The Potential Impact of the COVID-19 Pandemic on Political Finance Systems

Insights from Recent Public Funding Reforms

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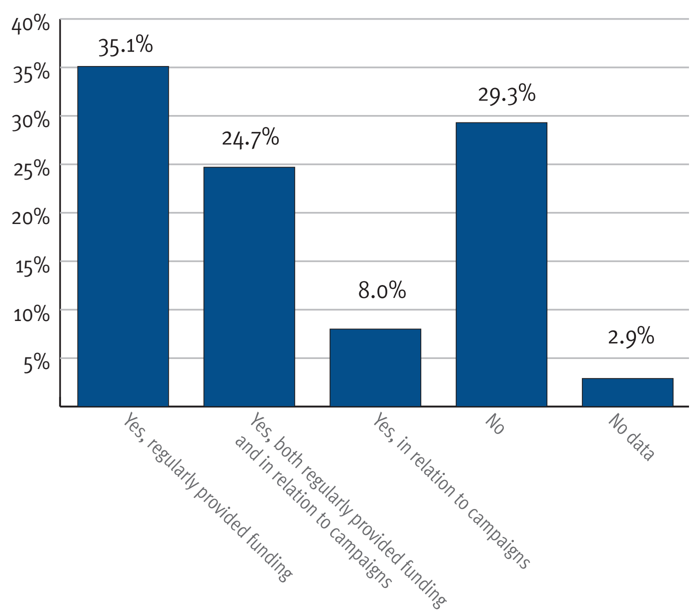
1. Overview

This Technical Paper analyses case studies of past public funding reforms and provides practical insights for states considering reform during and in the aftermath of the COVID-19 pandemic. The overall impact of the COVID-19 pandemic is likely to be much greater than any recent political or economic challenge. Nonetheless, the lessons learned from previous reforms of public funding for political parties demonstrate that states will need to be prepared for various scenarios. The crisis could also be an opportunity to address the inefficient use of state resources and to reform systems of political finance. At the same time, however, such reforms could have a number of unintended consequences. States will need to carefully consider how best to strike a balance between public and private funding for political parties in order to ensure the effective and transparent flow of money in politics.

While public funding has been a critical part of political finance systems in many states, the COVID-19 pandemic is likely to force some states to review their budgets and reduce their spending on certain programmes in order to address more pressing matters, such as unemployment and the provision of healthcare and education. There is no doubt that the current pandemic will have a unique and unprecedented impact on the flow of money in politics. Under such conditions, it is not difficult to envisage how the amount of public subsidies to political parties and candidates might be reduced or entire public funding mechanisms readjusted in order to save public money and channel it to the fight the pandemic and its aftermath. At the same time, it is important to note that the pandemic may also affect the capacity of private donors and reduce the level of their contributions to political parties and candidates. Restrictions on the size of gatherings will also make it more difficult to organize fundraising events. The pandemic could make political parties more dependent on public funding to sustain their political activities. For better or worse, any change in public funding will have a number of consequences across the entire political finance system and beyond.

The provision of public funding to political parties is a key feature of political finance systems in many states. Public funding seeks to level the playing field for all political parties by ensuring that they have sufficient financial sources to reach the electorate and sustain their day-to-day party operations, thereby encouraging political pluralism (International IDEA 2014; OECD 2016). Public funding also aims to balance the influence of private funding and to mitigate the risks of policy capture by narrow private interests. According to International IDEA's Political Finance Database, 68 per cent of the states surveyed provide public funding to political parties

Figure 1. Direct public funding to political parties



Source: International IDEA Political Finance Database, <https://www.idea.int/data-tools/question-view/548>

Box 1. Examples of the economic impact of COVID-19 on political finance, as of May 2020

Public funding

Brazil: A federal judge was asked to suspend the Special Fund for Campaign Financing for political parties and ruled that the funds should be made available to the federal government to be used for measures to deal with the pandemic (Globo.com 2020).

Hungary: The government of Prime Minister Viktor Orbán has secured emergency powers by decree in order to respond to the COVID-19 pandemic. Without any need to seek parliamentary approval, the government reduced the level of public funding provided to political parties. It is estimated that political parties will lose half their state funding in 2020 (Eder 2020; Szabo 2020). In May, in a move not directly related to the pandemic, the State Audit Office suspended the disbursement of state funds to a key opposition party because of irregularities in the party's finances. This decision was criticized by opposition parties as unlawful and politically motivated (Associated Press 2020).

Mexico: In order to generate more financial resources to fight the pandemic, the National Electoral Institute (INE) has set out a new procedure that enables political parties to decline public funding. Pursuant to Article 41 of the Constitution, political organizations can renounce their entitlement to all or part of the public financing that they have not yet received. Based on this provision, the INE declared that political parties that wish to do so could decline all or part of their public funding from May 2020. The funds declined by the political parties will be at the disposal of the Federal Treasury, which has the authority to allocate these resources as it deems appropriate.

Private donations

Canada: It is reported that political party fundraising has been affected by the cancellation of physical events and by increased unemployment. While Canada's political parties rely heavily on donations from individuals to cover their daily operational costs, they have been criticized for continuing to solicit donations from supporters during a public health emergency that is crippling the economy (Chamandy and Mangat 2020).

United States: Fundraising efforts for the 2020 presidential campaign have been affected by the suspension of traditional fundraising events. State-mandated bans on large gatherings mean that many in-person fundraisers have been put on hold, making it difficult to raise sufficient funds to run campaigns. In some cases, candidates have shifted to virtual fundraising efforts (Steakin 2020).

either during election campaigns or on a regular basis (see Figure 1). In addition to direct public funding, such support can take different forms such as tax breaks and free or subsidised access to the media.

The combination of increased expenditure and decreasing revenues amid the COVID-19 crisis will reshape economies in profound ways. States will need to review the role of public funding to support political parties while other potential non-state donors might be reluctant to contribute in the light of their own deteriorating economic situation. There is evidence that this is already happening (see Box 1).

2. Consequences of public funding reforms following major economic and political crises

Three case studies highlight how states have undertaken public funding reforms in the past decade in order to deal with political and economic challenges, in particular the aftermath of the 2008 global financial crisis. In the years following the 2008 recession, many states adopted measures or implemented reforms of their political finance systems that sought to reduce expenditure and increase transparency in order to combat the abuse of state resources. The case studies in this section highlight the consequences when public funding systems are reformed in response to economic and political crises. The lessons learned from these examples provide insights on the possible impact of the COVID-19 pandemic on political finance systems around the world.

2.1. Greece: the financial crisis leads to reforms that address abuses of public funding

In 2010, as the financial crisis intensified, it was revealed that Greece was spending EUR 65 million on funding political parties in a country with a population of 11 million (GRECO 2010). Political party funding had come under scrutiny following allegations of its misuse by senior politicians and political figures. Greek political parties credited the majority of their revenue to public subsidies and bank loans. In a political system dominated by two main parties at that time, most of the funding went to these large parties. Public subsidies to political parties were often used to guarantee bank loans. Under such conditions, the larger parties routinely pledged future state funding as collateral for loans. When they lost power, these parties were left with debts and significantly smaller incomes. At the time, the former ruling party, the New Democracy Conservatives, declared a debt of EUR 250 million that it was unable to repay.

The Greek Government implemented reforms in 2014 intended to combat corruption, reinforce transparency and audit the finances of political parties and elected officials. The new framework introduced limits on donations from single sources, enhanced reporting mechanisms on party finances and tightened regulations concerning bank loans to political parties by prohibiting parties from using public funds beyond the current financial year to guarantee debt.

The economic crisis revealed flaws in Greece's system for funding political parties and provided an opportunity to increase accountability and address the inappropriate interdependence between political parties and banks. Nonetheless, a number of challenges remain. For instance, in order to address the abuse of public funding and other state resources by political parties, Greece will need to embed its political finance system in a wider anti-corruption strategy that also deals with the management of conflicts of interest, whistle-blower protection, asset disclosure by elected officials and other integrity-related policies (OECD 2018).

2.2. Italy: direct public funding abolished but new challenges with private donations emerge

The allocation of public subsidies to political parties can cause controversy among the public if state resources are scarce and needed for other public services such as schools and hospitals. Public funding for political parties is often already unpopular, given citizens' unwillingness to fund parties or candidates whose views they do not share. In Europe, for example, only 19 per cent of the public trust political parties, while 77 per cent do not (European Commission 2019). In Latin America, only 13 per cent of the public trust political parties (Latinobarómetro 2018). At times of financial difficulty, using limited public funds to support political parties and candidates becomes even less popular.

In Italy, the reduced trust in politics and political parties following the financial crisis and increasing concern over the abuse of state resources by politicians coalesced to bring about the elimination of direct public funding to political parties. The global financial crisis affected a system already under pressure following many years of political instability and economic decline in a country already in crisis. The 2008 recession in conjunction with scandals associated with the illicit funding of political parties and political corruption led to popular discontent and resentment against the political class. In response to the public outcry, the Italian Government abolished state funding of political parties in 2013. A gradual reduction of public financing began in 2014, reducing support by 40 per cent in the first year, 50 per cent the following year and 60 per cent the year after until direct public funding was fully phased out by the end of 2017. State funds were replaced by an indirect system of tax deductions on voluntary contributions to political parties. Individuals can donate up to EUR 100,000 annually to each political party, while legal entities can donate up to EUR 100,000 per annum in total. Taxpayers have also the option of earmarking 0.2 per cent of their annual income tax as a contribution to one of the eligible political parties. Indirect public funding is also available in the form of subsidized media access allocated on the basis of seat share and in the form of tax relief.

Through its redesign of the party finance system, Italy aimed to combat the mismanagement of state funding, increase private donations and encourage direct and indirect contributions in support of political parties from citizens and legal persons. However, the abolition of public funding for political parties introduced a new dependence on private funding and multiplied the number of actors involved, resulting in an increased risk of illicit influence that was further aggravated by a lack of transparency. The new legislation also failed to include a ban on foreign donations, be they from companies, individuals or public bodies, and lacked a clear regulatory framework for donation disclosure.

Italy's 2018 general election exposed such vulnerabilities. It was the first to take place after the abolition of direct public funding and the first in which the foreign financing of Italian political parties was not only possible, but legal. Consequently, the Growth Decree, which became law in June 2019, among other things regulated foreign donations to political parties, which were only permitted to foundations and associations, and not transferable to political parties or movements (Transparency International n.d.). However, the regulations surrounding foreign donations are still quite vague and the ceiling for private donations is set high at EUR 100,000 per annum. Furthermore, the identity of the donor is not always disclosed. One lesson from Italy is that public funding reform requires careful consideration of how to regulate private sector donations from both individuals and corporations. Regardless of the crisis, political parties still need to operate. In the absence of public funding, they may be inclined to look for illicit sources.

2.3. Brazil: public funding increased to level the playing field but may have reinforced the status quo

Economic recessions have greater implications for low-income and middle-income states with precarious job markets and fragile social protection systems, thereby deepening prevailing economic inequalities. The growing concentration of economic resources in the hands of fewer people represents a significant threat and increases the risk of corruption and policy capture. Under such conditions, some states have decided to provide more public funding to political parties in order to level the playing field for political actors and reduce the dependency of political parties on private funding.

The global financial crisis pushed Brazil into recession in 2009, and it also experienced a severe economic crisis in 2014–2016. Record levels of unemployment alongside a series of corruption scandals and the impeachment of a former president have led to widespread public dissatisfaction with, and loss of trust in, the political system. In an effort to tackle corruption and increase transparency, Brazil implemented electoral reforms in 2015 which banned corporate donations. Before 2015, private corporations were the largest funders of political parties, electoral campaigns and candidates. During the 2014 elections, more than 90 per cent of resources for presidential candidates were derived from corporate donations.

In order to fill the gap left by the ban on corporate contributions, parliament introduced a Special Fund for Campaign Financing, which was funded by the federal budget and distributed among political parties to finance electoral campaigns. In 2018, the fund amounted to around USD 400 million. Although the original intention was to level the playing field, the allocation of funds among political parties openly favoured incumbents: 35 per cent was allocated according to the number of votes received in the most recent election; 48 per cent according to the number of representatives a party had in the lower house; 15 per cent according to the number of representatives a party had in the upper house; and only the remaining 2 per cent was distributed equally among all parties (Rocha 2018). Party leaders decide how to allocate the resources among members, and there are only ineffective controls over spending, which allows political parties to use taxpayers' money to cover expenditure on lawyers, accounting services and even property purchases.

In addition, despite the ban, corporate money still plays a key role in Brazilian elections since corporate donations can be channelled through individual donations, where challenges remain as the current legislation does not establish a specific donation limit (Parlamentria 2018). Instead, a percentage is calculated according to the income of the donor and individuals are entitled to donate 10 per cent of their last declared annual income. Candidates are also allowed to self-fund their campaigns, which creates an advantage for wealthy nominees and engenders a system of unequal representation.

3. Key issues

An overview of these case studies suggests that public funding reforms in the wake of a crisis can be a double-edged sword. To ensure a level playing field among all parties and candidates, it is imperative that public and private funding are balanced with adequate regulations. Although providing public funding to political parties and candidates may not be a popular measure in times of pandemic and economic recession, reducing the level of public subsidies can result in increased influence for private funding—including from illicit and foreign sources—on politics, as can be seen in the case of Italy. When private donations play a significant role in political party financing, the system becomes more vulnerable to policy capture. This makes it crucial to establish adequate regulation. Similarly, in the absence of proper regulation, public funding can serve to preserve a status quo that keeps traditional parties in power. The already unequal playing field between an incumbent and contenders can be exacerbated by the abuse of state resources. As in the case of Brazil, public funds are often allocated among political parties according to the results of previous elections, making it more difficult for new political forces to benefit from the system. This uneven allocation of resources is then further aggravated by the lack of expenditure regulations, which allows established political parties to use state funds to cover the high cost of electoral campaigns. The case of Greece highlights that reform of political finance regulations alone may not prove effective at regulating the abuse of public funding, but should be embedded into wider anti-corruption efforts. During and after the pandemic, it is also likely that political parties will raise and spend more funds through digital portals and online applications. This is an emerging area that existing political finance regulations often fail to address effectively. As part of public funding reforms, it will be important to put measures in place to ensure transparency and accountability in political parties' online income and spending.

Key issues to consider when reforming public funding for political parties:

- If states are to reduce the level of public funding for political parties during pandemics, careful consideration should be given to regulating private donations from individuals and corporations. Regardless of the crisis, political parties still need to operate. In the absence of public funding, they may be inclined to look for illicit sources.

- As a minimum, the regulation of private donations—such as setting reasonable donation limits, banning certain types of donor and putting transparency measures in place—should be considered when reducing the level of public funding.
- If states decide to increase public funding for political parties to support their operations during the pandemic, realistic and fair eligibility/distribution criteria should be introduced. Such an increase could result in a public outcry as channelling funds for political parties might not be seen as the most pressing need while public health systems are being overstretched or even overwhelmed. A proper communication strategy should therefore be devised to inform the public of the merits of such a scheme.
- In order to avoid overspending of public funding, spending caps should be put in place.
- The pandemic and bans on large gatherings are likely to increase online fundraising and spending online by political parties. It will be important to consider measures to ensure transparency in and the accountability of political parties' financial activities online.
- Crises such as the COVID-19 pandemic can present opportunities to address persistent political finance challenges, such as the abuse of public funding. In order to maximize the effectiveness of such measures, states should consider mainstreaming political finance in a wider anti-corruption strategy together with the management of conflicts of interest, whistle-blower protection and asset disclosure by elected officials.

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