

Political Funding Reform in India

A Report by Lok Satta

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In India, one cannot talk about public service without raising the issues of corruption, lack of transparency and accountability. Without raising esoteric issues on ethics, we need to focus attention on practical measures to combat corruption and increase transparency and accountability in all facets of public services.

Mark Twain once said, “Everyone talks about the weather, but no one does anything about it”. Corruption has become one such topic of conversation, with few in the establishment or outside really doing something to curb it. The fight against corruption is too important to be left to a few formal institutions or politicians. The people at large have enormous stakes in clean public life and corruption-free services. Experience all over the world showed that determined initiatives with public support can and will succeed in curbing corruption and cleansing the system effectively.

As many scholars like Robert Wade have pointed out, most corruption at the citizens’ level is extortionary, and people have often no choice when faced with the dilemma of having to lose much more in the form of lost money, time and opportunity, not to speak of anxiety, harassment and humiliation if they did not comply with demands for bribes. The only silver lining is, everyone, including those in positions of influence is a victim, and no one seems to be exempt from these extortionary demands. We seem to have achieved the ideal of socialism through equal treatment of all citizens in terms of extortionary corruption! With the advent of economic liberalization and delicensing of most industry, the nature of corruption is now undergoing a major transformation. The one-time grand corruption on large private projects – notably in power and other infrastructure sectors – has now become quite common. An even more alarming trend is the shift of corruption from licensing and permits to more dangerous and pernicious areas of sovereign functions of state like policing. The increasing nexus between hardened criminals, rogue policemen and corrupt politicians is one such example. It is clear that the state’s gradual withdrawal from economic activity does not automatically eliminate corruption. Even in liberalised environment, corruption has emerged as an indirect tax with horrendous consequences. An honest entrepreneur is harassed, and sometimes expelled from business. But more important, by favoring the tax-evaders, competition is severely distorted. Let’s consider a manufacturer who evades excise duty by bribing and colluding with tax officials. He then has to conceal his production. That means he has to steal power, as energy consumption cannot be disproportionate to production needs. Theft of power further reduces his cost of production, and leads to massive corruption and crisis in the state power board. Since sale of produce also has to be concealed, sales tax is evaded, leading to further fiscal deficits in the state. Finally, as sales revenues are unrecorded, he has no profits, and therefore can avoid corporate tax, and personal income tax. Now, imagine the genuine taxpayer who declares his full production and ends up paying excise duty, power tariff, sales tax, and extortionary bribes to buy peace. How can he compete with the rival manufacturer who, in collusion with the tax-man, evaded all taxes, and reduced cost of production? And after all this, if he somehow survives and

makes a modest profit, he has to pay corporate tax! In this perverse environment, even honest entrepreneurs are forced to resort to dishonest practices for survival, or they close their businesses. The number of small businesses which had to fold up because of their incapacity to deal with corrupt officials is legion.

Clearly, corruption seriously distorts competition and market forces, resulting in loss to the honest entrepreneur, consumer, and state exchequer. Hence, apart from liberal economic policies, many more practical and institutional initiatives are needed to successfully curb corruption. An important mechanism through which corruption can be tackled effectively is through political funding mechanisms. But, what is this relationship between political funding and corruption? An answer to this question can be better understood if we understand the crisis that is afflicting our political process.

Interlocking Vicious Cycles

In a well-functioning democracy, the political process ought to find answers to governance problems. Successful elections do not happen without preparation and planning. However, efficient functioning of administrative machinery alone does not constitute a successful election. A successful election is one which channelises and institutionalizes people's wishes and aspirations. Every election holds a promise for peaceful change. People in India have been voting for change time and again. But the political process is locked in a vicious cycle, and has become a part of the problem. There are several factors complicating the political process, perpetuating status quo.

First, election expenditures are large, unaccounted and mostly illegitimate. For instance, expenditure limit for assembly elections in most major states was Rs 600,000 until recently, when it has been revised to Rs 10 lakh. In reality average expenditure in most states is several multiples of it, sometimes exceeding Rs 10 million. Most of this expenditure is incurred to buy votes, bribe officials and hire musclemen. Sadly, the Southern states which are hailed for better governance, have the dubious distinction of being the worst offenders in this regard. The expenditure incurred in Andhra Pradesh in the recent Assembly and Lok Sabha poll is estimated to be more than Rs 800 – 1000 crores. On an average, the leading candidates for Assembly spend Rs. 1 to 1.5 crores each, and those for Lok Sabha about Rs. 3 – 4 crores each. The expenditure in the Kanakapura by-election for Lok Sabha held in 2003 was estimated by knowledgeable people at about Rs. 20 crores! The eventual winner was reported to have been heavily outspent by his nearest rival. Curiously, the stakes in that by-election were limited: only a maximum of a few months of Lok Sabha membership was at stake, and both the leading contenders would have been in opposition! Saidapet by-election in Tamil Nadu Assembly (2003) too was said to have broken records, with expenses exceeding Rs. 10 crores!

There are three features of such skyrocketing election expenses. First, large expenditure does not guarantee victory; but inability to incur huge expenses almost certainly guarantees defeat! There are a few candidates who win without large expenditure, but such constituencies are limited. Also in great waves, expenditure is irrelevant. The Lok Sabha victory of Congress in 1971, Janata in 1977, NTR's Victory in AP in 1983 – these

are among the many examples when money power had no role. But in the absence of ideology, and increasing cynicism, large expenditure has become necessary to win. Desperate to win at any cost, parties are compelled to nominate mostly those candidates who can spend big money. Such large, unaccounted expenditure can be sustained only if the system is abused to enable multiple returns on investment. The economic decision-making power of the state is on the wane as part of the reform process. But as the demand for illegitimate political funds is not reduced, corruption is shifting to the core areas of state functioning, like crime investigation. Robert Wade¹ studied this phenomenon of corruption, and described the dangerously stable equilibrium, which operates in Indian governance. This vicious chain of corruption has created a class of political and bureaucratic ‘entrepreneurs’ who treat public office as big business.

Second, as the vicious cycle of money power, polling irregularities, and corruption has taken hold of the system, electoral verdicts ceased to make a difference to people. Repeated disappointments made people come to the conclusion that no matter who wins the election, they always end up losing. As incentive for discerning behaviour in voting has disappeared, people started maximizing their short-term returns. As a result, money and liquor are accepted habitually by many voters. This pattern of behaviour only converted politics and elections into big business. As illegitimate electoral expenditure skyrocketed, the vicious cycle of corruption is further strengthened. All this demonstrates that political parties are not the only ones responsible for this state of affairs. We have not developed institutional mechanisms that would provide parties with incentives for good behaviour.

Parties and Political Funding

Political parties play essential roles in a representative democracy. They promote vital competition on policy and ideological alternatives, and are important conduits and interpreters of information about government. They provide channels for citizen participation in government decision-making process. Politics is a noble endeavour. It bridges the gap between unlimited wants and limited resources; it attempts to resolve the conflicting interests of various groups and bring harmony in society; and it provides a platform for people to participate and influence the decision-making process. Therefore in order to carry out their democratic functions effectively, political parties must be supported by financial and other resources. Such resources include funds to operate the basic infrastructure of political party institutions, as well as to communicate with the people.

In most democracies, political parties receive funding from both private and public sources. However, the balance between the two differ significantly. Political parties in Israel receive the bulk of their support (approx. 85 %) from the public treasury. In contrast, political parties in the United States receive most of their funds from private sources. The exception is the presidential campaign in the US that is financed partly through public funds. Arguments can be made for or against public or private funding,

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but it is undeniable that the nature of funding shapes the political process in a society as well as the regulatory framework. The debate over public and private funding is defined by constitutional principles. In the United States, for example, the right to raise private contributions by political parties is grounded in constitutional protection of free speech. However, the courts have agreed with arguments in favour of limiting private contributions in order to protect the ability of all individuals, wealthy and poor, to participate in political parties on an equitable basis. Some constitutions recognize the importance of political parties and have made provision for their support.

Political Funding Reform

Even in India, efforts have been made to address the lacunae of political funding. A law to this effect, having far-reaching consequences, has been enacted. The Election and Other Related Laws (Amendment Bill, 2003) (Funding Reform Bill) was a crucial change proposed in the Indian electoral process. Lok Satta, CSDS and Lok Niti had been advocating funding reform and direct state funding in elections. Except for public funding, most of the key provisions proposed by civil society groups found place in the Bill introduced first in Lok Sabha on 19th March, 2002, and the revised Bill was introduced in Parliament on 13th May 2003, after incorporating changes recommended by the Parliamentary Standing Committee on Home Affairs. The Election and Other Related Laws (Amendment) Bill, 2003 (Bill No. 18 of 2003) was approved by both Houses of Parliament in August 2003, and became law in September with the assent of the President. The law accomplished the following objectives:

First, it removed the loophole inserted in 1974 with respect to election expenditure ceiling in the form of explanation 1 under Section 77 of the Representation of the People Act, 1951. In a brazen display of dishonesty and political chicanery, the law was amended in 1974, and all expenditure incurred or authorized by a political party or by any other individual or body of persons or association was exempted from election expenditure ceiling. This amendment made a mockery of the election expenditure limits, and most parties and candidates violated the spirit of the law with impunity. This legal infirmity now stands removed by Section 4 of the new law, whereby only the travel expenditure incurred by leaders of political parties is exempt from election expenditure limits. For recognized political parties, the number of leaders whose travel costs are exempt is limited to forty, and for other parties, to twenty. By any standard, this is a reasonable exemption. Now, all other election-related expenditure incurred by a party, or person will be counted for ceiling purposes and shall not exceed the limits imposed by law – currently Rs 10,00,000 for Assembly constituencies and Rs 25,00,000 for Lok Sabha in major states.

Second, full tax exemption to individuals and corporates on all contributions to political parties is a strong incentive for open contributions to political parties. Parties need money for organization and mobilizing public opinion, and to compete in the marketplace of ideas. Candidates need money to get themselves known and to reach out to the voters and communicate effectively. Our failure to evolve rational incentives for political funding has severely distorted the electoral process. Parties and candidates have habitually abused

their political clout to extort money, and the license-permit raj of the past gave ample opportunities for unaccounted resource mobilization. This ambivalence led to several flip-flops in the past. Companies Act was amended in 1960, allowing corporate contributions to political parties. But in 1969, at the height of license-permit raj, such contributions were prohibited.

Then in 1985, the Rajiv Gandhi government amended the law again, permitting companies to contribute up to 5% of their average three years' net profits for political purposes. However, in the absence of tax incentives, most companies preferred to fund parties clandestinely for a variety of reasons – on account of the ubiquitous black economy, for fear of retribution from rival parties, and as a bribe or extortion money for favours received or anticipated, or avoiding harassment. For the first time, the law now provides for full tax exemption to individuals and corporates for all contributions to registered political parties. Sections 80 GGB, and 80 GGC have been inserted to this effect. Considering this, the tax incentive provided by the recent law is a vital step in encouraging open and accountable funding of parties in the long run.

Third, as a corollary to the previous provision, all contributions of Rs 20,000 and above must be disclosed by the party to the Election Commission, and such information will be in the public domain. This would ensure accountability and curb the inflow of black money in politics.

Fourth, indirect public funding to candidates of recognized political parties – including free supply of electoral rolls (already in vogue), and such items by the Election Commission as are decided in consultation with the Union government.

Fifth, equitable sharing of time by the recognized political parties on the cable television network and other electronic media (public and private). This is by far the most far-reaching reform from a long-term perspective. The recognized parties will now get free broadcasting time in all electronic media. If the Election Commission applies this provision creatively, not only will parties get free time, but we can have exciting debates between candidates and parties. This has the potential to transform the nature of political campaigning, and will reduce campaign costs dramatically. In one stroke, parties in India have been given a powerful platform to reach voters free of cost.

What More Needs to be Done – Public Funding

In spite of the enactment of The Election and Other Related Laws (Amendment Bill, 2003) (Funding Reform Bill), some issues still remain. There are no penalties for donors for non-disclosure of funding. Auditing by a chartered accountant from a panel approved by CAG has been deleted (from the earlier draft). Direct public funding to candidates or parties, if implemented, would promote performance-based candidates and parties. The vibrant functioning of political parties is also contingent on the internal democracy of the political parties and the effectiveness of anti-defection provisions. Further, rules

pertaining to equitable sharing of time by the recognized political parties on the cable television network and other electronic media (public and private) have not been framed.

The relevant section of the law (Section 39A of The RP Act) is as follows:

'39A. Allocation of equitable sharing of time.- (1) Notwithstanding anything contained in any other law for the time being in force, the Election Commission shall, on the basis of the past performance of a political party, during elections, allocate equitable sharing of time on the cable television network and other electronic media in such manner as may be prescribed to display or propagate any election matter or to address public in connection with an election.

(2) The allocation of equitable sharing of time under sub-section (1), in respect of an election, shall be made after the publication of list of contesting candidates under section 38 for the election and shall be valid till forty-eight hours before the hour fixed for poll for such election.

(3) The allocation of equitable sharing of time under sub-section (1) shall be binding on all political parties concerned.

(4) The Election Commission may, for the purposes of this section, make code of conduct for cable operators and electronic media and the cable operators and every person managing or responsible for the management of the electronic media shall abide by such code of conduct.

Explanation.- For the purposes of this section,-

(i) "electronic media" includes radio and any other broadcasting media notified by the Central Government in the Official Gazette;

(ii) "cable television network", and "cable operator" have the meanings respectively assigned to them under the Cable Television Networks (Regulation) Act, 1995 (7 of 1995).'

As can be seen, the law mandates the Election Commission to draw up suitable guidelines for implementing the above mandate. But the Commission is waiting for the Law Ministry to frame appropriate rules under the new legislation.

This legislation provides a golden opportunity to change the very nature of political campaigns in this country. For example, Lok Satta has successfully conducted over 300 debates between candidates, both at the Assembly and parliamentary constituency level as well as at the state level during the 1999 and 2004 elections in Andhra Pradesh. The debates were largely modeled after the American Presidential debates and were very popular with the public. These debates were broadcast live by the local cable channels, and provided an opportunity for the public at large to question their representatives on a variety of public policy issues.

Such an exciting debate format will not only prove to be extremely popular, but it will also change the nature of politics and electoral contests over time. Costs of electioneering will be brought down dramatically, informed choices will be encouraged, and competent candidates with leadership qualities and parties with sound ideas will have better chance of being elected. If such a decision is taken in principle, a code of conduct can be evolved, and a suitable debate format can be designed. An appropriate set of guidelines can be framed to suit the requirements of elections at the national, state and constituency levels.

The Law Ministry/Election Commission should put in place a mechanism for the conduct of such debates on all electronic media. This will ensure that the time allocated to parties can be utilized in a manner that will be attractive and appealing to the public, which will make it easier for the channels to broadcast them during primetime. Here are a few suggestions:

1. Assuming that there are 5 major parties with a plurality of vote shared between them – let us say parties A, B, C, D and E secured 35%, 30%, 20%, 10% and 5% votes in the previous election. Let us say that the party with the least vote share i.e. party E is eligible for 30 minutes time. Then one way to go about is organize a 150 minute debate between all the five parties (5 x 30) on the lines of American Presidential debates.
2. The other parties A, B, C and D will still be eligible for additional time over and above the 150 minute debate. One way of utilizing that time would be to ask the parties to air commercials or infomercials propagating the party's policies or accomplishments in an attractive format which would be appealing to the public.
3. The other alternative that could be considered is to have another round of debates between the remaining parties in multiple rounds – i.e. the 2nd round will feature debates between parties A, B,C and D and the third round could feature only parties A and B.

The above suggestions may be considered while framing rules for allocation of media time to recognized political parties. It is in the nation's best interest to further informed political debate as widely as possible and the electronic media with their wide reach are ideally placed to play a leading role in this effort. Once such rules and procedures are in place, most of the legitimate campaign finance needs would have been met through free broadcasting time in private and public electronic media. Then, the expenditure ceiling limits currently in operation – viz: Rs 10 lakhs for Assembly constituency or Rs 25 lakhs for Lok Sabha in major states would be more than adequate to meet the legitimate electioneering costs. Honest and decent elements can then be attracted by political parties for seeking elective public office.

The second important issue, which needs to be addressed, is enforcing compliance of disclosure norms in respect of political funding. Transparency of all such fund transfers is at the heart of any meaningful funding reform. Such transparency should be enforced at both the donor and recipient levels. Disclosure obligations should be backed by severe,

even draconian penalties for non-compliance. Only when there is a real risk, however small, of being jailed for non-disclosure will a donor insist on transparency. No donor is likely to deliberately invite a prison term after having contributed liberally (and secretly) to the political coffers.

The current law only provides for disclosure by political parties. But a non-transparent political culture has evolved over decades in India, encouraging unaccounted contributions to parties. Even if parties are ready to accept contributions only by cheque, past habits will not die soon. Corporates may be willing to forego tax exemption, and make secret, unaccounted contributions. This may be further accentuated by the pervasive black-money culture.

Penalties for non-disclosure by a party are difficult to enforce. Moreover, recipients of secret contributions have an incentive to conceal such sources. But a donor who parts with money has no real incentive to incur the wrath of law if there are stringent penalties for non-disclosure. Therefore, the burden of disclosure should fall equally on the donors. For instance, the following proposal could be considered

- Both the donor and recipient shall be obliged to make full disclosure to the Election Commission and the Income Tax authorities. Penalty for non-disclosure or false disclosure shall be:
 - *For Donors*: fine equal to ten times the contributions and imprisonment for six months.
 - *For Candidates*: disqualification for six years, fine equivalent to ten times the amount not disclosed, and imprisonment for at least one year.
 - *For Parties*: de-recognition and de-registration for five years, fine equivalent to ten times the amount not disclosed, and imprisonment of office bearers for three years.

The third, and critical issue relates to public funding. The law enacted in September 2003 is silent on public funding. Public funding should be considered only after other funding reforms are in place, and after parties are democratised and regulated. Any public funding to be successful should be limited, fair, transparent, verifiable and non-discretionary.

The following model could be considered for public funding. This model is based on a careful study of comparative international experience. The objectives of public funding are: provide parties with the necessary resources to effectively participate in normal political activity; and to provide support by way of reimbursement of costs of electioneering. However, we have a system of raising resources from private sources, and election expenditure ceilings mandated by law.

Pre-Conditions for Public Funding

- Political Party regulation to ensure internal democracy
- Party candidates to be democratically selected by secret ballot by members or their elected delegates
- Decriminalization of politics

- Rectification of defects in electoral rolls
- Elimination of voting fraud through introduction of voter identity cards and electronic voting.
- Strict disclosure and penalty norms

Essential Elements of Public Funding

- Transparent
- Verifiable
- Non-Discretionary
- Incentive for performance
- Encourage private resource mobilization
- Prevent fragmentation
- Fair to new parties and independents
- Finite cost to exchequer
- Equal treatment of all candidates

Gist of Proposals for Public Funding

- Rs. 10 per vote polled.
- Independent and party candidates to be treated on par as long as they cross the threshold of 10 % of valid votes polled in the constituency to become eligible for public funding.
- Party gets 1/3 of the eligible funding, and candidate receives 2/3 of the funding.
- Parties to receive 50 % of advance @ Rs.5 per vote based on their performance in earlier elections.
- Independents to be reimbursed after the poll.
- Stringent enforcement and strict penalties for non-compliance of disclosure norms.
- From the eligibility norm, the funds raised by the party shall be deducted.
- In order to encourage raising of private resources, public funding shall not exceed 1.5 times that raised by the party.
- The total fund availability (public funding + party expenditure + private sources) shall not exceed the expenditure ceiling limited prescribed by law.

Such a public funding pattern is simple, equitable, economical and verifiable.

Cost of Public Funding

Let us now calculate the cost of public funding in India.

- Population	102 crore
- Estimated no. of eligible voters	65 crore
- Actual votes polled (at 60%)	39 crore

Exclude 40% from funding on account of eligibility criteria and limits imposed: 10% voting threshold, ceiling limits, matching funds, funds raised by parties and candidates.

- Balance required for funding: for about 24 crore votes

- Funding cost at Rs.10 per vote is Rs.240 crores for the Lok Sabha elections, to be borne by the Union government.
- Funding cost for State Assemblies may be Rs. 300 crore on account of likely higher percentage of voting. This will be borne by the States.

A Public Fund for Political and Campaign Funding

- The Union and States shall start such Public Funds.
- All contributions from individuals and corporate bodies will receive the benefit of 150 % tax exemption without subject to any ceiling.
- The Public Fund shall be operated by the Election Commission, and candidates and parties will be funded from that Fund as per the norms.

Miscellaneous

- Any expenditure to give inducements to voters, distribute gifts, bribe public officials involved in conduct of election, or hire any workers or gangs for any illegal activity shall be unlawful. Penalties for such unlawful expenditure shall be disqualification of the candidate for six years, a fine equivalent to ten times the expenditure incurred and imprisonment for three years.

The Election Commission shall determine the compliance of this provision and make public these declarations. The EC shall be the final authority to decide on complaints of false declaration.

Conclusion:

Accountable and legitimate political party expenditure and campaign finance is at the heart of the fight against corruption. Incorporating public funding provisions in the current political funding law would be an important step forward. However, this law is not enough to resolve our political crisis. Most expenditure in elections is illegitimate, and many politicians have become ‘entrepreneurs’, converting politics into big business. The first-past-the-post system, coupled with parliamentary executive in states dependent on legislators’ support for survival on day-to-day basis, led to a deep crisis. Systemic reform alone will bring back sanity to politics. But the political funding reform now in place is a vital breakthrough, and an important first step in our quest for honest politics and good governance.
