Council of Europe

Group of States against Corruption

PROGRESS REPORT ON RC-III ICELAND

THE IMPLEMENTATION OF THE RECOMMENDATIONS OF GRECO ON ICELAND TRANSAPRENCY OF PARTY FUNDING (THEME II)

Government of Iceland
Prime Minister's Office
October 2010

1. Introduction.

Reference is made to GRECO's Third Evaluation Round - Compliance Report on Iceland regarding Transparency of Party Funding, adopted in March 2010. In the report the Icelandic Authorities are invited by GRECO to present a progress report on the implementation of the recommendations made be GRECO in the Third Evaluation Report on Iceland (GRECO Eval III Rep (2007) 7E Theme II) on Transparency of Party Funding.

Iceland wishes to inform that on September 9, 2010, a law was passed in Althingi (Parliament of Iceland) concerning amendments of the *Act on the Finances and Reporting Requirements of Political Organisations and Candidates, No. 162/2006.* The amendments have been published in the Offical Gazette, as *Act No. 121/2010.*

A short overview of the legislative changes is given below, but a more detailed overview of the recommendations and the work undertaken and amendments in relation to each one is given in chapter two.

Principal amendments in the new legislation

1. The statutory rules on donations from individuals and legal entities to candidates and on reporting requirements now include candidates in presidential elections. The Act places a ceiling on permissible election campaign expenses incurred by presidential candidates, connecting that ceiling with the number of voters, as has been the case with candidates in local elections. (ISK 35 million).
2. Maximum donation from individuals and legal entities to political organisations and candidates is raised from ISK 300,000.00 to ISK 400,000.00 Currency rate of Euro is approximately 150 ISK = 1 Euro. The amount in question was therefore raised from approx. 2000 euros to 2.667 euros., which corresponds to price level increases from 1 January 2007, the date the original Act (No. 162/2006) entered into force, until the present date. Special authorisation contained in the original Act, for additional collection of membership fees ranging up to ISK 100,000.00, has been abrogated. Membership fees collected must henceforth be included in the maximum donation.
3. Names of individuals contributing more than ISK 200,000.00 to political parties or candidates are to be made public. The anonymity threshold is therefore reduced from ISK 300,000.00 to ISK 200,000.00 for individual donors. The statutory rule requiring that all donations from legal entities be made public remains unchanged.
4. In order to promote non-discrimination among political organisations and to pave the way for new political organisations to be able to present candidates for election to Parliament, political organisations are authorised, irrespective of election results, to apply for subsidies of up to ISK 3 million from the Treasury in order to reimburse cost from their election campaign.
5. The reference amount for party units that may be excluded from consolidated financial reports and the reference amount for candidates exempt from the information disclosure requirement is raised from ISK 300,000.00 to ISK 400,000.00 in response to price level increases; cf. Item 2.

6. The Act stipulates which information from the accounts of political organisations and candidates shall be made public.
7. The Icelandic National Audit Office is granted the same authority to request documents from candidates, in order to ascertain that their donations and election campaign expenses are in compliance with the provisions of the Act, as it has to request documentation from political organisations.
8. Treasury allocations to political organisations are conditional upon the organisation's prior fulfillment of its statutory duty to disclose information to the Icelandic National Audit Office.
9. The bill stipulates that donations received by political organisations or candidates from unknown donors must revert to the Treasury.
10. A special rule is enshrined in the legislation, providing for the permissible amount of initial donations from individuals and legal entities; that is, donations provided from individuals and legal entities in direct relation to the establishment of a political organisation. The maximum amount for such donations is set at twice the maximum donation according to the law.
11. Amendments to the sanction provisions of the Act are made with the aim of clarifying the criminal liability of individuals and legal entities according to the Act, and of basing penalties and their framework on the severity of conceivable violations.

The work on the amendments was conducted by a committee of experts analysing all aspects, including GRECO's recommendations. The Parliamentary Bill of Law was proposed jointly by four out of five party leaders in Parliament, including both government and opposition parties. Iceland is of the opinion that these amendments adress in a satisfactory manner the recommendations that have been directed to Iceland by GRECO on the transparency of financial donations to political organisations in Iceland.

2. Implementation of recommendations - Overview of legislative changes in Icelandic legislation regarding transparency of party funding, and analysis of the recommendations by GRECO.

GRECO directed nine recommendations to the Icelandic authorities in its Third Evaluation Report of 4 April 2008 on transparency of party funding in Iceland. In particular, the recommendations include comments and suggestions for improvements and refinements of current statutory provisions on political organisations' finances, on rules and regulations deriving from those statutes, as GRECO is of the opinion that, in passing the 2006 Act, Iceland has already implemented all of the main points in the Committee of Ministers' Recommendation of 8 April 2003, Rec(2003)4, on common rules against corruption in the funding of political parties and electoral campaigns. That Recommendation lays the substantive groundwork for work carried out by the Council of Europe and GRECO in this area. Broadly speaking, the above applies to all of GRECO's recommendations, with one major exception. That exception pertains to the first GRECO recommendation, discussed below, and to the implementation of rules on transparency of financial contributions to presidential candidates. In that instance, GRECO justifiably pointed out a loophole in Icelandic legislation.

GRECO's recommendations were as follows:

1. *To introduce regulations ensuring an appropriate level of transparency of the campaign finances of presidential candidates;*
2. *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;*
3. *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;*
4. *To explore ways of sharing campaign finance information with the public prior to the election (e.g. through interim reports);*
5. *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;*
6. *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;*
7. *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;*
8. *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);*
9. *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.*

2.1 The first recommendation.

i. To introduce regulations ensuring an appropriate level of transparency of the campaign finances of presidential candidates;

The GRECO evaluation report states as follows concerning this recommendation:

"…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**."

In the bill of legislation later enacted as the current Act No. 162/2006, it was recommended that the statutory rules on contributions from legal entities and individuals also apply to presidential candidates. It was also proposed that, when presidential elections take place, budgetary allocations be made in support of candidates for election to the office of president of Iceland. That amount should then be allocated by application, following the presidential election, to those candidates who received at least one-tenth of votes cast in the election, in direct proportion to the number of votes received, subject to the requirement that the contribution may never exceed the candidate's election campaign expenses less contributions from legal entities and individuals according to Chapter III. Finally, the bill recommended that applications for State contributions to presidential candidates be accompanied by an audited financial statement for the election campaign. These provisions were omitted from the bill, however, on the recommendation of the General Standing Committee of Parliament at the time the bill was considered by Parliament, with the explanation that it was necessary to give closer consideration to how such contributions should be implemented before passing law on them.

In its current examination of the matter, the majority of the expert committee preparing the amendments, concluded that it was critical to set rules on presidential candidates' finances and disclosure requirements. It can be said that the necessity for this grew as a result of recent developments in the application of the power conferred on the president by the Constitution and the increased importance that the presidential office has therefore gained in the administration of the country. As such, the committee agreed with and underlined the statements in the GRECO recommendation, concerning the need to set rules ensuring adequate transparency of presidential candidates' campaign finances.

In accordance with this, Act No. 121/2010 states that the statutory provisions on permissible donations from legal entities and individuals to candidates apply also to donations to presidential candidates, as well as the provisions on information disclosure to the Icelandic National Audit Office and the public. The law stipulates that total election campaign expense incurred by a candidate for election to the presidency of Iceland may not surpass a certain threshold, connecting that ceiling with the number of voters, as has been the case with candidates in local elections (a certain sum for every individual in the voters registry), a total amount of approx. ISK 35 million. The law does not stipulate, however, that presidential candidates should have the possibility of receiving contributions from the State.

2.2 The second recommendation

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;

The GRECO evaluation report states as follows concerning this recommendation:

"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 (ISK 300,000.00) 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**."

The above-mentioned GRECO recommendation was discussed in depth by the expert committee. In the opinion of a majority of the committee, the recommendation under consideration focuses on the issue of when the amount of a donation is so high that it can be generally considered to create the risk of inappropriate connections between the donor and the candidate or political organisation to whom the donation is made, thereby justifying the disclosure of that connection to the public. The majority of the committee was of the opinion that even though a contribution of ISK 300,000.00 was not large in and of itself, it must be considered handsome when donated by an individual, and generally in excess of the amount that individuals are willing to contribute to a political organisation or individual candidate in order to support the causes that the organisation or candidate represents. In line with this, and with reference to the GRECO recommendations, it was proposed that the names of individuals who donate more than ISK 200,000.00 to political organisations or candidates be made public. The confidentiality threshold is thereby reduced from ISK 300,000.00 to ISK 200,000.00. In the opinion of the majority of the committee, this provision takes account of both points of view: on the one hand, adequate transparency of financial contributions, considering the risk that individuals will have inappropriate influence through their contributions; and on the other hand, the view that individuals should be free to support political organisations' activities with

contributions up to a specified moderate limit without public disclosure of the donation. Concurrent with this change, the new legislation raises the maximum contribution from an individual or legal entity from ISK 300,000.00 to ISK 400,000.00, or by an amount slightly less than the price level changes since the Act was passed in late 2006. The so-called confidentiality threshold will then be based on a contribution amounting to half of the permissible maximum according to the law. All contributions from legal entities are public according to the amended Act No. 162/2006.

2.3 The third reccommaendation.

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.

The GRECO evaluation report states as follows concerning this recommendation:

"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."**

As regards the first item in the above-specified recommendation, the majority of the committee was of the opinion that adopting statutory provisions clearly specifying a particular commencement date for campaign account entries could prove a double-edged sword. It must be borne in mind that adopting rules on specified time limits in this context could create the risk of circumvention of those rules; that is, that

systematic efforts will be made to ensure that campaign costs are incurred before the specified reporting period begins. The rules in Act No. 162/2006 require that all campaign contributions and expenses be specified in the campaign accounts. It does not matter when the expenses are incurred, and this has not caused any difficulties in implementing the Act. On the other hand, it can be argued that a lack of specified time limits for reference in this respect could result in non-transparency that merits a response. It is therefore recommended that, in instances involving primary elections, the reporting period be determined by the date when the primary is advertised by the political organisation in question, unless the campaign of the candidate concerned began earlier. In case of a presidential election, the reporting period shall begin at the point in time when the candidacy is submitted to the Ministry of Justice, unless the candidate's election campaign has begun earlier. The reporting period shall end at the point in time when the accounts are submitted to the Icelandic National Audit Office as provided for in Article 11.

The second and third items in the above-mentioned recommendation propose that the end of the reporting period for a primary election candidate's first report following the primary be defined and that, if the campaign accounts reveal a positive or negative balance, the candidate shall submit further reports on a regular basis until the excess funds have been disposed of or the debt retired. In the opinion of the majority of the committee, these comments were justifiable, as it is not a given that a candidate's campaign finances have been wound up at the time of the first report; therefore, it is not certain that the campaign accounts thus submitted provide an accurate view of the final financial position. For example, the campaign accounts may show a negative balance that the candidate must address, either by soliciting further contributions from legal entities and individuals or by covering the shortfall him- or herself. On the other hand, the campaign accounts could show a positive balance if the campaign expenses proved lower than the contributions intended to defray them. In both instances, it is appropriate that candidates be required to report on the final settlement of the campaign accounts; that is, whether further donations are solicited or how excess funds are allocated. In line with this, the amendments in Act No. 121/2010 set down statutory rules stating that if the accounts for the election campaign show a positive or negative balance, the candidate shall submit new accounts to the Icelandic National Audit Office each year, until the surplus has been allocated or the debt retired.

As regards the second item in particular, the majority of the committee was of the opinion that the Act states clearly that the first report is to include all contributions and all expenses incurred as a result of the campaign.

2.4 The fourth recommendation

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

The GRECO evaluation report states as follows concerning this recommendation:

> "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).”**

In general, it can be argued that transparency and restraint in political organisations’ and candidates’ funding would be enhanced if donors’ identity were made public prior to elections. It can be assumed that, as is mentioned in particular in the recommendations, such disclosure would be conducive to open discussion of campaign funding, particularly in instances of possibly inappropriate connections. On the other hand, it could be difficult to ensure, through such rules, that interim reports give an accurate view of the matter under scrutiny. It could prove difficult to prevent political organisations and individual candidates from trying to improve their image; for example, by choosing to solicit contributions after the election. Furthermore, it is primarily in those instances when contribution amounts are considered inappropriately large that a discussion of possibly questionable practices will arise. It can be assumed that the provisions on maximum contributions from legal entities and individuals actually prevent the development of a legitimate occasion for such discussion, unless other factors are involved as well. The experience gained so far from the implementation of the Act supports this conclusion. With reference to this, the majority of the committee concluded that it was not advisable, at least at present, to pass into law a disclosure requirement like that in the recommendation.

2.5 The fifth recommendation

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.

The GRECO evaluation report states as follows concerning this recommendation:

“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."**

It should be noted that the above recommendations were made before the first summaries of political organisations' annual accounts were published by the Icelandic National Audit Office as provided for by the Act, and before a final decision had been made on the format of the summaries. The format of the summaries was decided in mid-2008 by the Icelandic National Audit Office, in consultation with political organisations, and summaries of the political organisations' consolidated accounts for 2007 and 2008 have been published on the Icelandic National Audit Office website. Summaries of the consolidated accounts for the operational year 2009 are expected later this year. The same applies to the publication of summaries of candidates' election campaign accounts; cf. Article 11 of the Act. The Icelandic National Audit Office has prepared and published on its website a financial reporting form for candidates, to be used for submittal of information to it. As regards candidates, these provisions were first implemented following the 2009 Parliamentary elections, and summaries of candidates' campaign accounts have now been published in a standardised format on the National Audit Office website, according to the provisions of the Act. The Icelandic National Audit Office's execution according to the above has been in compliance with the law on this point, and in line with the views stated in the GRECO recommendations. However, the new legislation, Act. 121/2010 made specific amendments to Articles 9 and 11, with the aim of clarifying political organisations' and candidates' duty to disclose information to the Icelandic National Audit Office, and of explaining more clearly, in the actual provisions of the Act, which information from the accounts shall be included in the Icelandic National Audit Office's summaries. The provision specifies a deadline, 1 October each year, for the submittal of information to the Icelandic National Audit Office, whereas the current provision states only that this information shall be submitted on an annual basis. The amendment aims to systematise the disclosure of information to the Icelandic National Audit Office and thereby ensure that the publication of summaries from political organisations' consolidated accounts is not unduly delayed.

2.6 The sixth recommendation.

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.

The GRECO evaluation report states as follows concerning this recommendation:

"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."**

Since the above recommendations were presented in the GRECO evaluation report, a new Act on Auditors, no. 79/2008, has been passed in Iceland. That Act incorporated into Icelandic law European Council Directive 2006/43/EC of 17 May 2006 on statutory audits of annual accounts and consolidated accounts, amending Council Directives 78/660/EEC and 83/349/EEC and repealing Council Directive 84/253/EEC, as it was adopted in the European Economic Area with EEA Joint Committee Decision no. 160/2006. As has been stated previously, the bill includes a number of amendments to previous regulatory instruments on auditors. The Act applies to auditors and their work entailing auditing as defined in the Act. Among the major amendments are the following:

- That all auditors shall be subject to regular quality monitoring.
- That auditors be required to be members of the Institute of State Authorized Public Accountants (FLE).
- That all auditors be required by law to work in accordance with a detailed Code of Conduct set by the Institute of State-Authorized Public Accountants, subject to ministerial approval.
- The role of the Auditors' Council is changed. It carries out a supervisory role regarding the registration of auditors and auditing firms, continuing education, and regular quality monitoring, and ensures that auditors meet the requirements for certification as state-authorised public accountants.
- More stringent requirements concerning impartiality, particularly towards firms connected with the public interest.
- More stringent continuing education requirements for auditors.

It can be expected that the above-specified amendments have brought the Act better into line with the aforementioned Directives. As a result, Icelandic law now makes strict requirements concerning impartiality of auditors and of professional, independent audit, thus complying in full with the European regulatory framework. Nonetheless, international auditing standards have not yet been directly incorporated into Icelandic law. This has been the aim, however, cf. the Temporary Provisions of the aforementioned Act on Auditors, no. 79/2008, which stipulate that, until international auditing standards have been incorporated into Icelandic law, auditing shall, by law, be carried out in accordance with sound auditing practices. The term

sound auditing practices means that the audit is carried out using recognised methods in accordance with the International Standards on Auditing (ISA), issued by the International Federation of Accountants (IFAC), of which the Institute of State Authorized Public Accountants is a member. As such, the discussed international auditing standards actually carry considerable weight in the interpretation of statutory provisions on auditors' responsibilities in auditing accounts in Iceland, including the accounts of political organisations, but it is appropriate to reiterate that the rules and demands applying to the audit of political organisations' consolidated accounts are the same as those applying to the accounts of other legal entities, such as public limited companies.

2.7 The seventh recommendation.

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.

The GRECO evaluation report states as follows concerning this recommendation:

"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.**"

In order to respond to the above-mentioned recommendation from GRECO, the new legislation grants the Icelandic National Audit Office authority to request documentation from candidates in order to verify the information in their financial reports comparable to that which existed for political organisations. The Icelandic National Audit Office is authorised to request further documentation at any time, so as to ascertain that primary election campaign expenses and contributions from individuals and legal entities to the candidate are within the limits specified in Chapter III of the Act.

2.8 The eighth recommendation.

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).

The GRECO evaluation report states as follows concerning this recommendation:

"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).**"

The Prime Minister's Office asked the Director of Internal Revenue's for its opinion of this recommendation. The Prime Minister's Office also requested that the Director of Internal Revenue evaluate whether such a change in tax reporting forms would require an amendment to the Income Tax Act, or whether the forms could be changed without statutory amendment. The Director of Internal Revenue responded by saying that he had no comments or complaints about the GRECO recommendation, adding that he considered it likely that such a change in tax reporting forms would tend to increase transparency and facilitate monitoring. It was revealed that this change in tax reporting forms could be implemented without statutory amendment. Thereafter, the Prime Minister's Office requested that the tax reporting forms for 2009 be changed to accord with the recommendation, and the Director of Internal Revenue has complied with that request.

2.9 The ninth recommendation

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.

The GRECO evaluation report states as follows concerning this recommendation:

"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.**"

In response to the above-specified recommendation, amendments to the sanction provisions in Article 12 of Act No. 162/2006 have been made, with the aim of clarifying the criminal liability of individuals and legal entities according to the Act, and of basing penalties and their framework on the severity of conceivable violations. In this respect, the provisions of the new legislation are in line with the criminal law committee's proposals on possible responses to this recommendation from GRECO, as the review committee specifically requested that the criminal law committee provide an opinion and proposals on this point.

Paragraph 1 of the new Article proposes that anyone who accepts donations, or their equivalent, that either are prohibited according to Article 6 or exceed the permissible amount provided for in Article 7 shall be subject to fines or imprisonment for up to two years. The Article does not propose sanctions against those who provide donations in excess of statutory limits. The term *equivalent* refers to valuables whose monetary value can be assessed; cf. the definition in Article 2, Paragraph 1, Subparagraph 4 of the Act. Paragraph 2 recommends that neglecting to submit reports or information to the Icelandic National Audit Office within specified time limits be punishable by fines, with the same penalty applying if the information submitted is not in compliance with set rules. Paragraph 3 proposes that legal entities violating the provisions of Paragraphs 1 and 2 be liable for fines. In other respects, reference is made to Chapter II-A of the General Penal Code concerning the criminal liability of legal entities. Paragraph 4 proposes that violations of Paragraphs 1 and 2 be punishable irrespective of whether they were committed intentionally or due to negligence. In addition, Paragraph 5 proposes that attempted violations and participation in violations shall be punishable in accordance with Chapter III of the General Penal Code. Finally, Paragraph 6 proposes that it be permissible to seize unauthorised donations or donations in excess of statutory limits and submit them to the Treasury.

With these amendments, it is clear that the sanction provisions of the Act fully meet the requirements for clarity. Therefore, it should be clear to all those operating on the basis of the Act which violations could be punishable under the Act, which enhances the precautionary effect that the sanction provisions are intended to have.

The expert committee discussed the possibility of adopting administrative penalties of some type – such as administrative fines – in this area. The conclusion was, however, that there was no reason at present to pass such sanction provisions, as the experience gained from implementation of the Act was insufficient to enable a satisfactory assessment of the need for such measures. In this context, however, it is appropriate to point out that the amendments in legislation made by Act No. 121/2010

state that Treasury allocations to political organisations according to Article 5, Paragraph 1 of the Act be subject to the applicant's satisfactory prior fulfilment of the requirement to submit information to the Icelandic National Audit Office, pursuant to Article 9. Such a provision actually serves the same purpose as the authorisation to impose administrative fines, as it can be assumed that political organisations will fulfil their duties in this regard if they are indeed entitled to Government subsidy.

3. Conclusions.

In view of the above, The Icelandic Government concludes that Iceland has now implemented satisfactorily or dealt with in a satisfactory manner all of the nine recommendations addressed to Iceland be GRECO in the Third Round Evaluation Report (Theme II) – Transparency of Party Funding.