

Prioritising our regulatory activity

Audit, advice and campaign monitoring

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Translations and other formats

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Tel: 020 7271 0500

Email: publications@electoralcommission.org.uk

We are an independent body set up by the UK Parliament. Our aim is integrity and public confidence in the democratic process. We regulate party and election finance and set standards for well-run elections.

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1 Introduction

1.1 The value of a risk-based approach to regulation was highlighted by the 2005 Hampton report.¹ The report set out principles including the use of comprehensive risk assessments, provision of authoritative and accessible advice, and proportionate and meaningful sanctions. We set out our proposals to introduce an approach based on these principles as part of our *Better Regulation of Party and Election Finance* consultation in July 2009². We received a range of responses that have contributed to our approach to targeting our regulatory activity. The approach outlined in this document sets out how we will prioritise our resources to ensure they are used most effectively, so that we can achieve the most with the limited resources available to us.

1.2 An approach such as the one we have adopted is now a core part of regulatory good practice. It is **not** intended to create a 'league table' of parties' ability to comply with the law, or to predict where breaches of the law may occur. Rather, it is intended to help ensure that we are consistent, proportionate and transparent in specific areas of our regulatory activity: auditing, providing advice and campaign monitoring. It will make it easier for those we regulate and the public to understand what we do and how we do it.

¹ Philip Hampton, March 2005, *Reducing administrative burdens: effective inspection and enforcement*, available from www.berr.gov.uk/files/file22988.pdf. The Hampton Report sets out principles of good regulatory practice including the use of risk assessments, provision of authoritative and accessible advice, and proportionate and meaningful sanctions.

² http://www.electoralcommission.org.uk/_data/assets/pdf_file/0004/83074/Better-regulation-of-party-and-election-finance-consultation-2.pdf

2 Prioritising our regulatory activity

Why prioritise our regulatory activity?

2.1 As the regulator of party and election finance, we are concerned with the risk that those we regulate may fail to comply with the rules, and the impact that failure could have on public confidence that political finances are transparent and that the rules are followed.

2.2 We have developed risk-based profiling to inform the way in which we audit the records and processes of political parties and their accounting units, focusing particularly on those that operate on a large scale, have significant income or have had past problems in complying with the law. We also use risk to target our monitoring of electoral campaigns, and to help us decide when to offer advice on our own initiative to those we regulate.

2.3 Over 400 political parties are registered with the Commission, and some larger parties have registered accounting units which have their own legal obligations under the Political Parties, Elections and Referendums Act 2000 (PPERA). All parties have to report to us about donations and loans they receive, and keep accounting records. We have powers under PPERA to ensure they do this properly. We already seek to carry out this regulatory role in an efficient and risk-based way – for instance, where we are aware that a political party or one of the other organisations that we regulate is struggling to comply with its legal obligations, we will offer help as needed and monitor future compliance carefully.³

2.4 Wherever possible, we seek to use advice and guidance, rather than enforcement action, in order to secure compliance with the law. This reflects the Hampton principle that helping people to understand what they have to do from the outset, and supporting them to get it right, is the most effective way of securing compliance. We provide help to those we regulate in a variety of ways. We explain the requirements of PPERA to political parties when they first register with us. We publish a range of guidance on how to comply with the law on our website. Our Advice and Guidance Team is always ready to provide advice on specific matters, and can provide formal written opinions on difficult issues if needed. We also offer training to party staff, candidates and agents.

³ Minor parties are not included in risk profiling as they do not have many statutory reporting requirements and, by definition, they have a small and limited operational scale.

2.5 In 2009 we consulted on our future regulatory approach, including proposals to adopt a more formal risk methodology to ensure that our approach to regulation is as consistent and transparent as possible, and that we use our resources effectively. Responses to the consultation were supportive, and raised some helpful queries about how we would organise and prioritise this aspect of our work.⁴ We have consequently refined our proposed approach to make its aims and mechanics as clear as possible.

2.6 We use formal processes, including risk profiling, to plan three aspects of our regulatory work:

- auditing financial records and processes
- assessing when to offer advice to those we regulate
- monitoring election campaigning activity

⁴ http://www.electoralcommission.org.uk/_data/assets/pdf_file/0014/100139/Report-on-Enforcement-Policy-Consultation.pdf

Auditing financial records and processes

How we assess parties and accounting units

2.7 We develop profiles of parties and larger accounting units to support our audit strategy, which is outlined later in this document. We select registered political parties and their accounting units for monitoring and, where appropriate, for audit, by assessing them against the following characteristics:

- **financial** position – if a party has a relatively high level of income, has significant debts or cash surplus, receives public funding, or has submitted accounts that contain material inaccuracies, it is more likely to be selected
- past **compliance** record – if a party has a poor recent compliance history, it is more likely to be selected
- **operational** scale (central parties only) – if a party has contested elections, holds elective office or has a relatively complex operational structure (for instance, a number of accounting units with separate financial management), it is more likely to be selected

2.8 We are developing profiles against these characteristics of each registered political party, and of those party accounting units with annual turnover of over £25,000. Our assessment of parties and accounting units against these characteristics is based entirely on publicly available (or non-confidential) information, such as past compliance failures, activity at elections and statements of accounts. The profile has three parts, covering the organisation's finances, compliance and operational scale.

Part one: Finances

2.9 Our profiling of **finances** is based on information relating to financial scale, cash flow and past accounting accuracy, derived from the statements of accounts which parties and larger accounting units are required to provide to us under PPERA. These indicators illustrate the volume of regulated transactions a party is likely to be managing and possible funding pressures. The indicators we use relate to reported income, net assets/liabilities, material inaccuracies in accounts and receipt of public funds.

2.10 We weight these indicators to produce a rating of A, B or C for each party. A rating of 'C' may indicate, for instance, a party with high levels of debt that has had its recent statements of accounts qualified by an auditor. A 'B' rating may typically be a relatively high-income party with no material inaccuracies in its recent accounts. An 'A' rating will indicate a low-income party.

2.11 If a party has a rating of 'B' or 'C', this indicates that the party operates on a scale where failure to comply with the regulatory requirements may have a significant impact. If a party's financial position remains broadly similar from year to year its rating is unlikely to change significantly over time, although the rating may improve to some extent if the party can avoid material accounting errors.

Part two: Compliance record

2.12 We profile a party's **compliance record** on the basis of reporting performance and breaches of the law over the past three years. This illustrates a party's capacity to comply with its obligations. The indicators we use include late submission of statutory returns, late reporting of donations and loans, late submission of registration details and other breaches of the law. The full list of indicators we use is in Appendix A.

2.13 Again, we weight the indicators to produce a rating of high, medium or low. A 'high' rating indicates a good compliance record over the same period. A rating of 'low' means that the party has a record of significant compliance failures in the last three years. If a party's compliance record improves over time, its rating will improve accordingly.

Part three: Operational scale

2.14 We profile **operational scale** through indicators such as the number of accounting units registered by the party, the level of elected office held by members of that party (e.g. local or national representation) and the number of elections it has contested in recent years. This helps to illustrate the scale of the party's activity and therefore how significant the impact of a failure to comply with the regulatory requirements might be. The full list of indicators we use is in Appendix A. This characteristic does not apply to accounting units.

2.15 The indicators for operational scale produce a rating of between 1 and 5, as shown in Appendix A. Those parties rated 4 or 5 will hold significant elected office, may have a high number of accounting units and will have contested most elections in the last five years. Those rated 3 may hold elected office in local authorities and have received reportable donations in the last year. Those rated 1 or 2 will be newly registered parties and those that have contested few elections in the last five years, and hold no significant elected office. This rating is only likely to change significantly if a party markedly ramps up or scales down its activity over time.

Who sees the profiles?

2.16 Once the profiles have been fully updated each year with data from parties' latest statements of accounts and other statutory returns, we will contact parties individually to inform them of their profile and its implications in terms of interaction with our audit function (see paragraphs 2.18-2.25 below). The

profiles and accompanying explanatory information will also be published on our website annually after they have been updated and the parties have been informed.

2.17 We will publish the profiles, and the supporting information, of parties and accounting units in both Great Britain and Northern Ireland. Information and profiles relating to parties in Northern Ireland are being published because the information on which the profiles are based on does not include anything we are barred from publishing during the prescribed period.

How risk profiling informs our audit strategy

2.18 To support our statutory remit of monitoring compliance with the rules on party and election finance, PPERA gives us supervisory powers to monitor the income and spending of organisations we regulate, and to audit their accounts. Those party accounting units with a low turnover do not have to submit their accounts to us for publication, but do have to keep adequate financial records. We need to ensure that parties and their accounting units have robust processes in place to account for their income and spending. We may undertake an audit of a party's procedures and records to confirm this.

2.19 The aim of audit is to provide assurance as to the accuracy and completeness of returns made to the Commission. We check both the validity of transactions identified for inclusion in returns (accuracy), and that there are robust processes in place to ensure that all appropriate transactions have been identified and included (completeness). Availability of resources dictates that we can never check every single transaction, so our audit strategy seeks to provide a reasonable level of assurance that parties and accounting units have the appropriate systems in place to ensure compliance. We target our audit activity at the areas where it is most needed in a structured approach to ensure the most efficient and effective use of resources, so that this specialist resource is directed where it is most needed in improving compliance.

2.20 Risk profiling is a key element in providing an effective and efficient audit service. Given the large number of parties and accounting units, an intelligence-led process is essential in identifying those who would gain most benefit from our audit activity. This approach also ensures that audit activity is focussed on meeting the Commission's objectives in relation to transparency of party finance, rather than relying on an ad hoc approach with audit activity determined only by random sampling selection.

2.21 The nature of the information used in producing our profiles means that smaller parties, those with low annual income, those who contest fewer elections and those who do not hold elected office will not routinely be identified as high risk. However, we will undertake some random audits of parties with lower rated financial and compliance risk profiles, in line with good regulatory practice, to supplement our risk-based work and test the effectiveness of our profiling. Random auditing aside, we identify parties and accounting units for auditing on the basis of overall profile ratings as set out in Appendix B.

2.22 Our audit staff are likely to contact those that fall within the 'significant' category. Next steps may include an audit of the party's processes, in-depth scrutiny of the party's compliance functions, increased monitoring or correspondence addressing key concerns.

2.23 Our audit staff are unlikely to engage substantively with most of those in the 'moderate' category, although we may undertake increased monitoring or provide additional guidance addressing specific concerns, for example where a party's compliance record has become significantly worse. We will not normally audit those in this category, other than as a result of random sampling.

2.24 We are unlikely to engage with those in the 'low' category, except through random sampling.

2.25 As noted above, when we inform parties and accounting units of their profile each year we will also explain what it means in terms of interaction with our audit function.

Offering advice to those we regulate

2.26 As we have described above, we aim to secure compliance by helping those we regulate to understand the law and get things right, rather than simply by taking enforcement action after things go wrong. To help drive compliance, we may offer advice to those we regulate on our own initiative, where we have information that suggests a political party or other regulated body may need help in complying. For instance, we may do this where:

- a new party appears to be fundraising on a large scale but does not have experience of complying with the rules on donations and loans
- a party has gone through a significant structural change, such as a split, merger or large-scale change of leadership, or those staff with knowledge of the party and election finance rules have left
- a party has made a significant change in its campaigning or fundraising methods, which may affect its volume or sources of funding

2.27 By definition we will not hold information of this kind about every registered party, and so it cannot be used to create formal profiles. We will log and collate relevant information as we receive it, but will not publish it. Our Advice and Guidance Team will refer to the information we hold when considering whether it is appropriate to offer advice on our own initiative. This process is underpinned by our horizon scanning activity which gathers media reports about emerging trends and likely areas on which we may need to target in future. The types of information we will log are set out in Appendix C and can be grouped under three headings:

- public profile
- governance and capacity
- external factors

2.28 Information about **public profile** will include whether the organisation concerned is represented or holds power in an elected body, such as the UK Parliament, Scottish Parliament, National Assembly for Wales, Northern Ireland Assembly, the European Parliament, or a significant regional or local body.

2.29 Information about **governance and capacity** will include any concerns apparent when the organisation first registered with us, and whether the organisation's compliance infrastructure (records, systems and staff) appears adequate to deal with the scale of its fundraising operations and spending. It will also include any change in structure, governance or leadership over time, and any significant change in the organisation's policies, campaigning or fundraising methods which may affect the sources or volume of its funding.

2.30 Information about **external factors** will cover changes in the external environment that may affect the organisation's sources of funding, such as economic difficulties.

2.31 All these types of information will help to give a picture of how risks are changing over time and how specific issues may impact on a party, indicating a need for us to offer advice or guidance on our own initiative.

2.32 Where we offer advice to a party on our own initiative, there is no obligation on the party involved to accept it. We can only compel a party to follow our advice if a breach of the law has occurred and we have issued a compliance notice requiring the party to take steps to ensure that it complies in future.

Monitoring election campaigning activity

2.33 The rules that we regulate include restrictions on spending and donations at elections and referendums. In the run-up to major elections and referendums we carry out a targeted programme of campaign monitoring work, focused mainly on assessing the level and type of campaigning activity. This work has three purposes:

- raising awareness of the rules and the need for compliance
- obtaining information that we may use when reviewing parties' and candidates' spending returns, and
- identifying emerging issues and opportunities for us to offer proactive advice to those we regulate

2.34 We select the constituencies and areas in which to carry out this activity according to a set of criteria which are listed in Appendix D, generally focusing our work on areas where campaign spending is likely to be significant.

2.35 We publish a briefing for those contesting the election when we start to undertake each programme of campaign monitoring, and we report on the outcome of this work in any report on campaign spending for the relevant election.

Appendix A

Financial, Compliance and Operational profile indicators ⁵

Financial data indicators

- reported income*
- net asset / liability as a percentage of reported income*
- material inaccuracies in accounts in the last three years*
- receipt of public funds*

Compliance record indicators

- failure to submit accounts or other statutory returns due in the last three years*
- late submission of statements of accounts due in the last three years*
- late submission of quarterly donation or loan returns in the last three years
- late submission of campaign expenditure returns in the last three years
- late submission of weekly donation or loan returns [*only applicable to a UK general election that precedes audit year*]
- individual donations or loans reported late in the last year*
- individual donations reported incorrectly in the last year*
- other breaches of the financial requirements of the 2000 Act in the last three years, including any sanctions imposed by the Commission and non-payment of fines*
- late submission of annual confirmation of registration details in the last 3 years
- instances of registered details not up to date in the last 3 years

⁵ All indicators apply to political parties. Those criteria indicated with * also apply to accounting units.

Operational scale

Rating	Characteristics
1	<ul style="list-style-type: none"> • Has no accounting units • Holds no elected office • Contested no elections in last five years • Not submitted quarterly returns in last year
2	<ul style="list-style-type: none"> • Has fewer than five accounting units • Holds no elected office above local government level • Contested fewer than three elections in last five years • Not submitted quarterly returns in last year
3	<ul style="list-style-type: none"> • Has accounting units • Holds no elected office above local government level • Contested fewer than four elections in last five years • Submitted quarterly returns in last year <p>or</p> <ul style="list-style-type: none"> • Has an accounting unit with income or expenditure over £25,000 but under £100,000
4	<ul style="list-style-type: none"> • Has between 1 and 100 accounting units • Holds significant elected office above local government level • Contested four or more elections in last five years • Submitted quarterly returns in last year <p>or</p> <ul style="list-style-type: none"> • Has an accounting unit with income or expenditure over £100,000 but under £250,000
5	<ul style="list-style-type: none"> • Has 101+ accounting units • Holds highest available⁶ elected office • Contested more than four elections in last five years • Submitted quarterly returns in last year <p>or</p> <ul style="list-style-type: none"> • Has an accounting unit with income or expenditure over £250,000

⁶ Such as UK Parliament, Scottish Parliament, National Assembly for Wales, Northern Ireland Assembly or the European Parliament.

Appendix B

Profiles and audit outcomes

Operational scale ⁷	Financial data	Compliance record	Likelihood of audit
4-5	A	High	Low
		Medium	Moderate
		Low	Moderate
	B	High	Moderate
		Medium	Moderate
		Low	Significant
	C	High	Moderate
		Medium	Significant
		Low	Significant
3	A	High	Low
		Medium	Low
		Low	Moderate
	B	High	Low
		Medium	Moderate
		Low	Moderate
	C	High	Moderate
		Medium	Moderate
		Low	Significant
1-2	A	High	Low
		Medium	Low
		Low	Low
	B	High	Low
		Medium	Low
		Low	Moderate
	C	High	Low
		Medium	Moderate
		Low	Moderate

⁷ This characteristic only applies to central parties

Appendix C

Information to inform proactive offers of advice and guidance

Public profile – type of information

- party represents or holds power in an elected body (UK Parliament, Scottish Parliament, National Assembly for Wales, Northern Ireland Assembly, European Parliament, regional or local assembly or council)
- party has a significant profile at registration (e.g. with high-profile founders or funders)

Governance and capacity – type of information

- process of registration with the Commission indicates limited capacity to comply with future regulatory requirements
- compliance infrastructure (e.g. records, systems, staff) inadequate to deal with scale of fundraising
- significant structural change (e.g. party schism or merger), sudden change in Parliamentary or organisational leadership, change to governance arrangements
- significant change in policy, campaigning or fundraising methods that may affect sources or volume of funding

External factors – type of information

- changes in the external environment that may affect sources or level of the organisation's funding

Appendix D

Election campaign monitoring – selection criteria

The extent of the monitoring we carry out will depend on the type of election and our view of the associated likelihood and impact of risk. When selecting where to focus our monitoring resources, we consider the following criteria:

- historic data or projections suggesting that the contest will be marginal or particularly hard-fought;
- any evidence of significant funding flowing into organisations campaigning in the relevant area, including locally-based parties and the accounting units of larger parties, either via reported donations or through transfers from other parts of an organization;
- any evidence of significant campaign spending by such organisations, or by national organisations targeting activity in the area;
- any evidence that one or more candidates (or prospective candidates) may have a higher than usual personal profile, for example where two sitting holders of elective office are competing against each other because of a boundary change; and
- an historic record of non-compliance by one or more of the participating organisations.