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Indian Democracy Paying for Political Funding: A Socio-Legal Perspective

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ABSTRACT - This article keeps its focus on the global phenomenon of relationship between businessmen, politicians, bureaucrats and white collar crimes committed by the prestigious personalities in respect of funding to political parties. In Indian context too this is a widespread practice in the elections and otherwise providing funding to politicians and their parties indirectly to obtain the benefits after winning the elections. There are so many laws and policies made by the governments to reduce or prevent these illegal practices but lacking a strong legal framework. Although it was considered as a necessary tool for the development of political parties or of democracy to provided funding by the corporate world like Birla and Tata, before independence and after independence too, like main corporate houses as Reliance, yet its excessive use and bad effects has deteriorated the Indian democracy and political practices. To prevent the practices in political funding in our country it is required to set effective enactment as in UK and France.

Keywords: *Democracy, Political Funding, Global Phenomenon, Electoral Trust, Corporate Funding, Party Funding, Legal Framework, Representation Of People Act, 1951, Santhanam Committee, Wanchoo Direct Taxes Enquiry Committee, Confederation Of Indian Industry (Cii), Election And Other Related Laws (Amendment) Act In 2003, The Companies Act 2013, The Income Tax Act, 1961, Association Of Democratic Reforms, Fund-Raising Practices, Limit On Corporate Funding, Grass-Root Funding*

I. Introduction

Politicians take money out of the exchequer, sell patronage and extort money, all in the name of mobilizing funds for political activity.¹

It is a global phenomenon of relationship between business world, politicians, bureaucrats and crimes by the prestigious personalities in domain of white collar crimes which is well known by the modern society. This reality lies in Indian phenomenon too witnessing the recent scams like 2G, Coal, Satyam and Vyapam Scam especially political funding or business donations to political parties is one of the main causes of corruption and cronyism in the country which requires reforms. Consequently, the principles of accountability and transparency in corporate funding, requires increased focus and, to set up an “Electoral Trust” was approved by the Central Board of Direct Taxes (CBDT).

According to the Global Integrity Report published by the IDEA, India ranked 11 globally, well over its South-Asian peers, even China. However, when it came to Government Accountability, the difference between India's score in the 2009 report and the 2011 report is unappreciable. It has remained in the same bracket-that of being 'very poor', even though it scores highly on Judicial Accountability. The reason behind this is its low score when it comes to 'funding of political parties' – a universally accepted determinant of the transparency and integrity of the democratic process.

Political parties are essential for the organization of the modern democratic polity; and are crucial for the expression and manifestation of political pluralism. In order to carry out their core activities, they need appropriate funding. However, with this come the inherent twin fallacies of the undue influence of money on the democratic political process; and the illegitimate enrichment of politicians. Thus, funds play a very important and potentially distorting effect on the democratic process, and are ought to be properly regulated by public law.

The traditional type of party financing, that through membership fee, is not viable in the present day and age. Private funding other than through membership fee-such as contributions made by parliamentarians through deductions from their statutory allowance or donations come with their own set of problems. In this context, the mere impression of misuse of funds may in itself be sufficient to erode public confidence in the political system and its political actors. The economic liberalization of 1991, which introduced drastic policy reforms that changed the social and political landscape of the country forever, was expected to bring an end to the corruption that had plagued the country since the 1970s. However, even after two decades of liberalization, an economically resurgent India is still ridden with a crisis of governance- scams and scandals dominate the headlines, providing fodder to detractors of the government and affecting the reputation of the country at the international level.

Through this paper, the author seeks to argue that the widespread and pervasive corruption in India is already account of the flawed political party funding and election expenditure laws, which driver parties and politicians to misuse the government's discretionary powers over resourced action of raise funds for election campaigns and politician parties. For the sake of brevity, the paper has been divided into four parts dealing with the subject's historical evolution, the legal framework for political party funding in India, a global comparative analysis and the future of political party funding in India, in that order.

II. The Evolution of Political Funding in India

Any well-functioning democracy requires vibrant political parties and competitive elections. Political parties perform several crucial functions, including : (i) the integration and mobilization of citizens; (ii) the articulation and aggregation of interests; (iii) the formulation of public policy; (iv) the recruitment of political leaders; and (v) the organization of the Parliament and the Government.² In order to effectively carry out these functions, the political parties and their candidates need ample financial resources. The evolution of this funding process in India can be broadly divided into two periods.

Before 1990

Traditional, political parties in India financed themselves through private donations and membership dues.³ Although corporate contribution was allowed, it was subject to certain restrictions and had to be duly accounted for by the company.⁴ A major step towards ensuring compliances was the enactment of the *Representation of People Act, 1951*, (hereinafter, "RPA") wherein limits were introduced on the amount that could be spent on election campaigns. Candidates who exceeded these limits stood the risk of getting disqualified and their elections getting annulled.⁵ By the 1960s, the

phenomenon of black money⁶ funding political parties had become an accepted reality. Ample amount of light was thrown on the issue of black money entering the political corridors through the *Santhanam Committee on Prevention of corruption*⁷ and the *Wanchoo Direct Taxes Enquiry Committee*.⁸ During this period, there was a marked tendency amongst businesses and individuals to evade corporate and income taxes on account of the highly regulatory and protectionist policy framework in the nascent years of the country's independence.

Later, the Indira Gandhi government, through the placing of a blanket ban on all corporate donations to political parties, sought to prevent large business groups from exercising undue influence on politics.⁹ However, no manner of state funding as a substitute to corporate funds was provided, making the reliance of political parties on black money an unfortunate necessity.

The Judiciary played its part in these early stages too. The Supreme Court, in the case of *Kanwar Lal Gupta v. Amar Nath Chawla*¹⁰ ruled that party spending on behalf of a candidate should be included while calculating that candidate's election expenses in order to determine whether the election expenditure limit has been violated. However, this judgment was effectively nullified by the amendment of the RPA in 1975.¹¹ Thus, the limit on election expenditure became largely ineffective as though there was a limit on the direct personal expenditure of the candidate; there were no discernible limits on the expenditure of the party or the supporters of the candidate.

The main development in the 1980s was the amendment of the Companies Act in 1985, which through Section 293A, once again allowed corporate donations to political parties under certain conditions, subject to approval by the Board of Directors and appropriate disclosure.

After 1990

In 1993, the Indian industry became publicly concerned about the issue of political funding, with the Confederation of Indian Industry (CII) setting up a task force which recommended¹² that corporate contributions be made tax-deductible and that shareholder confirmation of board decisions about political contributions is required. Thereafter, in 1996, the *common Cause Judgment*¹³ forced political parties to declare their annual incomes thus bringing transparency in party finance; whereas the amendment of the RPA, based on the Goswami Committee recommendations,¹⁴ facilitated cost reduction by reducing the campaign period from 21 to 14 days.

Another major change brought about by the amendment was revising the expenditure limits to Rs. 4,50,000 and Rs. 1,50,000 for Lok Sabha and state assembly constituencies respectively, the figures which in 1997 were further revised to Rs. 15,00,000 and Rs. 7,00,000 respectively of the RPA was not amended, thus leaving open the window for black money to infiltrate into the process of political funding. Thereafter, in 1998 the government provided a partial state subsidy in the form of allocation of free time for seven national and 34 state parties on the state-owned television and radio networks.¹⁵ The *Indrajit Gupta Committee Report*¹⁶ recommended partial state funding in kind and the denial of state funding to parties that failed to maintain and submit audited accounts and income tax returns. The committee also recommended a separate election fund to which the central and state governments would together contribute Rs. 5000 million annually. However, a majority of the state governments expressed their inability to do so. Sadly, even this committee remained non-committal towards Explanation 1 to Section 77 (1) of the RPA.

The true wave of important changes started after the year 1999, especially with regard to more detailed disclosure of candidates. The decision in *Association for Democratic Reforms v. Union of India*¹⁷ made inroads to the Election Commission, directing it to collect data on the criminal record of candidates and to make this information available to public, along with information on educational qualifications, and the assets and liabilities of the candidates.¹⁸ In spite of challenges, this judgment was reaffirmed on

March 13, 2003 and the Election Commission issued an order based on this judgment on March 27, 2003, making such declarations mandatory.¹⁹

Following this, the most significant development in campaign finance reform was the *Election and Other Related Laws (Amendment) Act* in 2003, which brought about, among other changes, the long awaited amendment of Explanation 1 to Section 77(1) of the RPA, redefining the boundaries of candidate's expenditure.

III. The Legal Framework of Political Funding in India

Over six decades since the legislature took its first step towards a legislation governing the funding of political parties, the situation still presents a sordid state of affairs. To be understand where the system has fallen short, we need to undertake a discussion of the legal framework and the loopholes in the system.

The Representation of People Act, 1951

Section 29B of the RPA provides that 'subject to the provisions of the Companies Act of 1956, every political party may accept *any amount of contribution voluntarily offered* to it by an person or company other than a government company.' Further, the proviso states that no political party shall be eligible to accept any contribution from any foreign source.²⁰

Thus, there are no limits on individual donations to political parties or political candidates as per the relevant provision of the Representation of People Act, 1951 stated above. Further, as to the requirement of the disclosure of donations to political parties, the relevant Provisions- Section 29C,²¹ and falls drastically short since it does not require the public disclosure of reports mandated by it.

Under the RPA, and the Conduct of Elections Rules, 1961, the Election Commission of India has limited powers to ask for accounts or information regarding political parties' and candidates' contributions and campaign expenditures. The law provides for ample civil and criminal consequences for violations of financing or accounting norms,²² but in practicality, they have hardly been put into application.²³

Lastly, Section 77 of the RPA, read with Rule 90 of the Conduct of Election Rules, 1961 prescribes the maximum expenditure that can be incurred by a candidate that has to be accounted for as per procedure. By an amendment of the rule in 2011, the limits have been increased further, depending upon the size of the states and the Union Territories.

The Companies Act, 1956

Section 293 (1) (e) of the Companies Act, 1956, empowers the board of directors of a company to continue "to charitable and other funds not directly relating to the business of the company;" sums not exceeding Rs. 50,000 or 5% of the average net profits of three financial years whichever is greater. The High Courts of Bombay and Calcutta have taken the view that donations to political parties are covered by this provision and that companies could lawfully make donations to political parties if such a power was conferred by the objects clause in the Memorandum of Association.

In *Jayantilal Ranchdass Koticha vs Tata Iron & Steel Co. Ltd.*,²⁴ Chagla, C.J. observed:

“We think it our duty to draw the attention of Parliament to the great danger inherent in permitting companies to make contributions to the funds of political parties. It is a danger which may grow apace and which may ultimately overwhelm and even throttle democracy in the country.”

Similar views were also expressed by the Calcutta High Court in *Indian Iron and Steel Co. Ltd., In re.*²⁵

In its report²⁶ published in 1957, the Companies (Amendment) Act Committee referred to both these judgments and recommended that full information relating to such contributions should be incorporated in the accounts. Consequently, Section 293 was inserted imposing limits to the amount which could be donated in any financial year.²⁷

However, the issue concerning donations to political parties by corporations continued to be a matter of debate even after the incorporation of Section 293A. By the Companies (Amendment) Bill, 1968, donations to political parties were banned altogether. However, by the Companies (Amendment) Act, 1985, a new section 293A was enacted replacing the old section to permit political donations. Now the maximum amount that can be donated cannot exceed 5% of its average net profits.²⁸

The Companies Act 2013 – Political Contribution²⁹

As per section 182, Political Contribution means the expenditure incurred directly or indirectly by a Company on an advertisement in any publication, being a publication in the behalf of a political party or any contribution of an amount to such Politically Party and where such publication is not by or on behalf of, but for the advantage of a Political Party, shall be deemed to be a contribution for a political purpose. Restrictions are imposed on contributing directly or indirectly to any political parties on following : (a) A Government Company and (b) A company which has been in existence for less than 3 financial years.

- Maximum Amount of Donations can be 7.5% of Average Net Profits during the 3 immediately preceding financial years.
- Board resolution is required for political contribution and disclosures are also required to be made in P/L account for total amount contributed and name of the party to which such amount is contributed.
- If the company makes any contribution, in contravention of the provisions of the law then company will be punishable with fine up to 5 times the amount contributed and every officer in default will be punishable with imprisonment up to 6 months and with fine up to 5 times the amount contributed.
- Companies contributing any amount to Electoral Trust Companies for contributing to a political party are not required to make disclosures as required under section 182(3) of the Companies Act, 2013 only amount contributed to trust need to be mentioned in accounts of the company. Electoral Trust Companies will be required to disclose all amounts received by companies and contributed to political party.

The Income Tax Act, 1961

Section 80 GGB of the Income Tax Act, 1961 permits deductions for contributions by any person³⁰ to a political party³¹ in the computation of total income of such person. No limit has been prescribed regarding the amount that can be contributed as in the case of companies. Tax incentives like giving deduction for contributions produce the same financial strain on government as direct spending. However, direct expenditure has the merit that is identifiable, whereas the same cannot be said for expenditure in the form of tax reduction. Tax economists³² consider spending through incentives, exemptions and deductions as unreasonable as it goes against the concept of neutrality in a tax system distorting the concept of ability to pay.

Also, the giving tax benefit to political parties suffers from the following loopholes:³³

- a) No direct nexus with the carrying on of a business of profession;
- b) The political parties may put pressure and threats on business houses for making contributions;
- c) Permission accorded for political donations has not, in any manner, helped in advancing the cause of democracy; and
- d) This makes it difficult for small or independent parties to contest the elections.

The Election and Other Related Laws (Amendment) Bill 2003 (Funding Reform Bill)

This was a crucial change proposed in the Indian electoral process. It stipulated full tax exemption to individuals and corporate on all contributions to political parties. There was an effective repeal of Explanation 1 under Section 77 of RPA-expenditure by third parties and political parties now came under ceiling limits and only travel expenditure of leaders of parties was exempt. The act further stipulates equitable sharing of time by the recognized political parties on the cable television network and other electronic media.

Thus, the new act made sure that there was an increase with respect to transparency of funding. It also helped in providing raising resources for legitimate campaign expenditure. However, even this act suffered form deficiencies. No penalties were mandated for donor for non-disclosure of funding. The provision in an earlier draft for auditing by a chartered accountant from a panel approved by the CAG was deleted. Furthermore Even this act did not provide for any form of direct public funding to candidates or parties.

IV. A Global Perspective on Political Party and Election Finance Regulations

India is one of the fastest growing economies of the world, and going by the rate of growth of the last one decade, is touted to become a global superpower in the next decade. However, this image is tarnished at the international level by the rampant corruption and policy paralysis that successive governments are accused of suffering form.³⁴ It is thus imperative that we take a holistic vies of global best practices in every aspect of policy making, political funding no exception.

Australia

The Australian political finance regime is largely open and unregulated. There is no ban on donations from foreign interests³⁵ or on corporate donations.³⁶ When it comes to anonymous donations, there is no blanket ban as such, but there is a specific limit on donations exceeding \$ 5000.³⁷ there are also no limits prescribed to the limit on the amount which a donor can contribute to a political party or a candidates.³⁸ There are specific bans on vote buying³⁹ and state resources being used in favor or against a political party or candidates.⁴⁰ However, there are no limits on expenditure. Both parties and individuals have to report regularly on their finances and this information is to be made public. There is a separate institution-titled the commonwealth Director of Public Prosecutions, which has a formal role in political

finance oversight. There are sanctions in the form of fines and imprisonment for political finance infractions.

France

In France, public subsidies for parties and candidates were introduced from 1988, and corporate donations were banned from 1995.⁴¹ There is also a ban on donations from foreign interests.⁴² Public subsidies were over 50% of party income in 1998 and 90% of headquarters income for small parties. There are both contribution limits and spending limits for both parties and candidates. Tax deductions are available upto 40% of individual donations and party membership dues. Parties have freedom and autonomy despite public subsidy but have to disclose all contributions received.⁴³ The sanctions for political funding infractions are fines, imprisonment, loss of public funding and loss of elected office.⁴⁴

Germany

In Germany, tax deductions for small donations and party membership dues have existed alongside public funding since 1959. Since 1992 tax deductions for corporate donations have been removed. Public funding exists on a matching grant basis in which the ceiling for public subsidies is the income obtained by parties from private sources.⁴⁵ Public funding is for parties with no earmarking for elections or other activities. There are no expenditure or contribution limits and disclosure of donor identities and amounts is limited to big donors. Over time this system has led to the bulk of party income from private sources coming from individuals other than corporations.⁴⁶

United Kingdom

The Political funding regime in the United Kingdom shows a marked difference from the other European democracies as there is an absence of direct or indirect state subsidies.⁴⁷ The regime otherwise is tightly regulated on account of the *Political Parties, Elections and Referendums Act, 2000*. Thus, there is a ban on donations from foreign interests. On the other hand, there is no ban on corporate donations of any kind. Even anonymous donations are not banned entirely, but are restricted.⁴⁸ There are expenditure limits for both parties and independent candidates. There are disclosure norms stipulated for the reporting of campaign financing for both political parties and candidates. The sanctions imposed for political finance infractions include fines, imprisonment, forfeiture and deregistration of parties.⁴⁹

United States of America

The U.S. system does have limits on contributions but not on expenditure, unlike India. The Supreme Court's decisions in *Buckley v. Valeo*⁵⁰ and more recently, *Citizens United v. FEC*⁵¹ have firmly laid down the policy framework for political funding. There is a ban on donations from foreign interest⁵² and on corporate donations to political parties and candidates. Tax relief is available as an indirect public funding source.⁵³ Vote buying is banned⁵⁴ and limits are placed on the expenditure by political parties and candidates.⁵⁵

Commitments and Realities

As elucidated previously, the deficiencies in the system of political financing are increasing in magnitude and diversity. As such, it is important to understand the most pressing issues concerning the regime in India today.

Present Scenario

In 2011,⁵⁶ the Chief Election Commissioner, S.Y. Quraishi called for corporate funding and donations being made subject to audit and disclosure so as to deduce the nexus between the party and a corporate.⁵⁷ In a report published in Economic Times on January 10, 2012⁵⁸ it was observed that the Aditya Birla Group increased its contribution to political parties about fourfold to Rs. 30.5 crore in 2009-10 while the Bharti Group cut it from Rs. 17 crore to zero. A general trend that has been observed is that a

majority of companies do not want to lean towards any one party and that politicians, even of a national stature, openly demand black money.⁵⁹

In news reports as late as August 2012,⁶⁰ it was reported that in the past five years, Indian companies have donated over Rs. 4400 crore to six major political parties,⁶¹ averaging over 870 crore per year. A similar observation was made in a recent report published by the Association of Democratic Reforms (hereinafter, “ADR”).⁶² notably, donations from named contributors formed a very small percentage of the total income. In a report dated September 25, 2012,⁶³ the two major political parties refused to divulge the details of contributions made to them in the previous year.

V. The Winds of Change: Proposed Legislations and their Impact

In a recent position⁶⁴ espoused by ASSOCHAM, one of their key demands is that both spending and expenditure during elections should be without any caps to the flow of donations. In contrast, the pending Companies Bill, 2011⁶⁵ has provisions stipulating that corporate funding to political parties must increase from 5% to 7.5%⁶⁶ of the average net profits earned by a company during the three immediately preceding financial years. A novel step here has been suggested by ADR by drafting the *Political Parties (Registration and Regulation of Affairs, etc.) Bill, 2011*,⁶⁷ under the chairmanship of Justice M.N. Venkatachaliah.

The bill makes a plethora of suggestions for the regulation of the constitution, functioning accounts, audit, and other affairs of and concerning political parties participating in elections. Chapter III of the draft, relating to finances, stipulates disclosure and donation limits and requirements.⁶⁸ It also empowers the Registrar to specify any other sources from which donations may not be accepted by political parties or candidates. Further, upon the enquiry of the Registrar into any infraction, sanctions such as penalties, imprisonment and non-entitlement to tax benefits have been envisaged.⁶⁹ It needs that all political parties should stick to transparency in funding process while receiving money for polls from the corporate concerns. Indian democracy has developed its values in many years but still there is no transparency in respect to political funding. If we do not remove in political funding the opaque system any level of economic growth cannot be inclusive.⁷⁰

VI. Conclusion

The above discussion keeps before us various thoughts and multifaceted problem to be analyzed and sorted out. Consequently, the following points to be considered:

- The expenditure ceilings appear to invite evasion. The low expenditure limit tends to induce dishonesty, a profoundly unhealthy development for any democracy.
- The absence of public funding means that parties and candidates must raise and spend money on their own for each election. This has exacerbated the dependence on black money and institutionalized corruption.
- The lack of any effective system of internal transparency and accountability within parties reinforces corrupt fund-raising practices.
- The limit on corporate funding to parties, even though proposed to be increased, can be increased even further so as to reduce the reliance on black money.

- Contributions to individual candidates is not allowed, which forces them to raise funds through illicit means.
- Finally, party leadership, under the current system has no incentive to raise funds through grass-root funding.

The solution to these problems lies in taking a holistic views of the global best practices when it comes to political funding mechanisms. Every long standing democracy of the world has something to offer and inculcate. The practice of public funding of political parties and grass-root funding prevalent in Western European democracies should be given careful consideration as a viable way of the future. Individually, practices from countries such as internal political party regulation from Germany can be adopted. In terms of disclosure and transparency norms, the U.S. political funding practices represent a benchmark that is worth emulating. From the U.K. the stellar practice of taking shareholder approval before making corporate donations can be incorporated.

Additionally, the practice of electoral trusts carried out by the Tata and Birla conglomerates is an innovation that can be adopted on a larger scale by other corporate groups. Electoral trusts fund all political parties above a certain level, including independents and local candidates, which provide a certain degree of transparency to the process. Even futuristic practices such as creating an electoral fund out of the donations of the net taxpayer base of a country can be taken into consideration for providing a wholesome remedy to the loopholes existing in the political funding regime.

The transparent funding which should include to reveal source of donations through a separate election account would remove the public perception that a quid pro quo through illegal granting or donating business and political level classes.

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20. Defined under clause (e) of §2 of the Foreign Contribution (Regulation) Act of 1976 (49 of 1975)
21. Declaration of donation received by political parties-(1) The treasurer of a political party or any other persona authorized by the political party in this behalf shall, in each financial year, prepare a report in respect of the following, namely:
 - (a) the contribution in excess of twenty thousand rupees received by such political party from any person in that financial year;
 - (b) the contribution in excess of twenty thousand rupees received by such political party from companies other than Government companies in that financial year.
 - (c) The report under sub-section (1) shall be in such form as may be prescribed.
 - (d) The report for a financial year under sub-section(1) shall be submitted by the treasurer of a political party or any other persona authorized by the political party in this behalf before the due date for furnishing a return of its income of that financial year under section 139 of the Income-tax Act, 1961, to the Election Commission.
 - (e) Where the treasurer of any political party or any other person authorized by the political party in this behalf fails to submit a report under sub-section (3) then, notwithstanding anything contained in the Income-tax Act, 1961, such political party shall not be entitled to any tax relief under the Act
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27. Sub section (2) also requires the company to give particulars in its profit and loss account of the amounts donated and the names of the political party or persons who were the recipients of these donations
28. Determined in accordance with the provisions of Sections 349 and 350 during the three immediately preceding financial years
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