim would be to provide an incentive for people to participate in the democratic process and for parties to encourage them to do so.

Different ways such schemes could be designed are evaluated in Annex J.

Advantages

Were these incentives to have the intended effect, they would have many advantages both in terms of how political parties are funded but also in terms of increasing people's participation in party politics. They could help widen the funding base and help compensate parties for the loss of income through a cap on donations. The wider benefits are that more people may become involved in parties through donating money and it may encourage parties to seek out small donations, particularly in areas where there is little incentive for party activity because the seat is safe for one political party.

It has the advantage over a general subsidy in that each member of the public decides which party, if any, they wish to support, and it is used only to support the political party they agree with.

Disadvantages

An incentive scheme may have a minimal effect on participation. The reasons behind the low levels of participation in parties and voter turnout are many and complex and getting more people to donate to parties may not result in those people getting involved in party politics.

Incentive schemes are likely to increase the administration costs for parties and not bring significant financial gains. The scheme could contribute to the continuing centralisation of political parties if the refunds went to the party headquarters rather than the local party.

All the options for incentivisation schemes have the potential for abuse and some could encourage channelling of donations to optimise public funds, although appropriate regulation and enforcement will reduce this and the extent of avoidance may not in practice be that great.

Each of the possible incentive schemes present practical issues for implementation (see Annex J). Most would remove the current anonymity for donors who give less than £200, although their identity would be unlikely to be known beyond the party and the body administering the scheme. While the risk of the information being disclosed may be small, it may discourage people from giving money to parties where they are particularly concerned about the impact disclosure would have for them.

Do you support the principle that additional public funds should go to political parties?

If so, do you support the idea of a general cash subsidy or a more targeted grant or the idea of financial incentives to encourage small donations?

Questions for Discussion

Below is a list of the questions that appear at the end of each of the scenarios in the previous section.

Scenario 1

- Do you think the current system (with a few minor changes) needs further time to bed in before thinking of more radical change?

Scenario 2

- Do you favour the specific ideas described in scenario 2 for increasing transparency?
- What do you think of the idea of decreasing the amount parties can spend nationally on campaigning?
- Do you think the amount that can be spent on local campaigning should be increased?

Scenario 3

- What do you think of the proposal that donations should be capped?

Scenario 4

- Do you support the principle that additional public funds should go to political parties?
- If so, do you support the idea of a general cash subsidy or a more targeted grant or the idea of financial incentives to encourage small donations?

General

- Which elements of the above scenarios do you think are most important?
- Are there any issues which you think are important that we have not covered?

To help us take your views into account during discussion with the political parties, please let us know what you think as soon as possible. The Prime Minister has asked that we report by the end of the year. In order to meet this deadline, we would appreciate all comments by 20 November 2006.

To send us your views, please reply via our website: www.partyfundingreview.gov.uk
or alternatively:

Email: review@partyfundingreview.gsi.gov.uk

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