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Evaluation Report on Iceland
Transparency of Party Funding
(Theme II)

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I. INTRODUCTION

1. Iceland joined GRECO in 1999. GRECO adopted the First Round Evaluation Report (Greco Eval I Rep (2001) 10E) in respect of Iceland at its 6th Plenary Meeting (10-14 September 2001) and the Second Round Evaluation Report (Greco Eval II Rep (2003) 7E) at its 19th Plenary Meeting (28 June-12 July 2004). The aforementioned Evaluation Reports, as well as their corresponding Compliance Reports, are available on GRECO's homepage (http://www.coe.int/greco).

2. GRECO's current Third Evaluation Round (launched on 1 January 2007) deals with the following themes:

   - **Theme I – Incriminations:** Articles 1a and 1b, 2-12, 15-17, 19 paragraph 1 of the Criminal Law Convention on Corruption[1] ETS 173), Articles 1-6 of its Additional Protocol[2] (ETS 191) and Guiding Principle 2 (criminalisation of corruption).

   - **Theme II – Transparency of party funding:** Articles 8, 11, 12, 13b, 14 and 16 of Recommendation Rec(2003)4 on Common Rules against Corruption in the Funding of Political Parties and Electoral Campaigns, and - more generally - Guiding Principle 15 (financing of political parties and election campaigns).

3. The GRECO Evaluation Team for Theme II (hereafter referred to as the "GET"), which carried out an on-site visit to Iceland from 6 to 9 November 2007, was composed of Ms Jane LEY, Deputy Director, Office of Government Ethics (USA), Mr Lars-Åke STRÖM, Head of Division, Government Office's Commissions in Gothenburg (Sweden); and the scientific expert, Mr Yves Marie DOUBLET, Deputy Director, National Assembly, Legal Department, Unit of Legal Studies (France). The GET was supported by Ms Laura SANZ-LEVIA from GRECO's Secretariat. Prior to the visit the GET was provided with a comprehensive reply to the Evaluation questionnaire (document Greco Eval III (2007) 7E, Theme II), as well as copies of relevant legislation.

4. The GET met with officials from the following governmental organisations: Prime Minister's Office (including the Secretary to the Committee which drafted the Law on Financing of Political Parties), Ministry of Justice, Ministry of Finance, National Audit Office, Central State Tax Office. In addition, the GET met with members of political parties represented in Parliament (Independence Party, Social Democrat Alliance, Left-Green Movement, Progressive Party and Liberal Party) and some of their auditors. Moreover, the GET met with (and received written information from) media representatives and academics. Finally, the GET met with the NGO National Movement.

5. The present report on Theme II of GRECO's Third Evaluation Round – "Transparency of party funding" – was prepared on the basis of the replies to the questionnaire and the information provided during the on-site visit. The main objective of the report is to evaluate the measures adopted by the authorities of Iceland in order to comply with the requirements deriving from the provisions indicated in paragraph 2. The report contains a description of the situation, followed by a critical analysis. The conclusions include a list of recommendations adopted by GRECO and addressed to Iceland in order to improve its level of compliance with the provisions under consideration.

6. The report on Theme I – "Incriminations" –, is set out in Greco Eval III Rep (2007) 7E, Theme I.

[1] The Criminal Law Convention on Corruption (ETS 173) entered into force in respect of Iceland on 1 June 2004.
[2] The Additional Protocol to the Criminal Law Convention (ETS 191) was signed by Iceland on 15 May 2003; it has not yet been ratified.

II. TRANSPARENCY OF PARTY FUNDING - GENERAL PART

Definitions

7. A political party is defined as an association which takes part in parliamentary or municipal elections (Article 2(1) of Law No. 162/2006 on the Financial Affairs of Political Organisations and Candidates and Their Duty to Provide Information).

Registration of political parties

8. There are no particular requirements for registering a political party other than those applicable to the registration of non-profit legal persons. In this connection, the Icelandic Registry of Enterprises, under the Ministry of Finance, is responsible for registering political parties. In order to register a political party, the identity (names and identity numbers) of its Board Members as well as the statutes of the association (including *inter alia* data on the name of the party, its objectives, the identity of its founders, internal rules) must be submitted. Information contained in the Registry of Enterprises is publicly accessible.

9. At present, there are 349 registered political parties (including local branches) in Iceland; some of them are no longer active.

Party representation in Parliament

10. Following the May 2007 parliamentary elections, the parties represented in Parliament are:
    - Independence Party (Sjálfstæðisflokkurinn): 25 seats
    - Social Democrat Alliance (Samfylkingin): 18 seats
    - Left-Green Movement (Vinstri hreyfingin - grænt framboð): 9 seats
    - Progressive Party (Framsóknarflokkurinn): 7 seats
    - Liberal Party (Frjálslyndi flokkurinn): 4 seats

11. In addition, the Icelandic Movement (Íslandshreyfingin) and the Association of Elder Citizens and Invalids (Baráttusamtök eldri borgara og öryrkja) participated in the last general election, but did not obtain any representation in Parliament.

12. The Icelandic party system makes the formation of a single-party majority in Parliament very unlikely; thus, the country is generally ruled by coalition governments. The current Government is formed by a coalition of the Independence Party (Sjálfstæðisflokkurinn) and the Social Democrat Alliance (Samfylkingin).

Participation in elections

Parliamentary elections

13. Iceland has a unicameral Parliament, the Althingi, which is composed of 63 members elected by the people by secret ballot on the basis of proportional representation (d'Hondt system) for a term of four years.

14. All persons who, on the date of an election, are 18 years of age or older, have Icelandic nationality and have a permanent residence in Iceland, have the right to vote in elections to Parliament (Article 33, Constitution). The right to candidacy is granted to every national having the right to

vote in elections to Parliament and an unblemished reputation. Supreme Court judges, however, are not eligible (Article 34, Constitution).

15. The country is divided into six constituencies – three of the biggest of which are located in the capital Reykjavík and its surroundings; each constituency has nine seats in Parliament, awarded on the basis of the outcome of voting in that constituency. The additional nine seats (referred to as "equalisation seats") are distributed to constituencies and allocated to political parties so that the parliamentary representation of each will reflect as closely as possible the total votes it received. Only parties receiving at least 5% of valid votes cast can be allocated equalisation seats.

16. A party intending to participate in parliamentary elections needs to present to the Election Commission, no later than 15 days before the elections, a list of names which are twice the number of available seats in that constituency, a signed declaration from all the candidates indicating that they accept to be on the list, together with a declaration of support from a certain number of voters in that constituency (between 30 and 40 times the number of seats).

Presidential elections

17. Any person who is at least thirty-five years of age and fulfils the requirements necessary to vote in elections to Parliament, with the exception of the residency requirement, is eligible to be elected President (Article 4, Constitution).

18. The President is to be elected by direct, secret ballot of those who are eligible to vote in elections to Parliament. A presidential candidate is to be proposed by not less than 1,500 voters and not more than 3,000. The candidate, if there is more than one, who receives the most votes, is duly elected President. If there is only one candidate, s/he is duly elected without a vote (Article 5, Constitution).

Overview of the party funding system

19. Rules governing political finance were recently introduced via Law No. 162/2006 on the Financial Affairs of Political Organisations and Candidates and Their Duty to Provide Information of 21 December 2006, which applies to political parties and alliances participating in elections to the Parliament and municipal governments, as well as individual candidates, who run either for internal party elections (primaries) or posts at municipal level. The main objectives of Law No. 162/2006 are to reduce the risk of conflicting interests and to provide transparency in financial affairs with the ultimate goal of increasing public trust in political activities and strengthening democracy (Article 1, Law No. 162/2006).

20. Law No. 162/2006 entered into force on 1 January 2007 with a deferred effective date for the provisions on primary elections of 1 June 2007. In addition, the National Audit Office issued, in March 2007, a set of Rules on the Financial Accounts of Political Parties, which comprise some minimum standards for reporting the finances of political parties and electoral candidates.

Public funding

21. Public funding is granted to support operational activities of political parties. According to the political parties interviewed at the time of the GET's visit, public funding constituted some 60% to 90% of their revenue. Party subsidies may thus not be used for any commercial or private purpose.

22. Direct public funding is provided through (Chapter II, Law No. 162/2006):

(i) annual contributions from the State Treasury (according to authorisation given by the Parliament to the Ministry of Finance in the State budget). This type of support consists of two different allocations: (a) financial grants divided between parties according to votes gained in the last general elections. Parties which obtained at least one seat in Parliament or received more than 2.5 % of votes in the last general elections can apply for such grants; and (b) parliamentary support for every party represented in parliament. An equal amount, called a "unit", is to be paid for each Member of Parliament. One unit is also paid for each parliamentary group. In addition, an amount equalling twelve units is allocated to parliamentary groups of the political organisations that have no seats in the Government, dividing these units among them in proportion to the number of votes. The following chart illustrates the contributions from the State Treasury corresponding to the period 2003-2008:

*Million EUR	Proposal 2008	Budget 2007	Budget 2006	Budget 2005	Budget 2004	Budget 2003
Political parties	3.2	3.2	2.1	2.1	2.1	2.1
Parliamentary fractions	1.2	1.2	1	1	1	0.9
TOTAL	4.4	4.4	3.1	3.1	3.1	3

(ii) annual contributions from municipalities: local authorities with more than 500 inhabitants are to support parties which have obtained at least one seat in the local council or at least 5% of the votes cast in the last municipal election. The overall amount of the funding to be provided is to be decided by the local authority itself at the time of adoption of the municipal budget and distributed on a proportional basis. Smaller communities are free to decide whether to provide financial support to parties, but if they do so, they are bound by the same aforementioned rules. In 2007, 32,750,000 ISK[3] (271,635 EUR) was distributed proportionately to the parties with seats in Reykjavik's City Council. In 2008, the contribution to political parties from the city of Reykjavík will amount to 33,600,000 ISK (278,685 EUR).

23. Some form of indirect funding of election campaigns is provided through free broadcasting time on the State-owned television channel at the time of election campaigns. There are no specific provisions on media space, but, according to the Law No. 53/2000 on Broadcasting, all radio and television stations are bound by the basic rules of democracy and freedom of expression. On this basis, parties are treated equally when allocating air time.

24. Moreover, the GET heard during the on-site visit that indirect funds were being provided in the form of use of Government resources (e.g. staff, material, premises, etc.).

Private funding

25. Donations are defined as any direct financial contribution or any other item which has a financial value, regardless of its origin or nature (cash or in kind), including exclusive discounts, favours and concessions (e.g. discounts on the market price of advertisements, rent or other payment for the use of real estate), free use of staff (excluding volunteer work), free use of facilities and equipment (apart from the use of personal property of volunteers which is not used for commercial purposes), waivers of residual debts (whether in part or in full), unusual loan terms or assistance in financing

[3] Exchange rate from ISK to EUR as of 1 April 2008.

(Article 2(4), Law No. 162/2006). Donations in kind are to be assessed at cash value at their market price; detailed rules on the calculation of what is to be considered "market price" are laid down in Article 9 of the Rules on the Financial Accounts of Political Parties etc.

26. Membership fees constitute another source of income for political parties, although they have rarely been collected on a regular basis. The membership fee that a political party may require from its members must not exceed 100,000 ISK/year (830 EUR).

27. Political parties are permitted to perceive income from advertisements in party publications and renting activities (Article 11, Rules on the Financial Accounts of Political Parties etc). Any other sale of services and goods for fund-raising purposes is prohibited, with the sole exception of informal sales of refreshments, badges and lottery tickets, bazaars, admission to meetings organised by the parties etc., as long as these do not exceed 100,000 ISK (830 EUR) per year per single purchaser (Article 12, Rules on the Financial Accounts of Political Parties etc).

28. A number of restrictions apply to the sources of private funding. In particular, pursuant to Article 6 of Law No. 162/2006, political parties and electoral candidates are not permitted to accept donations from:
    - anonymous donors;
    - undertakings which are majority owned by or under the control of the State or municipalities;
    - public entities other than the State Treasury or municipalities, such as undertakings which are jointly owned by the State and municipalities;
    - foreign nationals who do not have the right to vote in Iceland, undertakings or other entities which are registered in other countries.

29. Moreover in respect of the amount/size/periodicity of private contributions, political parties and electoral candidates are not allowed to receive more than 300,000 ISK (2,488 EUR) per year from any individual donor (whether a physical or legal person). Membership subscriptions below 100,000 ISK/year (830EUR) and general/public discounts (which are available to anyone on the basis of tariffs or general business practices) are not accounted for in the above-mentioned threshold (Article 7, Law No. 162/2006).

30. Donations in excess of the 300,000 ISK (2,488 EUR) threshold are to be returned as promptly as possible. If returning of such donations proves to be impossible, they are to be kept separately in the accounts of political parties and electoral candidates and deposited on a separate time-deposit account (Article 2, Rules on the Financial Accounts of Political Parties etc).

Taxation regime

31. Legal persons donating to a political party qualify for a tax-exemption of up to 0.5% of their income (Article 31(2), Law No. 90/2003 on Income Tax).

Expenditures

32. No restrictions on the total amount of expenditure which a political party may incur are imposed. However, for the last parliamentary elections held on 12 May 2007, political parties reached a consensus on a budgetary limit of 28,000,000 ISK (232,240 EUR) for expenses linked to advertising during the electoral campaign.

33. The costs for individual candidates running for internal party selection processes (primaries) must not exceed 1,000,000 ISK (8,295 EUR) in addition to a supplement which is calculated in inverse proportion to the number of inhabitants entitled to vote in the relevant electoral district (the calculation of the supplement increases as the number of voters in the relevant constituency decreases).[4]

III. TRANSPARENCY OF PARTY FUNDING - SPECIFIC PART

(i) Transparency (Articles 11, 12 and 13b of Recommendation Rec(2003)4)

Books and accounts

34. Generally, the accounts and financial reports of both political parties and electoral candidates are subject to the provisions of the Annual Accounts Act No. 3/2006, as applicable (Articles 13 and 18, Rules on the Financial Accounts of Political Parties, etc). In this context, they have an obligation for all legal persons in Iceland to keep accounting books and records. All accounting books, accounting records and documents, as well as letters, facsimile sheets and telegrams or their duplicates, including documents kept by computer, microfilm or by any other comparable method, are to be kept in a secure and safe manner for at least seven years from the closure of each relevant accounting year (Article 20(1), Law No. 145/1994 on Book-Keeping). An annual account is to be kept for at least 25 years (Article 20(4), Law No. 145/1994 on Book-Keeping). The falsification of accounts or accounting documents, the creation of documents without real substance etc, as well as the destruction of such documents are considered a major violation of law, which, according to the Penal Code may be subject to fines or to imprisonment up to six years.

Political parties

35. The Boards of political parties and managing directors are responsible for the preparation of an annual financial report, including an income statement, balance sheet, statement of cash flows, notes and the report of the board (Article 15, Rules on the Financial Accounts of Political Parties etc).

36. In addition, political parties are required to maintain a consolidated account for all units falling within their scope, such as associations, district councils, holding companies and related foundations, whether they are registered or not. Consolidated accounts are to provide a clear and comprehensive view of the results, assets and changes in cash in both the parent and the subsidiary association (Article 16, Rules on the Financial Accounts of Political Parties etc).

37. Party units with an income below 300,000 ISK (2,488 EUR) per year are excluded from the consolidated accounts.

Electoral candidates

38. Electoral candidates are to keep the finances of their campaign separate from their private finances. A separate bank account for campaign purposes is to be opened, through which all cash

[4] Article 7, Law No. 162/2006: In an electoral district with more than 50,000 inhabitants of 18 years and older, 75 ISK (0,62 EUR) per inhabitant; in an electoral district with 40,000 to 49,999 inhabitants of 18 years and older, 100 ISK (0.83 EUR) per inhabitant; in an electoral district with 20,000 to 39,999 inhabitants of 18 years and older, 125 ISK (1 EUR) per inhabitant; in an electoral district with 10,000 to 19,999 inhabitants of 18 years and older, 150 ISK (1.24 EUR) per inhabitant; in an electoral district with less than 10,000 inhabitants of 18 years and older, 175 ISK (1.45 EUR) per inhabitant.

deposits and withdrawals in connection with the campaign must pass. All entries in the accounts are to be recorded in accordance with general accounting principles and backed by supporting evidence, such as the originals of invoices, receipts for donations received, etc.

Reporting obligations

39. The Rules on the Financial Accounts of Political Parties etc. provide some minimum standards for reporting political finance: political parties and electoral candidates are therefore permitted to report in greater detail (Article 1, Rules on the Financial Accounts of Political Parties etc). Moreover, at the time of the GET's visit, the National Audit Office was preparing standardised forms for consolidated financial reports of political parties and candidates, which were in the process of being consulted with/commented by political parties.

Political parties

40. Pursuant to Article 9 of Law No. 162/2006, political parties have to submit a consolidated financial report (where annual accounts of political parties and those of the units falling within their scope have been merged into a single account) to the National Audit Office on an annual basis.

41. The Rules on the Financial Accounts of Political Parties etc. detail the level of itemisation to be contained in the party's consolidated financial report, including a (i) consolidated income statement; (ii) consolidated balance sheet (comprising a statement of cash and flows); and (iii) notes.

42. In particular, the consolidated income statement is to comprise, as a minimum (Article 15, Rules on the Financial Accounts of Political Parties etc):

(a) Information on income:
- Contributions from the State Treasury
- Contributions from municipalities
- Financial donations from legal persons
- Donations from legal persons in the form of exclusive discounts
- Other in kind donations from legal persons (i.e. favours and concessions, free use of staff, free use of facilities and equipment, waivers of residual debts, unusual loan terms or assistance in financing)
- Financial donations from physical persons
- Donations from physical persons in the form of exclusive discounts
- Other in kind donations from physical persons (i.e. favours and concessions, free use of staff, free use of facilities and equipment, waivers of residual debts, unusual loan terms or assistance in financing)
- General membership fees
- Income from rent or real estate
- Income from rent or movable assets
- Service revenues, including admission fees to meetings, entertainments and other similar social events
- Sales of goods, including income from sales of refreshments, lotteries, raffles, etc.
- Other operating income

(b) Information on expenditure incurred by:
- Head Office
- Parliamentarians

- Regional subsidiaries
- Party Congress
- Primary elections
- Parliamentary elections
- Municipal elections
- Other expenditure.

43. The consolidated balance sheet is to contain detailed data on assets and liabilities.

44. Finally, the notes attached to the consolidated financial report are to provide overall totals of the donations received from individuals (whether in cash, discounts or any other form). With respect to the donations received from legal persons, their names are to be disclosed in the notes to the annual financial report or in a separate attachment, together with the amount and type (in cash, discounts or any other form) of the donation. Furthermore, the notes are to include details on the consolidation of accounts, namely by providing information (name of entity, share, nature of operation) concerning the entities/units falling within the scope of the political party.

45. In the event that two or more political parties organise a joint electoral campaign in a specific electoral district, a separate financial report is to be prepared for the joint campaign (Article 17, Rules on the Financial Accounts of Political Parties etc).

Electoral candidates

46. Electoral candidates are to submit to the National Audit Office a financial report on their electoral campaign within six months from the time of the election (Article 11, Law No. 162/2006). Law No. 162/2006 entered into force with respect to candidates on 1 June 2007, which in practical terms means that candidates do not have to report on the income/expenses incurred in connection with the general election which took place in May 2007. Since the next elections are the municipal ones, which are scheduled in 2009, the reporting requirement with respect to candidates will not be due until 2010.

47. Electoral candidates are required to specify their own contributions (whether in cash or in kind) in their accounts. They must keep a separate register of individual cash donations, specifying the name and identity of the donor in question. In kind donations (e.g. free use of staff, sponsoring of advertisements, discounts, etc) are to be recorded at their market price. If a campaign is financed through a loan, details must be provided on the identity of the lender, the amount of the borrowing and the lending terms. Cancellation of debts and obviously favourable loan terms are to be assessed as a donation from the lender to the campaign (Articles 20 and 21, Rules on the Financial Accounts of Political Parties etc).

48. According to a standardised draft form being prepared by the National Audit Office, a candidate's financial report is to include the following elements:
(i) Endorsement of the financial statements (sworn statement of the candidate referring to the veracity of the income and expenditure declared)
(ii) Auditor's report
(iii) Income statement specifying the campaign period, including:
(a) Information on income: donations on legal persons (including name of legal person, nature and amount of donation); donations from individuals, local governments, candidates own contribution, contributions from the political party (including nature and amount of donation); and other income.

(b) Information on expenditure: campaign office, advertising and promotional expenses, meeting and travelling expenses, other operational expenditure, other expenditure.

(iv) Balance sheet (assets and liabilities)

(v) Notes on donations received from legal persons (including name of legal person, nature and amount of donation) and from individuals, local governments, candidates own contribution, contributions from the political party (overall totals including nature and amount of donation). Moreover, when there is substantial surplus or deficit of the campaign, the notes should also contain details on what will be done with the surplus or who will be paying for the deficit of the campaign. In addition, the notes are to provide explanations concerning liabilities (identity of the lender, the amount of the borrowing and the lending terms).

49. Electoral candidates are exempt from the obligation on financial reporting if the cost of the electoral campaign does not exceed 300,000 ISK (2,488 EUR).

Donors

50. Legal persons are required to identify any donation made to a political party/electoral candidate in their annual reports to the tax authorities (Article 7, Law No. 162/2006).

Access to accounting records

51. The chartered auditors verifying the books and accounts of both political parties and candidates have the right to request all documents and information indispensable to perform the audit. The National Audit Office is vested with wide investigative powers to, at any time, call for all necessary documents to verify that the funding received by political parties complies with the requirements of Law No. 162/2006 (Article 8, Law No 162/2006). It is not, however, empowered to request supporting further evidence (e.g. receipts, invoices) concerning candidates' accounts. Finally, the tax authorities have access to the accounting records of political parties and candidates (Article 94, Law No. 90/2003 on Income Tax).

52. Political parties, candidates for election, and the National Audit Office do not fall under the Information Act No. 50/1996. Therefore, detailed financial information – other than what is to be contained in the abridged reports to be published by the National Audit Office, is not accessible to the public.

Publication requirements

53. The National Audit Office is responsible for publishing a summary of the financial reports of parties and candidates showing information on the total income received and expenses incurred. The figures provided in respect of the party's income must detail the source of the contribution (whether public – State/local, or private – physical/legal persons) and the identity of the legal person donating the relevant funds. Any discount from market price has to be indicated specifically (Article 9 in relation to political parties, Article 11 in relation to candidates, Law No. 162/2006). The GET heard at the time of the on-site visit that the National Audit Office was in the process of developing the contents of the summary form; it planned to publish the summary forms in its website (http://www.rikisend.althingi.is).

54. The GET was informed during the on-site visit that some political parties have in the past publicised their financial statements, or/and the financial declarations of their Members of Parliament, in their respective website.

(ii) Supervision (Article 14 of Recommendation Rec(2003)4)

Auditing

55. Political parties are required to have their books endorsed by a certified auditor. Audit reports are to indicate whether the relevant consolidated financial statements have been prepared in accordance with the obligations of Law No. 162/2006 and the Rules on the Financial Accounts of Political Parties developed by the National Audit Office, as well as general accounting principles (Article 8, Law No. 162/2006).

56. Likewise, the financial statements prepared by individual candidates, which contain the final account of their electoral campaigns, are subject to audit by certified auditors (Article 10, Law No. 162/2006).

Monitoring

57. The National Audit Office is responsible for monitoring political financing; it is vested with wide powers to ensure not only a formal, but also a material control of the information provided by political parties (Article 8, Law No. 162/2006). It is not, however, empowered to carry out material checks of candidates' accounts.

58. The National Audit Office is an independent body, operating under the auspices of Parliament. The Presidential Committee of Parliament appoints the Auditor General for a period of six years. The National Audit Office selects its own working agenda (although it may also act at the request of the Presidential Committee of Parliament, ministries or individual central governmental bodies); its procedures have to respect the principles of objectivity and professionalism as well as strict adherence to international auditing standards. Furthermore, pursuant to Article 3 of the National Audit Act of 1997, the staff employed in the National Audit Office is to be independent of those ministries and organisations where the audit is being carried out.

59. In principle, in the event of an irregularity/deficiency in a financial report, the National Audit Office would contact the party or its auditor to clarify/remedy the situation. If nevertheless the irregularity detected suggests a potential instance of corruption, the National Audit Office will immediately report to the police, as appropriate.

(iii) Sanctions (Article 16 of Recommendation Rec(2003)4)

Sanctions

60. Infringements – whether intentional or due to gross negligence - of the provisions contained in Law No. 162/2006 are sanctioned with fines or imprisonment of up to six years (Article 12, Law No. 162/2006). It is possible to appeal the court's decision before the Supreme Court.

61. Due to the recent adoption of Law No. 162/2006, there is no experience developed in the application of its sanctioning regime.

Immunities

62. The Constitution of Iceland grants immunity to members of Parliament for statements made in Parliament (Article 49). With regard to criminal action the same article states that no member of Parliament may be remanded in custody during a session of the Parliament without the permission

of the Parliament unless s/he is caught in the act of committing a crime. The provisions of the Constitution granting immunity from prosecution were designed to ensure that Members of Parliament could remain active and independent without interference. Their declared purpose is not to protect Members of Parliament individually.

63. The President may not be prosecuted on a criminal charge except with the consent of the Parliament (Article 13, Constitution).

Statutes of limitation

64. The general statutes of limitation contained in Article 81 of the Criminal Code are applicable in respect of procedure and sanctions for violations of laws and regulations on political financing (i.e. ten years for the imprisonment sanction of up to six years, and two years if the penalty imposed is a fine).

IV. ANALYSIS

65. Until 2007 no comprehensive legislation had been enacted in Iceland regarding political funding. The prevailing view was that, in strict observance of the constitutional right of freedom of association expressly granted to political parties by Article 74 of the Icelandic Constitution, these organisations were free to decide their internal functioning, including the sources and nature of their income and expenses. In this connection, there were no restrictions on the financial support of natural and legal persons for political parties, with the sole exception of foreign donations which were prohibited according to Act No. 62/1978. Furthermore, no disclosure requirements were placed on political parties or candidates for election. Nor were there specific provisions concerning the scrutiny of their funds. Political parties were nevertheless subject to the general accounting and auditing rules governing the operations of private legal persons. Likewise, by virtue of Article 6 of the National Audit Act of 1997, the National Audit Office was entitled to verify the accounts of all organisations receiving State funding. This type of financial audit was however never performed in respect of political parties.

66. In the last years, a few political scandals involving alleged instances of nepotism and corporatism have been reported in the media. The aforementioned cases prompted debate in the country calling for greater transparency and stricter control of political finances. Moreover, the GET learned that another critical thrust encouraging the adoption of legislation in this area was the observation made by GRECO in its First Round Evaluation Report on Iceland (2001) which specifically pointed at the desirability of regulating the financing of political parties (paragraphs 13 and 58, First Round Evaluation Report).

67. Law No. 162/2006 on the Financial Affairs of Political Organisations and Candidates and Their Duty to Provide Information entered into force on 1 January 2007 with a deferred effective date for the provisions on primary elections of 1 June 2007. Law No. 162/2006 bans donations from anonymous and foreign sources, undertakings which are majority owned by/under the control of the State or municipalities as well as other types of public entities (e.g., undertakings which are jointly owned by the State and municipalities). It sets a cap of 300,000 ISK (2,488 EUR) on the value of donations that parties and candidates are entitled to receive per donor and per year; it limits candidate spending during primary elections. Furthermore, the recently adopted legislation addresses the financial reporting and disclosure obligations of both political parties and candidates in personal elections (primaries and municipal polls). The National Audit Office is entrusted with a new role in regulating and monitoring the finances of political parties and candidates, which it immediately effected by issuing, in March 2007, implementation regulations concerning the

reporting obligations of political parties and candidates (i.e. Rules on the Financial Accounts of Political Parties etc). In the GET's view, the adoption of Law No. 162/2006 (and its implementation regulations) is clearly a significant step forward to enhance transparency and accountability in the financing of political parties and election candidates for which the authorities must be commended. The aforementioned legislation broadly reflects the requirements of the Recommendation Rec(2003)4 of the Committee of Ministers of the Council of Europe on Common Rules against Corruption in the Funding of Political Parties and Electoral Campaigns.

68. The GET's visit took place before any elections that would have been subject to Law No. 162/2006 or before any annual financial reports of the parties were due (no party reports will be due under the system established by this Law until 2008 and reports from candidates in primary elections will not be due until 2010). Thus, the GET was limited in its review as to the sufficiency of the terms of the recently adopted legislation, since implementation was still at its very early stages. The reading of these documents was complemented with information on the initial steps taken by the National Audit Office to enforce Law No. 162/2006 and observations on political finance practices by representatives of the parties and other individuals with whom the GET spoke. The following analysis is to be seen against this background; time and experience with the law will show if there are difficulties that are not now necessarily apparent. In this connection, Law No. 162/2006 specifically directs the Prime Minister to, no later than 30 June 2010, appoint a committee representative of all the political parties at the Parliament (Althingi) to review the law and its implementation.

69. At the start, it is important to note that Law No. 162/2006 applies to political parties and alliances participating in elections to the Parliament and municipal governments, as well as individual candidates, who run either for internal party elections (primaries) or posts at municipal level. Candidates for the office of President are thus not covered by the provisions of the Law. While the GET recognises that the functions carried out by the President may be primarily representative, the Constitution does invest in the President substantial legislative and executive authorities that can be exercised, if necessary. The President is in a position of high public visibility and concern for the transparency of election campaigns of candidates for this office exists even though the election itself may not be party-political. The authorities recognised that this was indeed an issue that merited further attention; an internal ongoing discussion was taking place when the GET conducted its visit as to the appropriateness of introducing transparency rules in relation to the funding of presidential candidates. The GET is of the opinion that this is a lacuna in the system which needs to be addressed and consequently recommends **to introduce regulations ensuring an appropriate level of transparency of the campaign finances of presidential candidates.**

Transparency

70. As political parties are legal persons, they have been and continued to be required by Icelandic law to keep proper books and accounts. In addition, under Law No. 162/2006 the accounts of political parties are to be consolidated to include, in a clear and comprehensive manner, the accounts of all units/entities falling within their scope (e.g. associations, district councils, holding companies and related foundations, whether they are registered or not); only party units whose income is below 300,000 ISK (2,488 EUR) are excluded from the consolidated accounts. Candidates are required to conduct their financial operations in relation to primaries and municipal campaigns through a separate bank account and to manage their finances according to general accounting principles. The GET considers that the accounting requirements placed upon political parties and candidates are important tools to strengthen the financial discipline of political actors and decrease possibilities for corruption. Moreover, the GET notes with satisfaction that Iceland has paid due attention to the challenging issue of consolidating the accounts of political parties in

line with Article 11 of Recommendation Rec(2003)4, which requires political parties to include in their accounts, as appropriate, the accounts of related entities.

71. Law No. 162/2006 and its implementing regulation require parties and candidates to keep records of the donations they receive. The GET is pleased to note that the definition of what constitutes a donation is reasonably expansive; it comprises both monetary (including cash) and in kind contributions (which are to be recorded at their commercial value). The definition of a donation though does not require any valuation of government resources such as offices, telephones, etc. used by a Member of Parliament's political assistant when conducting campaign activities. The GET was informed that there is no restriction on the use of these government resources for this purpose; quite the contrary, the reason that the minority parties get more public funding than those in the Government (see paragraph 22) was to help balance this disparity.

72. Both parties and candidates[5] are required to report on their income and expenses to the National Audit Office. In particular, political parties are to submit consolidated financial reports (including data on all units/entities falling within their scope) on an annual basis; candidates are required to file their campaign finance statements within six months from the time of the relevant election (primaries/municipal elections). At the time of the GET's visit, the National Audit Office (in close consultation with political parties) was in the process of developing standardised forms for reporting political finances, accompanied by guidance on their completion. The GET welcomes, in principle, the development of common formats to present information relating to parties/candidate's accounts in a coherent and comparable manner. The GET was provided with samples of the aforementioned draft forms, which will require comprehensive data on income (including the nature and value of each donation) and expenditure, debts and assets of parties/candidates.

73. Under Law No. 162/2006, the names of legal persons, the value and the type (whether in cash or in kind) of their donations are required to be itemised in the financial reports submitted by parties and candidates to the National Audit Office. However, the amount of all donations of natural persons given to a party or candidate is presented as one aggregate figure. The GET learned that Iceland made a conscious decision to set a cap of 300,000 ISK (2,488 EUR) on the value of donations that parties and candidates are entitled to receive per donor and per year as a trade-off to not requiring the identification of the names of natural persons who were donors for purposes of their privacy. The GET acknowledges the need to protect the right to privacy of natural persons, but considers that such an individual right has to be balanced with the wider public interests at stake (transparency concerns aimed at detecting and unveiling instances of improper private influence in political finances). The GET takes the view that the right to privacy may well prevail as long as political donations are small – and therefore, unlikely to constitute an improper source of influence; however, a donation of a natural person of up to 2,488 EUR cannot be considered modest (for example, in connection with municipal elections) and merits its itemisation from a perspective of transparency and accountability. Moreover, the GET notes that the current situation (non-disclosure of identity of natural persons donating to a party/candidate) allows, for example, a legal person to both exceed the ceiling of the permissible amount of donations it can make throughout the year, and to conceal its identity, by channelling its financial support to a party/candidate through separate individual donations of its employees. In order to enhance transparency and to prevent improper financing, the GET recommends **to consider establishing, for purposes of reporting the identity of contributors who are natural persons, a separate threshold level that is below the ceiling on the value of donations that parties/candidates are entitled to receive but is still of some significance.**

[5] Candidates whose campaign costs are below 300,000 ISK (2,488 EUR) are exempted from the obligation to report to the National Audit Office.

74. While the reporting obligations contained in Law No. 162/2006 appear to be rather complete in respect of their degree of detail, the GET has misgivings concerning their timing. Political parties are required to submit their consolidated financial reports on an annual basis; however, Law No. 162/2006 is silent on an actual deadline. The authorities indicated that the reporting deadline would most likely follow the general accounting timeframes, i.e. the accounting period would lapse from 1 January to 31 December and the latest possibility to report would be six months after the completion of the financial year (by 30 June). The GET was informed after the visit that the deadline for the first reporting exercise since the Law entered into force (i.e. the accounts of 2007) is 31 May 2008.

75. The GET notes that there is nothing in Law No. 162/2006 and no guidance in its implementing regulations as to when a person becomes a candidate for the purposes of having to begin keeping records for a financial report. The absence of a statutory deadline for the commencement and closure of campaigns, makes it impossible to ascertain the full extent of candidate's campaign expenditure, and therefore, introduces uncertainty as to whether the spending limits for primary elections (see paragraph 33) have been duly respected. The candidate is to provide a report within six months following the election, but again it is unclear whether the report is to cover the period until the date of the election or until the date the report is submitted. In addition, there is no provision or guidance in the Law No. 162/2006 or its implementing regulations as to reports of candidates after the initial report, particularly if the candidate has a surplus of funds or a debt that has to be reduced by further contributions. Furthermore, the GET was also made aware during the on-site visit that the primary elections were becoming increasingly critical to the overall process because it was then that ballot rankings were established and the probability of becoming a Member or being selected for a leadership position in the Government was fairly set. Because transparency and oversight of the electoral process are critical for the sake of its own credibility, the GET recommends **to (i) introduce clear provisions determining when an individual becomes a candidate for purposes of the start of the requirement to maintain records for a financial report; (ii) define the end of the reporting period for the first report to be filed after the primary; and (iii) require any candidate who reports a positive or negative balance in a campaign account to continue to report on a regular basis until the excess is disposed of or the debt has been retired.**

76. Moreover, the GET is of the opinion that transparency in election financing would benefit significantly from more frequent reporting, which goes beyond the annual reporting of political parties and the *ex-post* reporting of candidates required by existing legislation. For reporting to be effective, it has to be timely. In this connection, frequent reporting (e.g. through interim reports during election campaigns) enhances the openness of political funding during the crucial period of campaigns as it allows a candidate/party's opponent, the authorities or the electorate to detect questionable transactions that may take place during elections. Consequently, the GET recommends **to explore ways of sharing campaign finance information with the public prior to the election (e.g. through interim reports).**

77. Political parties are under no obligation themselves to make their accounts public, although some of them have done so in the past on a voluntary basis. Candidates are also not required to make their accounts for the election campaigns public. In addition, the GET was informed that detailed financial information on political finances would not fall under the provisions of the Information Act No. 50/1996. Nevertheless, the National Audit Office is required to prepare a summary of the financial reports of each party/candidate and to make it public. While the names of the legal persons who have contributed are to be disclosed, the other information that will actually be made public by the National Audit Office as part of the summary was still under discussion when the

GET visited Iceland. As a minimum, Law No. 162/2006 requires that the summaries must include information on the total income obtained and expenses incurred by parties/candidates; this is in line with the provisions of Article 13b of Recommendation Rec(2003)4. As to the media to be used to publicise the aforementioned summaries (once issued), the National Audit Office intended to do so through its Website. The GET considers that publicity is key in ensuring transparency of party funding; public access to reported information on political finances is therefore essential to an effective system of disclosure. Furthermore, it is crucial that the information contained in the summaries is both sufficiently detailed and comprehensible and that it is released in a timely and accessible manner. For this reason, the GET urges the National Audit Office to rapidly comply with its obligation to publicise parties/candidates' political finance accounts and recommends **to (i) define the contents of the summarised financial reports of political parties'/candidates' accounts (including required information on income received and expenses incurred) as soon as possible and (ii) publicise the summaries in a timely manner.**

Supervision

Auditing

78. The financial accounts of both parties and candidates are to be endorsed by a certified auditor. The GET found, however, that the auditors in some instances were long time members of the party to whom they provided their services and that they had served as their parties' respective auditor for a number of years. In this respect, Iceland has not adopted international standards for their auditors where such standards could well assist with the issue of independence. Furthermore, the GET was informed that auditors are not required by law to report to the competent law enforcement bodies any accounting irregularities that they may encounter in the course of an audit, rather any concerns would normally be made a part of the audit opinion provided to the client. The GET heard during the on-site visit that auditors are bound by a duty of secrecy vis-à-vis their clients. The interlocutors met admitted that the existing auditing legislation was 10 years old and that room for reform existed in this particular area. In light of the above, the GET recommends **to (i) establish clear rules ensuring the necessary independence of auditors called upon to audit the accounts of political parties and candidates; and (ii) establish procedures for auditors of such accounts, consistent with accepted international auditing standards, on when, how and to whom to report suspicions of significant/substantial infringements of existing legislation on political funding which they may come across in the course of their work.**

Monitoring

79. The National Audit Office is the key institution responsible for monitoring political finances. The GET was pleased to note that the independence and professional skills of the National Audit Office appeared to be beyond any doubt. At the time of the GET's visit, the National Audit Office had one attorney working with the Auditor General and Deputy Auditor to develop the regulations and provide guidance. The Auditor General expected to hire one or two more accountants to assist with this function, and while the 2008 appropriations were being discussed when the GET conducted its visit, the Auditor General did not think that there would be any problem with getting the additional resources necessary to carry out this function.

80. With regard to investigative resources, the National Audit Office indicated that if they saw a potential violation of donation limits or other law, they would turn that information over to the police rather than conduct an investigation themselves. The National Audit Office expects to review all of the reports and, if necessary, to seek clarification from the parties, candidates or their auditors.

While the National Audit Office is vested with wide powers to ensure not only a formal, but also a material verification of the information provided by political parties, it has, however, no authority to carry out material checks of candidates' funding. The National Audit Office recognised that this is an area which has not been regulated by Law No. 162/2006, but where there may well be a need, in the future, to investigate candidates' accounts beyond the information that they themselves provide in their financial reports. In such a case, the National Audit Office would have no legal basis to request any further evidence (e.g. invoices, receipts) to carry out an in depth material (and not merely formalistic) verification of the information disclosed in the relevant financial reports. Consequently, the GET recommends **that the National Audit Office be vested with appropriate authority to carry out, as needed, a material verification (in addition to the existing formal review) of the information provided by election candidates.**

81. The GET noticed that the National Audit Office was given a significant amount of discretionary authority in Law No. 162/2006 in terms of developing procedures, but that the initial implementation regulations it issued (i.e. Rules on the Financial Accounts of Political Parties etc) were more a restatement of the Law than additional guidance. The GET was nevertheless pleased to note that training sessions were organised by the National Audit Office at the beginning of 2007 in order to familiarise political parties with their new reporting obligations. The National Audit Office was perceived by the parties and others with whom the GET spoke as being available for questions and helpful; however, it also seemed as if much more work was going to be required in order to ensure consistency in the reports. For example, the answers from the National Audit Office provided to individual questions had not been compiled and made generally public in a Frequently Asked Questions (FAQ) format or other written format so as to help others with the same questions and to provide transparent consistency. Moreover, the Office was intending to try to respond to some issues by agreement with the parties rather than by a regulation or written guidelines. While getting consensus is important, it is equally crucial that such agreements be made public by the Audit Office in order to help instil public confidence in the system.

82. As a part of a larger system of monitoring, legal persons are required to identify any donation made to a political party/candidate in their annual reports to the tax authorities so that they can qualify for a tax exemption (up to 0.5% of their income). The GET considers that the aforementioned requirement on legal persons to report donations constitutes a useful control mechanism. The GET was made aware that decisions by tax authorities are made available for public inspection for a short period, but the current tax forms do not distinguish between the donations given by a legal person to a political party from those provided to other organisations (religious groups, charity organisations, cultural activities and scientific research institutions). The GET was informed that the tax authorities could, without amending Law No. 90/2003 on Income Tax, change the reporting fields on their forms so that political contributions would be shown separately from other contributions. . Consequently, the GET recommends **that the reporting fields of tax forms be changed to separate political donations from contributions to non-profit entities (such as charities or religious associations).**

83. Moreover, the tax authorities would still have to grant a deduction for a contribution in excess of the allowed 300,000 ISK (2,488 EUR) ceiling because the tax law has not been coordinated with the recently adopted legislation on political funding. The fact that a contribution which is in excess of the limit can still be eligible for a tax exemption is certainly troubling, but that issue falls under Article 4 of Recommendation Rec(2003)4 dealing with the tax deductibility of donations, which is not under review in GRECO's Third Evaluation Round and can therefore not give rise to a formal recommendation.

Sanctions

84. In the GET's view, a weak aspect of Law No. 162/2006 is its rather general and ambiguous provision on sanctions. Infringements (whether intentional or due to gross negligence) are punished with fines or imprisonment of up to six years. In this context, the conditions under which the available penalties (fines/imprisonment) could be enforced are written so vaguely as to raise a reasonable question as to its validity. The criminal sanction of imprisonment for six years will probably never be sought because of its severity, particularly in comparison to penalties for far more venal crimes in Iceland. Furthermore, it is not clear who would be the physical person serving the sentence if a party was found in violation. Without more, the current sanctions available under Law No. 162/2006 need to be reviewed. In the GET's opinion, the introduction of more flexible penalties (including, possibly, administrative and civil sanctions) in addition to criminal sanctions could prove to be valuable to further dissuade political parties and candidates for election from breaching the rules regarding political funding. In the light of the foregoing considerations, the GET concludes that the current sanctions do not appear to be effective to address violations of the requirements laid down in Law No. 162/2006, nor are they proportionate. If they are not imposed or cannot be imposed they certainly will not be dissuasive. The GET recommends **to review the sanctions available for the infringement of rules concerning the funding of political parties and election candidates and to ensure that these sanctions are effective, proportionate and dissuasive.**

V. CONCLUSIONS

85. In 2007, a new legislative framework on political financing entered into force in Iceland. The authorities should be commended for this important step forward to enhance transparency and accountability in an area which was not regulated in the past. The piece of legislation of the greatest importance in this respect, i.e. the Law No. 162/2006 on the Financial Affairs of Political Organisations and Candidates and Their Duty to Provide Information, broadly reflects the requirements of the Recommendation Rec(2003)4 of the Committee of Ministers of the Council of Europe on Common Rules against Corruption in the Funding of Political Parties and Electoral Campaigns. In addition, efforts are being made to proceed with the implementation of the recently introduced legislative/policy framework at a good pace. In this connection, the National Audit Office (an independent oversight body out of the Executive) is responsible for developing the necessary reporting requirements and procedural mechanisms to give effect to the legal provisions. It remains critical that further arrangements are introduced to allow an easy and timely access of the public to information on political finances. Furthermore, it is important that the National Audit Office is vested with appropriate authority to carry out proper substantial supervision of candidates' financial reports, as needed. To a large extent, the challenges are today more in the enforcement of the law. For this reason, the existing sanctioning system needs to be developed in order to provide for penalties appropriate (i.e. effective, proportionate and dissuasive) to the severity of the range of misdeeds that are possible under the law. Finally, transparency rules in relation to the campaign finances of presidential candidates, an area uncovered up to now, are still needed.

86. In view of the above, GRECO addresses the following recommendations to Iceland:

i. **to introduce regulations ensuring an appropriate level of transparency of the campaign finances of presidential candidates (paragraph 69);**

ii. **to consider establishing, for purposes of reporting the identity of contributors who are natural persons, a separate threshold level that is below the ceiling on the value**

of donations that parties/candidates are entitled to receive but is still of some significance (paragraph 73);

iii. **to (i) introduce clear provisions determining when an individual becomes a candidate for purposes of the start of the requirement to maintain records for a financial report; (ii) define the end of the reporting period for the first report to be filed after the primary; and (iii) require any candidate who reports a positive or negative balance in a campaign account to continue to report on a regular basis until the excess is disposed of or the debt has been retired (paragraph 75);**

iv. **to explore ways of sharing campaign finance information with the public prior to the election (e.g. through interim reports) (paragraph 76);**

v. **to (i) define the contents of the summarised financial reports of political parties'/candidates' accounts (including required information on income received and expenses incurred) as soon as possible and (ii) publicise the summaries in a timely manner (paragraph 77);**

vi. **to (i) establish clear rules ensuring the necessary independence of auditors called upon to audit the accounts of political parties and candidates; and (ii) establish procedures for auditors of such accounts, consistent with accepted international auditing standards, on when, how and to whom to report suspicions of significant/substantial infringements of existing legislation on political funding which they may come across in the course of their work (paragraph 78);**

vii. **that the National Audit Office be vested with appropriate authority to carry out, as needed, a material verification (in addition to the existing formal review) of the information provided by election candidates (paragraph 80);**

viii. **that the reporting fields of tax forms be changed to separate political donations from contributions to non-profit entities (such as charities or religious associations) (paragraph 82);**

ix. **to review the sanctions available for the infringement of rules concerning the funding of political parties and election candidates and to ensure that these sanctions are effective, proportionate and dissuasive (paragraph 84).**

87. In conformity with Rule 30.2 of the Rules of Procedure, GRECO invites the authorities of Iceland to present a report on the implementation of the above-mentioned recommendations by 31 October 2009.

88. Finally, GRECO invites the authorities of Iceland to authorise, as soon as possible, the publication of the report, to translate the report into the national language and to make this translation public.