

**Party Finance Regulation: Israel in  
Comparative Analysis**

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# 1. Introduction

The financing of elections is universally recognized as playing a significant role in guaranteeing equality of political opportunity. Cost is an important factor in determining the list of candidates (Pinto-Duschinsky, 2002: 69; Casas-Zamora, 2005: 39; Smilov and Toplak 2007), Lack of sufficient funds may put at issue the principle of equal political opportunity because the flow of information, which affects voters' decisions, is harmed by the lack of financing. The need to obtain large amounts of funds, however, may result in candidates and officeholders spending too much time raising money, at the expense of their public duties and communicating with constituents, as well as in contributing to public cynicism regarding the political process.<sup>1</sup> While no democratic system can function without money concern over campaign financing has increased in recent years due to rising costs of conducting political campaigns.

Trying to bring some order to political races, ensure the principle of "one person, one vote" and limit the corrupting potential of big money, many countries have opted to various methods of regulating the flow of money in politics. Individual systems of regulation differ greatly among the democracies. Nevertheless two major policy lines can be identified which are the subject of most regulatory efforts. Bans and limits are geared to restrict anonymous, foreign or corporate sources of funds or spending on politics. Disclosure and reporting rules for parties and candidates are aimed at the transparency of political money (Nassmacher, 2003: 10). The first option emphasizes the need to prohibit undue influence on the political process. The second emphasizes the right of the people to know, as well as their ability and determination

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<sup>1</sup> *Campaign Financing of National Elections in Foreign Countries: Comparative Analysis* (1997). Report for Congress, Staff of the Law Library, Washington DC, p. 1.

to judge, all aspects of party behavior, including fund-raising and spending, when asked to cast a vote.

The distinctiveness and comparative relevance of the Israeli system lies in several attributes. First, Israel has a multi-party system in which every party employs a different selection method of its leaders and parliamentary representatives.

Accordingly, the mode of financing the selection of representatives varies from one party to another. Second, a large state funding is given in a package that places the parties under relatively tight and effective enforcement while they run parliamentary campaigns. Coupled with the small size of the country and the free flow of information, Israel is a fertile arena to research the effect of financing various electoral methods in one country under one legal system.

It should be added that the relative effectiveness of enforcing electoral finance regulations at the national arena, stands in contrast to the considerable inefficiency at the municipal level and what used to be a total lack of control or enforcement in intra party selection contests. The latter, intra party races, have become just as important for office seekers as the national ones, if not of even greater importance (Hofnung 2002).

## **2. What is "political finance"?**

What is "political finance"? The narrowest definition is "money for electioneering."

This money may be spent by candidates for public office and also by their political parties or by other individuals or organized groups of supporters. It is used specifically to compete in an election and to pay the costs of complying with the applicable laws governing political finance. Money for electioneering is often known as "campaign finance" (Pinto-Duschinsky and Walecki, 2004: 9).

Since political parties play a crucial role in election campaigns in many countries, and since it is hard to draw a distinct line between campaign expenses of party organizations and their routine activities, party funds may reasonably be considered "political finance," too. For the purposes of this lecture "political finance" will be understood to mean campaign finance and party finance. However, it is important to note that "political finance" actually has even wider meanings.

Other types of "political finance" may include the following:

- Financing of bodies such as party "foundations" and other organizations which, though legally distinct from parties, are allied with them and advance their interests
- The costs of political lobbying;
- Expenses of newspapers and other media that are incurred and paid specifically to promote a political line;
- The costs of litigation in politically relevant cases;
- Third-party or "independent" expenditures.

The fact "political finance" consists not only of campaign and party funding but also of these related types of money poses a problem not merely of definition. It also creates a problem for those attempting to enforce laws designed to control the funding of political parties and candidates for public office.

### **3. Political finance**

#### **A. Paying for Democracy**

Election campaigns, political party organizations, and politically active pressure groups all cost money that must be found somewhere. The frequency with which new

laws concerning campaign and party finance are enacted is testimony to the failure of many existing systems of regulations and subsidies. Hardly a week goes by without a new scandal involving political money surfacing in some part of the globe (Pinto-Duschinky, 2002: 69). These scandals are frequently the signal that existing political finance regulations are not working properly. Either the laws are inadequate or they are not being enforced.

When regulations are enacted to control the campaign costs of political candidates and the finances of political parties, the effect is to have money diverted into related but uncontrolled forms of political activity (Pinto-Duschinky, 2002: 70). For instance, when money spent on policy research is subject to disclosure and to other forms of financial control if it is conducted under the aegis of a party organization but not if it is under the aegis of a party-linked "foundation", the expected result is that a "foundation" will be created as a device to escape the legal controls that pertain to political party.

The problems involved with political finance led many countries to adopt public funding of parties and political organizations. The reasoning beyond public finance was that adequate financial support from unbiased and neutral sources (the state) would free parties and candidates from over dependence on organized or public interests who aspire to get easy and quick access to decision makers in return for their political contributions (Hofnung 1996: 139). Although public funding is not a quick and instant remedy to all political troubles, my experience had taught me that generous public allocations reduce the incentives to circumvent electoral laws. Many politicians, when having at their disposal decent funds to run effective campaign, would opt to obey the law and comply with legal requirements.

One of the strings attached to become eligible for public funding is disclosure. Disclosure means the giving out of information which might otherwise be kept secret. Such information is commonly enforced in compliance with legal regulations of political finance and is intended to reveal the sources of electoral funding.

### **B. Disclosure Requirements**

Disclosure is a necessary condition for any system of public control of political finance. Disclosure is a prerequisite for the enforcement of expenditure ceilings and contribution limits, and also for the allocation of public subsidies. Development experts as well as democracy practitioners are now realizing that politics is as important to successful development as economics. Political accountability is defined in part by "transparency in party financing" as well as "asset disclosure" (Ward, 2002). Disclosure requirements are part of a broad set of regulations governing election law in general, but they do have significant meaning when political finance is concerned. There are several reasons why countries can benefit by increasing emphasis on disclosure and transparency:

Illicit or illegal money can too easily find its way into the governance equation and cast a shadow of suspicion and mistrust on all players involved in the electoral process (Hofnung, 2004: 77). Without disclosure, money can come from anywhere in the world, and in any amounts. Without disclosure there is no way to follow the track of financial transactions in the electoral process. The ability to follow the money, or construct "audit trail" is the first barrier against system irregularities. Disclosure is also essential for enforcing limits, bans and prohibitions.

To be effective disclosure needs enforcement agency, administrative capability, sufficient budget and educated manpower. Political parties or individual candidates may be tempted to avoid transparency or report a distorted picture of their financial activity to for a number of reasons. One reason for lack of reporting or misreporting is receipt of larger donations in cash. In several countries, especially new democracies, donors may be excessively concerned with preserving their privacy and require no reporting as a precondition for a contribution. In short, while disclosure is an important element of a fair electoral process, its significance is reduced in the absence of effective audit mechanisms.

#### **4.National Elections and Internal Party Contests: Risks and Opportunities**

The introduction of state subsidies to political parties was aimed at reducing corruption and ensuring transparency of parties' financial transactions. Fifty years after the introduction of public funding, political corruption is still prevalent in modern democracies. Although state subsidies are granted to political parties, intra party races between candidates remain under financed and only loosely regulated. While in majoritarian systems, internal party races are seen as part of the electoral process, not much is known about the finance of such races in systems of proportional representation. Revelations of corrupt practices accompany most electoral campaigns in many countries. Considerable amount of such accusations relate to candidates activities while trying to secure a safe front position in their own party's list of candidates. I will argue that the lack of oversight, regulation and proper funding of internal party races forces candidates to seek financial support regardless of possible

future implications. The Israeli experience can reflect the dangers of insufficient regulation and enforcement of internal party competition.

## **5. Israel**

### **A. The electoral System**

*Parliamentary general elections:* the State of Israel utilizes a national proportional representation voting system, i.e. each list receives a relatively proportional number of seats in the Knesset – the House of Representatives – according to the number of votes it received. The representative principle is followed in Israel to an extreme manner, constrained only by the requirement to pass the qualifying threshold (raised in 2004 from 1.5% to 2%). To determine the number of votes constituting a seat, the overall count of valid votes given to lists that passed the qualifying threshold is divided by 120; Excess votes (votes received by a list passing the qualifying threshold but not sufficient for a whole seat) are distributed to the list with the average number of votes per seat. Any two lists may reach an agreement between them before the elections, concerning the distribution of excess votes. In case of such agreement, excess votes of such two parties are seen as one block assigned to the party (among the two) with the larger number of excess votes.

Between the years 1996 and 2001 Israel went through an experimental phase of utilizing a Direct Vote for Prime Minister System (devised as a seemingly promising solution to the continual political deadlock between *Labor* and *Likud* parties). According to this new-introduced system, voters were asked to cast split ticket, electing directly the Prime Minister *and* then voting for political party (not necessarily relating to the same list), After experimenting with that system in three



electoral campaigns in five years (1996, 1999, 2001), this system was abolished in favor of the previous single-ballot one.

## **B. Internal Party Selection Processes**

During the first four decades of Israel's existence, electoral lists were drawn up in sealed rooms by party leaders who chose and placed (rather than elected) candidates for the entire list that would be presented before the public on election day. That custom has been rapidly changed during the 1980s, and the introduction of mass primaries by the Labor Party before the 1992 served as a signal that legal regulation is needed.

The Parties Law of 1993 left the state out of supervising internal party races and entrusted the parties themselves with the monitoring and enforcement of reporting requirements. As we shall see, this regime has proved to be a total failure of enforcement. Despite ample newspaper reports and numerous complaints by losing candidates in several parties of their opponents' heavy spending and campaign violations, not a single candidate in any party has ever been found guilty by an internal auditing body of committing serious campaign violations.<sup>2</sup>

## **C. Political Finance**

Political finance enforcement in Israel is intended at striking a balance between conflicting and competing goals. It tries to allow for fair competition, accountability,

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<sup>2</sup> For example, After the Likud (Israel's governing party) internal elections of December 2002, four Likud ministers and four Likud MKs failed to report donations they received for their internal campaign, in violation of the party by-laws. Even though 78 of the contestants never filed a report, no penalties were imposed. *Ha'aretz*, December 15, 2002.

honest disclosure, limiting expenditures, and controlling donations. Its success in achieving these goals, as we shall see, is limited and varies in different campaigns and political settings.

Public funding of political parties was introduced in Israel on an experimental basis in 1969 and then on a permanent basis in 1973, initially enacted to take place only at national elections. Local elections were financed by the national parties out of their total funding. No permanent law regulating local elections existed until 1993.

Historically speaking, Israel has tried all three methods of funding: private, public and mixed. Initially, Israel opted for a **private** system, and until 1969 the state was involved neither in contributing to nor in supervising parties' financial affairs. Parties were left to their own devices in funding their routine activity and electoral campaigns. Then, due to the unprecedented high cost of the 1965 general elections, Knesset factions agreed to experiment with public funding of electoral campaigns for the general elections of 1969. This experiment was the first move towards the adoption of a **mixed** system of party funding, formally adopted in 1973 (Party Finance Law 1973). This system granted parties public funding according to their proportional Knesset representation, and permitted them to solicit private donations as well. In return for funding, both election campaigns and routine party activities, the parties were subject to a loose regime of disclosure, prohibition of contributions from corporations, and expenditure ceilings. Parties were still able to receive unlimited donations from private persons including non-Israeli citizens.

When the Supreme Court ruled as illegal an increase in funding awarded in 1991 to political parties, politicians opted for a reform rather having to pay back the money already spent. The reform in public finance that passed in March 1994 (the Finance of Parties Law) was based on a political deal which granted the parties

considerable additional money to cover their deficits, in exchange for much stricter demands of transparency, accountability and public financial reports. Each party is entitled (adjusted to November 2008) to receive funding unit of 720,000 NIS (roughly \$200,000) a year for each Knesset member on the party's list (with additional funding unit to each party regardless of its size) for routine party activities. An additional grant of NIS 1,200,000 (roughly \$330,000) in an election year is awarded to a for each Knesset member for covering campaign expenses.<sup>3</sup> The new law also allows small parties to spend more than their relative size of the electorate (in relation to big parties) during electoral campaigns, assuming they collect additional money from lawful sources, which contributes to equality in opportunities. The authority to make amendments in public financing was transferred from the Knesset to a public committee. The law sets low ceiling of legal contributions to parties, 2000 NIS (\$580) in election year (\$290 in non-election year). Contributions cannot be accepted from corporations or associations but only from Israeli citizens. Violations of the law may result in prison terms.<sup>4</sup> As a result of the 1994 reform, Israeli parties now rely almost entirely on **public funding**, with private contributions accounting for only 1-2% of reported campaign expenses.<sup>5</sup>

Although formally the mixed system of party financing remained in place, for all practical purposes, parties have ceased their fund-raising activities. This does not

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<sup>3</sup> This simple equation is applicable to new parties or parties who maintained their number of seats in the outgoing Knesset. When changes in representation occur, parties are awarded number of funding units that represents the half of their accumulated number of seats in the last two electoral campaigns + one basic unit. Thus for example, if a party received 2 seats in election A and 4 in election B, it is then awarded 3 units that represent the average number of seats in those two campaigns (three) + one basic unit= 4

(2+4=6; 6:2=3; 3+1=4).

<sup>4</sup> It took thirteen years before a person was sentenced to jail term for violations related to financing internal party election. Nevertheless it is commonly believed that many violations had occurred in the past.

<sup>5</sup> Testimonies given before the *Public Commission on funding of Political Activity*, 2000. The overall contribution figures are not disclosed in the State Comptroller's report.

mean, however, that individual contributions are no longer accepted. Rather, this form of fund-raising has found a new focus – individual candidates competing in internal party races for parliamentary representation and party leadership. While national parties had long received generous public funding for routine activities and electoral campaigns, individual internal party contests had never been publicly funded and were only loosely regulated. Consequently, the funding of individual contests came to depend on the source that the national party system has gradually eliminated since 1969, namely private funding.

In sum, the Israeli political finance system is built on generous, year round funding, for national parties and substantial increases during electoral period. Local political activity is funded by the state only during elections, while internal selections contests are exclusively privately funded.

#### **D. Enforcement of Finance Regulations on National Parties**

Israeli parties are required to manage two different accounting systems, one for national elections and one for routine party funding (between elections). Money given to routine activities can be transferred to national elections, but it stands against the expenditure ceiling that the parties are required to maintain. Overspending above the legal ceiling may result in heavy fines. For that reason parties try to define borderline activities as routine and avoid classification of those expenses as electoral.

Funding and enforcement of political activity is carried out by the state only with relation to national parties (or local lists in the case of municipal elections). In other words, the legal bodies who have a standing before state authorities are registered parties by their representatives. Individuals are mentioned only as possible

law offenders (subject to legal sanctions) but not as possible beneficiaries of state funding.

Parties are eligible to receive generous funding, but they are also subject to strict scrutiny by the audit of a special unit of the State Comptroller. Once accepting advances from the state (60% of the basic unit for each Knesset member on the list), they have to report for expenditure and for every donation they receive. The Comptroller takes an active roll in looking into the financial dealings of the parties. The staff of the Comptroller gathers its own information and conduct independent inquiries. Failure to provide sufficient explanations can lead to negative reports and severe fines. At the end of the electoral campaign, parties are required to submit financial reports. Again, failure to submit the report by the time due, or according to the Comptroller specifications may result in heavy fines. For example, following the elections of 1999, the comptroller slapped the Labor Party with an unprecedented large fine of NIS 13,784,000 (\$2.8 million) for its violations of the party financing regulations.<sup>6</sup>

### **E. Individual Candidates in Internal Party Races**

The Israeli electoral system allows for parties only to compete in national elections. Even at municipal elections where direct election of mayors is employed, individuals can run only when they appear on electoral lists. Candidates are recognized and may run their own campaigns only in intra-party races intended to select between contestants who compete for securing front place on the party's electoral list. The Parties Law sets expenditure ceilings for internal elections that are adjusted yearly. In

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<sup>6</sup> It is rare that parties who acquire Knesset's representation do not submit reports on time, as they risk fines by the State Comptroller. It happens quite often that parties that fail to secure representation in the Knesset do not submit reports. The law does not call for fines in such a case.

November 2008, those ceilings stand in internal campaigns at NIS 405,000 per candidate (\$116,000) for 100,000 eligible voters and (\$.58 for each additional eligible voter) in a Knesset's primaries, and four times as much in primaries for party leadership and party candidate for prime minister. In past elections, many candidates have treated those ceilings as a mere recommendation rather than a law intended to ensure fair competition.<sup>7</sup>

Individual candidates in intra-party contests are required by law to submit reports of their financial dealings. Until recently, enforcement of this requirement was not carried out by a state agency, as is the case with national lists. Until 2006, the Parties Law of 1993 entrusted the parties themselves with the tasks of monitoring and enforcement of reporting requirements. This law has left a major loophole that makes the reporting requirements no more than a procedural anecdote. Candidates are only required to report activity within the nine months preceding the primaries,<sup>8</sup> while contributions and expenditures prior to that date are exempt from disclosure. Moreover, given the fact that internal candidate selection generally takes place less than two months before the general elections, the desire to avoid public scandal prevents strict enforcement and exposure of illegal activities.

In spite of the numerous tactics employed in 1996, 1999 and 2003 by more than six hundreds of candidates, the auditing bodies of the four parties that held primaries, did not find even a single candidate responsible for a violation which may result in anything more serious than a small fine.

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<sup>7</sup> The current Prime Minister of Israel, Ariel Sharon, has barely escaped criminal indictment related to accepting corporate donations and overspending the internal ceiling in his bid to become the Likud Party leader in 1999. State Comptroller (2001), *Report on the 2001 Special Elections*, Jerusalem, pp. 22-32.

<sup>8</sup> The nine-month requirement takes full effect only if elections are held on time. In seven of the last eight general campaigns, elections were called early, before the Knesset had completed its four-year term.

In short, while the transition to primaries as the method of selecting party candidates appeared on the surface to be more democratic than before, and seemed to have diffused some of the political leverage of a handful of power brokers in internal party selection procedures, it made candidates much more dependent than before on adequate financial backing.<sup>9</sup> The practices revealed in primaries campaigns have been kept alive even when a party switched to other selection methods.<sup>10</sup> If the party itself does not establish a system for funneling part of the public funding to finance intra-party competition, candidates are totally dependent on either personal wealth or contributions, or both. Since there is a legal loophole, which allows unlimited contributions to be raised until nine months before the start of the campaign, the temptation to engage in corrupt promises and practices in return for financial backing grows considerably. More corruption in such an electoral environment is imminent.

#### **F. Lessons of the Israeli Experiment**

Enforcement is fairly tight and effective when national parties and parliamentary factions are concerned. In return for a generous funding, parliamentary factions are subject to year round monitoring by the office of the State Comptroller. While not pretending to claim that the system works without infractions or abuses, compared to other political systems and even other electoral environments in Israel itself, enforcement is effective in the sense that parties are deterred from knowingly committing offences. In most cases parties prefer to comply with the guidelines published by the State comptroller rather than paying fines for illegal violations.

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<sup>9</sup> One party, Meretz, gave non incumbent candidates in kind support, to run their internal campaign in 1996, 1999, 2003 and 2006.

<sup>10</sup> For the methods used in the Likud internal campaign see, Hofnung (2004).

The effectiveness of the national system, however, is not apparent in other electoral settings: elections for city mayors and local councils are marred by reports on cash payments, illegal contributions, expenditure violations and so on; Enforcement at intra-party internal selection campaigns is for all purposes nonexistent. Without state surveillance, the parties are left to carry their own inspection. This regime has proved to be corrupt and ineffective. Many candidates who rise to national prominence do so after exhibiting disregard to the provisions of the law and after raising illegal contributions, using public resources for their own campaign and spending as much as they can afford, for the sake of securing a front position on the party's list.

The moral of the Israeli case is that attempts to regulate the selected areas of campaign finance without taking into consideration the entire picture of the electoral process, may severely affect the entire political culture. The weakness of enforcement at local government and its absence at party internal races, resulted in discredibility and widespread contempt for the political process and the parliamentary system.

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