

**Review of the Australian Electoral Commission's
Disclosure Compliance Function under Part XX of
the *Commonwealth Electoral Act 1918***

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Forward

In early August 2012, the Electoral Commissioner called for a joint independent review of the Australian Electoral Commission's (the Commission) disclosure compliance function. The review was to be conducted by Ron McLeod AM, a former Commonwealth Ombudsman, as the Principal Reviewer. Mr McLeod was to be assisted by PricewaterhouseCoopers (PwC), a financial management consulting company.

Mr McLeod's role was to consider the manner in which the Australian Electoral Commission (the Commission) had managed the compliance aspects of the financial disclosure provisions of the *Commonwealth Electoral Act 1918* (Electoral Act) assisted by the conduct of a performance audit of the function by PwC.

Due to the overlap between the terms of reference for each exercise (included below) it was necessary and mutually agreed that the two reviews would proceed independent of the other but within an agreed framework of close cooperation and mutual sharing of information. The participants met on a weekly basis to discuss directions, progress and each other's focus of attention for the coming week.

Informal contact was maintained between meetings on a needs basis.

Each party attended formal presentations by Commission staff and a workshop open to all staff of the areas covered by the review. Detailed discussions between the reviewers and particular staff members were generally on an individual basis as the interests of both reviews were not identical.

Mr McLeod's review concentrated on the higher level or broader aspects fundamental to the effective administration of the Commission's legislative responsibilities. It sought to provide overarching guidance in relation to the way in which the disclosure compliance function could better operate to achieve improved outcomes. The PwC review was more technical in character and was focussed on a range of detailed work level issues.

By sharing information the two reviews proceeded in tandem in the knowledge of the considerations and outcomes that emerged from each other's reviews. In this way both received the benefit of the other's endeavours and each was able to proceed with the confidence that they were following similar paths albeit with different, though related, agendas.

In the ultimate the conclusions were in a similar direction and provided mutual reinforcement. No glaring discrepancies emerged that might otherwise have presented complications for the Commission.

The two reports can be read independently and the individual authors accept responsibility for their own reports. However, for the convenience of the reader the two reports are presented together and can be read as a single volume.

Readers will note some repetition between the parts that comprise the full report. This is due to the dual nature of the authorship and assists in enhancing the readability of the Parts that cover aspects of the report proper at a more detailed level.

Terms of reference for the two reviews are set out below.

The AEC has engaged Mr Ron McLeod AM to:

- *Ascertain the nature and type of work required to fulfil the AEC's statutory responsibilities in relation to monitoring and enforcing compliance by political parties, associated entities, donors and other third parties with the disclosure provisions in Part XX of the Electoral Act;*
- *Taking into account the nature of the statutory responsibilities and the nature of the work required to fulfil these, provide advice to assist in determining the most effective and efficient way in which the AEC can monitor and enforce disclosure compliance under the Electoral Act, including:*
 - *A consideration of the extent to which the AEC needs to further develop educative and informative measures to encourage voluntary compliance as opposed to ex-post-facto enforcement; and*
 - *A consideration of whether the AEC's current organisational structure most appropriately accommodates the functions of administering election funding, financial disclosure and party registration.*

PricewaterhouseCoopers will provide a range of assistance in relation to Mr McLeod's review, including the conduct of a performance audit of the AEC's compliance review function, which will:

- *In light of the scope and nature of the statutory responsibility and the type of work deemed necessary to fulfil it, involve an assessment of the efficiency and effectiveness of the AEC's conduct of compliance reviews, including:*
 - *A review and evaluation of internal policies and guidance material on Part XX of the Electoral Act regarding the compliance review function, such as:*
 - *Processes and procedures, including risk assessment frameworks which are used to guide decisions regarding work programs;*
 - *Audit methodologies, including the depth of testing performed; and*
 - *Past internal audit reports and recommendations.*
 - *An examination of the appropriateness of the scope and focus of compliance reviews; and*

- *An examination of whether the current workforce model in relation to disclosure compliance is appropriate to achieve efficient and effective compliance review coverage, and how it can be improved.*

The performance audit will be used to inform the broader review being conducted by Mr McLeod.

Each of us acknowledge the support we received from Commission staff and their willingness to assist. Special mention is made of the contribution of Ms Christine Wickremasinghe whose knowledge and management capacity made a major contribution to the review. She provided excellent support and advice to Mr McLeod and was an outstanding bridge between the two review groups and with Commission staff generally.

R N McLeod AM
Principal Reviewer

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Executive summary

Under the Electoral Act, the Commission is responsible for the administration of arrangements that involve substantial public funding of political parties and individual candidates. This responsibility is coupled with legal obligations imposed on political parties, associated entities, political donors and third parties incurring political expenditure (as well as candidates and Senate groups following an election) to declare for public disclosure, certain details in relation to monies received from all other sources on an annual basis. The Commissioner has enforcement powers designed to support compliance with the disclosure obligations by all involved.

In August 2012 the Electoral Commissioner called for an independent review of the Commission's compliance activities following some criticism in the Parliament regarding the compliance powers under Part XX, which led him to reflect on the importance of the perception of independence of the Commission.

Mr Ron McLeod AM, a former Commonwealth Ombudsman assisted by consultants from PricewaterhouseCoopers (PwC) was appointed to undertake the review.

While concentrating on the Commission's compliance function the review also examined a closely related work area responsible for processing the funding disclosure returns that form the basis of the detailed information that is published by the Commission.

The review acknowledges the efforts of the Commission's compliance area to date to improve its work practices. However, the review concluded that while the Commission's administration of the compliance function has been gradually improving over time, the current review activities have been too limited in their scope. In addition, a better developed governance and management structure needed to be put into place.

The function has been associated with a number of different branches within the Commission since its inception, and its role has not been fully integrated into the Commission's governance structure as well as it ought to have been. As a result of a lack of active involvement at the management level, there have been significant failures to fully follow through with a number of endorsed recommendations that had come out of a series of external performance audits conducted between 2002 and 2007.¹ Accordingly, there is still considerable scope for improvement, particularly in terms of a more strategic direction of its efforts.

The review concluded that the Commission needs to become more proactive in the way that it seeks to administer and enforce compliance with the financial disclosure scheme. It needs to broaden the coverage of its compliance review program by introducing a program of random testing to complement the current approach of reviewing every political party (and its associated entities) during a three year electoral cycle. This more focused approach in which

¹ The process surrounding follow-up of implementation of recommendations resulting from audits of various business areas is managed by the Commission's internal audit committee, known as the Business Assurance Committee.

targets for reviews under section 316(2A) of the Electoral Act are selected on the basis of a sound and comprehensive risk assessment framework that takes into account a wide range of factors, will provide greater confidence to the public and the Parliament that compliance with the scheme is being effectively enforced by the Commission.

This revised approach to the enforcement of the scheme must also be supported by an upgraded and more sustained approach to educating and informing clients about the nature of their obligations and how they can meet them.

This change in direction for the administration of the AEC's disclosure and compliance function requires a greater degree of integration and collaboration between the sections that comprise the Funding and Disclosure (FAD) group than has been the case to date. The move to a more proactive approach needs to be applied throughout all areas of FAD responsibility in order to be effective.

A new business model for the area needs to be developed that achieves these ends.

Increased resources to support acquisition of additional personnel with specialist analytical skills not available currently within the Commission and the enhancement and development of improved information technology facilities to support the function properly are key facilitators in the implementation of a new business model for the administration of this function.

A series of recommendations included in the report address the following:

- Strengthening the corporate governance framework
- Clearer definition of strategic mission
- Strengthened leadership by provision of a full time branch head position to manage the FAD sections free of other unrelated responsibilities
- Acquisition of stronger investigative skills
- Better application of risk management techniques
- More emphasis on intelligence gathering and analysis
- Introduction of random 'spot check' based reviews to complement more programmed activity
- Stronger integration of the compliance, party registration and disclosure sections
- Development of enhanced integrated information technology support.

All of these elements need to be addressed if the compliance function is to be invigorated in the manner proposed. An improvement in effectiveness will inevitably be gradual as a number of the changes recommended will take time and resources to be properly developed and implemented.

The approaches recommended are designed to strengthen the Commission's capacity to administer the political funding and public disclosure provisions of the Electoral Act. They

will also enable the Commission to be more confident that it is fully meeting its legislative responsibilities in an appropriate fashion.

Part 1: Directions for Change

Introduction

- 1.1. This report deals with a review of the Australian Electoral Commission's (the Commission) compliance responsibilities in relation to the political funding and disclosure provisions of the *Commonwealth Electoral Act 1918* (Electoral Act).
- 1.2. The review was established by the Electoral Commissioner after he was given 'cause to reflect' following commentary from the Joint Standing Committee on Electoral Matters (JSCEM) on the perception of the independence of the Commission in administering the disclosure compliance function under the Electoral Act.² The discussions by JSCEM highlighted the sensitivity of issues associated with the accountability of the political parties and individual members of the Parliament in respect of their receipt of monies from public and outside sources to support electioneering, and of the Commission in administering the relevant provisions contained in the Electoral Act.³

Disclosure of the sources of political funding

- 1.3. Knowledge of the extent of external funding provided or gifted to political parties and individual candidates for use in their electioneering efforts is a vital element in informing voters of the nature and extent to which funding from private sources exists. Public disclosure is a protection against political corruption and it creates a more informed and aware electorate by revealing information about the types of interests, organisations and people who support particular parties and candidates through donations and gifts.⁴
- 1.4. The obligation on political parties and individual candidates to disclose information about election campaign expenditure and its sources was introduced in 1983 in conjunction with the introduction of public funding of political parties and candidates. Public funding was initially based on the reimbursement of expenditure incurred in election campaigning but was replaced in 1995 by a direct entitlement scheme related to votes obtained by candidates, with a candidate needing to achieve at least 4% of the first preference vote to qualify for election funding.⁵
- 1.5. Regulation of the receipt and public disclosure of campaign funding and expenditure were seen as complementary, and a natural corollary to the introduction of public funding. Both elements taken together have added to the quality and sense of fairness of the political contests that characterise Australia's system of representative government.⁶

² See generally *Committee Hansard* 6 July 2012 and *Committee Hansard* 16 July 2012.

³ See generally *Estimates Hansard* 16 October 2012, pp. 92 – 105 for discussion by the Electoral Commissioner at Senate Estimates regarding the circumstances giving rise to the review and broader issues.

⁴ The media and academia, as well as others that write on the issues, play a role here as well, in bringing to public attention particular aspects of the information made public by the Commission under Part XX of the Electoral Act.

⁵ See generally Division 3 of the Electoral Act.

⁶ Some of the smaller political parties may not necessarily support this view.

- 1.6. The enabling legislation gave to the Commission the responsibility of administering the scheme. The Commission in 1983 was provided with enforcement powers that included the capacity to undertake reviews and inquiries designed to maintain compliance with the disclosure provisions. In addition a range of penalties were specified aimed at discouraging non-compliance.
- 1.7. The choice of the Commission as the body to administer the new election funding and disclosure scheme built on its long established reputation as an apolitical independent agency with long experience in managing the electoral process. Selection of the Commission by the Parliament to pick up this additional responsibility seems an obvious and logical one. Some other jurisdictions with similar schemes, have established bodies separate to their electoral organisations to oversight funding and public declaration arrangements. This option has been canvassed in Australia at the Commonwealth level but has not been favoured.⁷

History of compliance powers

- 1.8. Prior to 1991 the Electoral Act enabled the Commission to conduct investigations where, as a precondition, there were 'reasonable grounds' to believe that the provisions concerning funding and financial disclosure had or might have been contravened (section 316(3)).
- 1.9. A new power, section 316(2A), was added in 1991. It was similar in purpose and was accompanied by the same compulsive powers that were contained in the existing investigative power in section 316(3), but containing the important difference that it could be invoked without a prior 'reasonable grounds' test needing to be met. The new provision was also more restrictive than the existing investigative power in the limited sense that it did not extend to the use of compulsive powers to require the production of specified material and attendance of persons from sources not bound by the disclosure provisions, such as private persons or banks.
- 1.10. The genesis of the new provision was a legal advising from the Attorney-General's Department in the 1980's which to the surprise of the Commission at the time, indicated that it could not require the production of records relating to gifts that did not need to be included in a disclosure return.
- 1.11. At the Joint Select Committee on Electoral Reform inquiry after the 1984 election, the Commission advised of its inability to undertake random compliance audits. It indicated that section 316 had always been intended to cover the conduct of random compliance audits.

⁷ See for example Joint Standing Committee on Electoral Matters, *Advisory report on the Commonwealth Electoral Amendment (Political Donations and Other Measures) Bill 2008*, October 2008, Commonwealth Parliament of Australia, p. 76 and Joint Standing Committee on Electoral Matters, *Report on the funding of political parties and election campaigns*, November 2011, Commonwealth Parliament of Australia, p. 209.

- 1.12. The Commission believed its ability to administer and enforce the disclosure provisions of the Electoral Act was severely limited by being unable to undertake such reviews, however, the Joint Committee at the time was not persuaded to recommend any change.
- 1.13. The issue was revisited by the Joint Standing Committee on Electoral Matters (JSCEM) following the 1987 election. At hearings the then Electoral Commissioner indicated that if the Committee: *'...believed that a system of disclosure is an integral part of a contemporary democratic system, then [the Commission] believe that it should go further than it does at present...'*⁸
- 1.14. The Electoral Commissioner added that if the Commission had the power to conduct spot audits it would be able to say with a clearer conscience and more confidence that: *'Everything appears to be satisfactory and compliance with the Act appears to be satisfactory'*.⁹
- 1.15. The Committee recommended that the Act be amended to include *'the power to conduct spot checks of the electoral activities of the registered political parties'*¹⁰ without first having to establish that there were prior 'reasonable grounds' to do so. This was against the background of debate about concerns by some members of the lack of knowledge of what some parties were not declaring. The JSCEM report noted that: *'...the committee believes there is an alarming lack of information on sources of election funding of parties in federal elections and is of the view that brave steps must be taken to remedy this situation.'*¹¹
- 1.16. This provision has formed the basis for the Commission to develop and conduct the so called 'compliance reviews' that have been undertaken continually since then.

⁸ Joint Standing Committee on Electoral Matters, *Who pays the piper calls the tune – minimising the risks of funding political campaigns*, June 1989, Commonwealth Parliament of Australia, p. 75.

⁹ Joint Standing Committee on Electoral Matters, *Who pays the piper calls the tune – minimising the risks of funding political campaigns*, June 1989, Commonwealth Parliament of Australia, p. 75.

¹⁰ Joint Standing Committee on Electoral Matters, *Who pays the piper calls the tune – minimising the risks of funding political campaigns*, June 1989, Commonwealth Parliament of Australia, p. 76.

¹¹ Joint Standing Committee on Electoral Matters, *Who pays the piper calls the tune – minimising the risks of funding political campaigns*, June 1989, Commonwealth Parliament of Australia, p. 76.

Penalties – effectiveness as deterrents

1.17. The Electoral Act contains a range of penalties.¹² In summary they cover:

- Furnishes a return containing false, or misleading material

Agent of a political party	Up to \$10,000
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A person	Up to \$5000
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- Failure to lodge a return within the time allowed

Political party or branch	\$5000
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Others	\$1000
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If convicted and there is a continued failure to lodge a return, fresh convictions can be sought; the maximum penalty for each further conviction being a fine not exceeding \$100 per day.

1.18. As with most penalty regimes the scale of penalties applied under the Electoral Act was initially graded to reflect the degree of seriousness of the various offences. Penalties serve two purposes; they punish the wrong doers and also act as a deterrent to others.

1.19. It is unfortunate that the penalties have basically remained unaltered since the legislation on public funding and public disclosure of election funding was first introduced in 1983, despite a number of efforts on the part of the Commission, at times with support from the Joint Parliamentary Committee, to have them updated.¹³

1.20. Accordingly, the deterrent effect of the current low level of the penalties in discouraging non-disclosure is arguably negligible. The likelihood that public exposure would be detrimental to the reputation of the people or organisations concerned is of stronger value as a disincentive to offend.

1.21. Governments and the Parliamentary Electoral Committee historically seem to have been less than enthusiastic in supporting the setting of high penalties in relation to electoral funding and disclosure for a deterrent effect.

¹² See section 315 of the Electoral Act.

¹³ See for example Recommendations 1 and 7 in Joint Standing Committee on Electoral Matters, *Review of the Australian Electoral Commission's analysis of the Fair Work Australia report on the Health Services Union*, September 2012, Commonwealth Parliament of Australia, pp. xx-xxi, and Recommendations 26 and 27 in Joint Standing Committee on Electoral Matters, *Report on the funding of political parties and election campaigns*, November 2011, Commonwealth Parliament of Australia, p. xxxvii.

- 1.22. Currently there is a bill (the Commonwealth Electoral Amendment (Political Donations and Other Measures) Bill 2010) that in November 2010 passed through the House of Representatives and is awaiting listing for debate in the Senate.¹⁴ It includes amendments that if passed will lift substantially the penalties for breaches of the disclosure provisions.
- 1.23. Against this background it remains problematic when the penalties will be updated. In the meantime their deterrent value continues to decline.
- 1.24. Substantial funds are donated to political parties. The most recent returns, in a non-election year when donations are usually lower, revealed that 353 donors completed returns showing donations to political parties above the minimum threshold for disclosure (\$11 500 for the 2010-2011 financial year) that totalled \$28 758 942.¹⁵
- 1.25. With considerable sums of the magnitude illustrated above being involved, it is reasonable to believe that compliance is not complete, particularly when the punitive value of the penalties is so low. This situation adds weight to the need for the Commission to increase the reliance it places on its compliance program by taking steps to make it more effective in the interests of encouraging full disclosure.
- 1.26. Despite the knowledge that political campaigning is expensive and increasingly so and the importance that this factor has had in shaping the content and form of important parts of the Electoral Act, the availability of reliable statistics appears to be declining.¹⁶
- 1.27. Electoral expenditure of the ALP and the Liberal party was able to be compiled by the Commission for federal elections between 1984 and 1996 (except for 1993) from electoral expenditure returns. However, in 1993 and for elections since the one held in 1996, due to changes in the Electoral Act relating to the nature of the financial expenditure required to be disclosed, the Commission has been unable to continue the series.¹⁷

¹⁴ This bill is in substantially the same form as the Commonwealth Electoral Amendment (Political Donations and Other Measures) Bill 2008, which was again introduced in 2009 before the 2010 iteration following the commencement of the 43rd Parliament. The 2008 bill was reviewed by the Joint Standing Committee on Electoral Matters in October 2008, with the *Advisory report on the Commonwealth Electoral Amendment (Political Donations and Other Measures) Bill 2008*, October 2008, Commonwealth Parliament of Australia available at http://www.aph.gov.au/Parliamentary_Business/Committees/House_of_Representatives_Committees?url=em/taxlawbill_2/report.htm. The Committee at the time noted that the real value of a number of financial penalties had declined to a level that was 40% less in real value from when they had been set in 1983.

¹⁵ These figures were obtained using export features available on the Commission's financial disclosure website, accessible from <http://periodicdisclosures.aec.gov.au/Default.aspx> as at 9 October 2012. The disclosure threshold for the 2010-2011 financial year is also listed on this page.

¹⁶ See Joint Standing Committee on Electoral Matters, *Report on the Funding of Political Parties and Election Campaigns*, November 2011, Commonwealth Parliament of Australia, pp. 9-10. The Committee comments on the 'rising costs of election campaigning' citing concerns expressed to it by interested parties and groups. In the absence of statistics or 'hard evidence' of the magnitude of the rises, future policy will increasingly be based on anecdotal observations.

¹⁷ The figures on electoral expenditure by political parties are not available for the 1993 federal election because in 1991, the requirement for political parties to lodge election disclosure returns of donations received or electoral expenditure was replaced by the introduction of an annual disclosure obligation. The form of the disclosure obligation was settled following a High Court challenge, by the insertion of a new Division 5A into the Electoral Act in 1992. In 1995 the requirement for political parties to lodge disclosure returns of electoral expenditure following a federal election was reintroduced (hence the availability of figures for the 1996 election), but was again removed in 1998.

- 1.28. Independent research into the amounts of money that are in play in the political arena warrants more attention, perhaps through a referral to the Electoral Commissioner's Advisory Body on Electoral Research (CABER). The information obtained from such a project would be of importance to the Commission's ability to give informed advice to the government in relation to future proposals for legislative reform in the area.

Compliance rationale and current approach

- 1.29. The Commission's public website describes the rationale of the compliance reviews in the following terms:

The [Australian Electoral Commission] undertakes compliance reviews of the annual disclosure returns of federally registered political parties and their state branches and associated entities. The objective of compliance is to assess whether the return as lodged is a complete and accurate record as required by the disclosure provisions contained in Part XX of the Commonwealth Electoral Act 1918 (the Act). Compliance reviews are routine in nature, not being initiated by suggestion of any breach of disclosure obligations, and in general terms can be seen as being similar to financial audits.

Compliance reviews are undertaken over a three year cycle in the course of which every political party can expect to have at least one of its disclosure returns reviewed. It is the [Australian Electoral Commission]'s usual practice to also review the returns for the same year of the associated entities of a party being reviewed.¹⁸

- 1.30. The compliance function is performed by a small group of staff that numbers seven established positions, comprising a Director at EL 2 level heading up three two person teams of an EL 1 assisted by an APS5/6.
- 1.31. The available time for the individual compliance reviews is affected by a range of staff overheads, leave, training, study, general administration and other matters. The available time is then allocated to the program of compliance reviews based on a three year cycle.
- 1.32. Approximately 60-70 separate reviews are scheduled annually. The time allocated for the reviews varies according to the nature of the various entities, their past history and the significance of their roles from a funding perspective. An average time for reviews of political parties is about 120 hours though the smaller ones can take less time while the larger political parties can take considerably longer.

¹⁸ Accessed from Australian Electoral Commission, 'Compliance Reviews', http://www.aec.gov.au/Parties_and_Representatives/compliance/compliance-reviews.htm on 21 September 2012.

- 1.33. Ten per cent of available time is reserved for special investigations that have numbered six in the last three years and where this time is unused, it is allocated back to the standard compliance program.
- 1.34. Compliance reviews are described as routine in nature and more benign in character than ‘investigations’. Generally, each political party is sought to be reviewed once during an electoral cycle and when a party is reviewed, its associated entities are also included in the review. The reviews essentially involve using party and associated entity financial records (such as the general ledger, bank statements and financial statements) to construct a disclosure return that includes all the correct information. Returns submitted by donors to political parties are also examined for comparative purposes. In addition, the major political parties provide to the Commission some other in-confidence financial information in response to the issuing of a section 316(2A) notice, which is also used to assist in the conduct of the compliance checks.
- 1.35. Compliance reviews rarely lead to prosecutions. The AEC has had difficulty in convincing the Director of Public Prosecutions that cases involving failures to meet the disclosure obligations should proceed to prosecution. They have generally been judged to be of insufficient significance to be pursued given the sums involved and the low level of penalty for such offences.¹⁹
- 1.36. The review and performance audit considered two key areas central to the development of the compliance review program: the means for choosing political parties (and their associated entities) for inclusion in the program and the nature and purpose of inquiry into financial information that takes place.

Development of the standard compliance review program

- 1.37. The approach to reviewing all of the major political parties disclosure performance over a three year cycle was described as a reasonable way to ensure there was an even-handedness which reinforced the Commission’s apolitical character and reputation.
- 1.38. Additionally, the development of positive relationships with the political parties in the course of the compliance reviews was described as at least as important as the mechanics associated with checking the accuracy of the disclosure returns. In the course of rectifying discrepancies with staff of the political parties the opportunity is taken to provide assistance and advice on how best to manage the preparation and presentation of returns.

¹⁹ An alternative option in connection with penalties and prosecution has been canvassed by JSCEM and was included as Recommendation 26 in its 2011 *Report on the funding of political parties and election campaigns*. JSCEM recommended that the Electoral Act be amended as necessary to make offences under Part XX that could be classified as ‘straightforward matters of fact’ be subject to administrative penalties issued by the Commission, with a mechanism for internal review. This would remove the need to go to the DPP for every prosecution. This is considered a very worthwhile reform. However, this option has not yet been taken up by the Parliament.

- 1.39. This is seen as advantageous to the Commission's task as well as a way of breaking down any sense of distrust directed towards the Commission arising from its compliance responsibilities.
- 1.40. The review was advised that it has been the practice to only include in reviews of the political parties those associated entities that are 'controlled' or 'operate, wholly or to a significant extent for the benefit of (the)...political parties' due to resource constraints.²⁰
- 1.41. Entities that provide support to the parties that do not meet this test but have links such as being financial members or having voting rights, have not been chosen for inclusion in party based reviews as the risks associated with such cases has been judged to be of a lesser order.
- 1.42. On this basis trade unions have been excluded from review as they do not meet the first test despite many being regular and substantial donors. In addition, other entities that also fail the first test but are closely linked to political parties through formal membership or the existence of voting rights are excluded for similar reasons.
- 1.43. Given that the main focus has been on checking the accuracy of disclosure returns received, it is difficult to understand the logic behind these choices.²¹
- 1.44. The current approach has clearly been influenced by the limited focus of the annual compliance reviews' stated primary purpose, the skill levels of the staff available to conduct them and the necessity to spread the limited resources available thinly while at the same time endeavouring to have a program that is defensible from an even-handedness viewpoint.
- 1.45. A precise 'commencement date' for the current approach to devising the compliance review program was not able to be obtained. It appears to have 'evolved' over a number of years from at least the 1990s. Despite being subject to a number of audits over the past decade, including by external consultants between 2002 and 2007, the approach to compliance reviews has remained broadly constant, with only some minor adjustments to practices taking place in response to internal audit findings.²²
- 1.46. The current approach thus appears to have been largely accepted by previous senior managers within the Commission that have been responsible for the area.

²⁰ The Commission received supplementation for the resource costs associated with its assumption of the compliance responsibilities in 1993. Since then, the section has grown from two to eight positions. The additional positions have been funded by reallocation of resources from within the Commission's funding base.

²¹ The Director of the compliance area stated that unions have been excluded from the compliance program because the financial contributions from unions that are associated entities to the Australian Labor Party are from affiliation fees, which are not treated as gifts under Part XX of the Electoral Act. It was stated that reviewing unions was less necessary when those finances, apart from the payment of affiliation fees, are essentially irrelevant to the conduct of political parties or federal elections (like any other natural person member of a political party). It was also a decision based on the fact that union finances are already subject to independent audit and review by Fair Work Australia. This appears to be an approach that developed over time and was not formally approved in any explicit documentation made available to the review.

²² The PricewaterhouseCoopers report at Part 4 includes more information on this.

- 1.47. I consider that the existing means of choosing candidates for inclusion in the compliance review program with its narrowly based objectives is considered to be flawed and is in need of review.²³
- 1.48. Throughout the course of the review, staff indicated that the bulk of discrepancies identified in the compliance reviews appear to be differences that have not arisen from a deliberate intent to hide transactions. They basically appear to be the result of sloppy completion of the returns, errors that have occurred in the process or reflect poor quality financial management. In these cases the discrepancies are resolved by correction or adjustment with the Commission adopting an ‘honest broker’ role.²⁴

The public view of compliance activities

- 1.49. The Funding and Disclosure Services section of last year’s Annual Report of the Commission emphasises the manner in which the Commission assists in educating clients as to their disclosure obligations and the work it does to ensure that returns lodged are accurate. The compliance reviews are referred to as a means by which errors and omissions in the returns are identified and corrected before publication.
- 1.50. Reference is then made to the Commission’s ‘broader’ investigative powers in relation to possible breaches of the disclosure provisions noting finally that the Commission ‘...makes a judgement as to whether the potential breach may compromise public disclosure to a sufficient degree to justify diverting resources to conduct an investigation.’ While these comments are unexceptional in themselves they confirm the view that the main focus of the compliance reviews is more about ‘good housekeeping’ rather than being directed at reinforcing a full and frank disclosure process through specific testing for signs of non-disclosure.
- 1.51. The annual report published key performance indicators for the Funding and Disclosure Services group as follows:

- Election funding calculated and paid in accordance with the legislation, and
- Financial disclosures obtained and placed on the public record in accordance with legislated timetables

The results reported for these two performance indicators in 2010-11 were:

- Achieved: 99% of entitlements for the 2010 federal election were paid in the fourth week after polling day,
- Achieved: Financial disclosure returns were published within the legislated timeframes

²³ The PricewaterhouseCoopers report at Part 4 details the importance of a comprehensive risk management framework that takes into account a range of external factors in addition to purely financial matters.

²⁴ This terminology is used in the internal documentation in FAD’s compliance area outlining their procedures for developing the compliance review program and conducting compliance reviews under section 316(2A) of the Electoral Act.

- 1.52. A pleasing result for the Commission no doubt but it would have added little to community confidence that there was an effective enforcement regime in place designed to discourage deliberate non-disclosure.
- 1.53. I believe that the way in which the compliance function is being performed today falls short of fully meeting the parliamentary expectations when the amendment was passed in 1991. The heavy emphasis on compliance reviews that have concentrated on the accuracy of disclosure returns lodged compared with the relative absence of reviews focussing on non-disclosure appears to have been accepted by past senior management ‘administrations’ within the Commission and has continued largely unchanged for some years. However, it does not adequately address the more serious concern – the potential corruptive influence of secret donations.
- 1.54. The labelling of the compliance checks undertaken as ‘reviews’ rather than ‘audits’, the term used by the parliamentarians when the proposed new section 316(2A) was being debated, also lends support to the view that what emerged from the legislative change is a weaker process of scrutiny than what had been anticipated.
- 1.55. The compliance reviews have proved to be largely ineffective in identifying apparent deliberate failures to declare significant amounts of money or gifts, mainly because their focus has been essentially directed more towards verifying the accuracy of the amounts included in the disclosure returns received. This has been identified as an issue in PwC’s performance audit of the function, which is included at Part 4 of this report.
- 1.56. As observed earlier, a substantial sum of money is donated to political parties by a considerable number of persons and organisations. While it is reasonable to believe that there is likely to be a high degree of honesty associated with the disclosure process, it is considered that the Commission should be seen to be making some effort to satisfy itself that this is so.
- 1.57. It is acknowledged that the dual obligation imposed on donors and recipients to declare receipts above the disclosure threshold is, to a degree, a valuable mechanism that encourages accurate and complete disclosure. However, it provides no protection against cases that could involve complicity by the two parties to deliberately conceal a secret donation.
- 1.58. The effectiveness of the dual disclosure obligations is also limited by the differences between the precise nature of the obligations. Donors to political parties have to disclose individual donations totalling more than the disclosure threshold and each individual donation to a political party where the total of those donations is more than the disclosure threshold.²⁵ However, political parties only need to disclose the total of sums received from individual donations that are ‘more than’ the disclosure threshold.²⁶

²⁵ See section 305B of the Electoral Act.

²⁶ See section 314AC of the Electoral Act.

- 1.59. These are inherent limitations in the design of the present disclosure scheme that need to be taken into account in its administration.²⁷
- 1.60. On the surface, the most positive benefit to the community is the assurance that flows from the existence of the public disclosure laws, bolstered by the Commission's enforcement powers that are designed to act as a brake against corrupt behaviour. However, a close examination of the approach and the results obtained from the Commission's compliance reviews over a number of years belies this confidence.
- 1.61. Giving more emphasis to the specific targeting of non-disclosure and the collection of objective information aimed at assisting the Electoral Commissioner to be able to make judgements about the extent of non-disclosure is needed in a properly balanced program. Even if efforts fail to reveal any or many instances of undisclosed gifts, for the Commission to be seen to be actively watchful would remove any grounds for criticism that it was not fulfilling its legislative obligations. It would also place the Commission in a better position to give more soundly based assessments to the Parliament about the level of compliance being achieved.
- 1.62. It is pleasing to note that the recent report from the JSCEM *Review of the Australian Electoral Commission's analysis of the Fair Work Australia report on the Health Services Union* tabled during the course of this review has reached a view similar to the direction of the conclusions reached by this review. In rejecting a proposal that compulsory auditing of returns prior to submission to the Commission be introduced, the Committee noted:

*The [Australian Electoral Commission] is the body best placed to conduct compliance reviews under the Electoral Act. However, the committee appreciates that there are resourcing pressures on the unit that prevent a review of all returns and those with suspected obligations. In developing its compliance review programs and prioritising reviews, the [Australian Electoral Commission] should take into consideration: ensuring reviews are undertaken on a cross-section of organisations; returns that involve the movement of significant sums; and cases where returns – or the lack of returns – seem to warrant closer examination.*²⁸

²⁷ The Joint Standing Committee on Electoral Matters examined this issue during its 2011 Inquiry into the funding of political parties and election campaigns. It recommended that the Electoral Act be amended to remove difference between the disclosure obligations for political parties and donors to political parties and align the obligations. See further Recommendation 9, *Report on the funding of political parties and election campaigns*, November 2011, Commonwealth Parliament of Australia, p. 69.

²⁸ Joint Standing Committee on Electoral Matters, *Review of the Australian Electoral Commission's analysis of the Fair Work Australia Report on the Health Services Union*, September 2012, Commonwealth Parliament of Australia, p. 55.

Interpretation of the legislation

- 1.63. In the course of the public hearings in July 2012 for the JSCEM inquiry into the Commission's analysis of the report on the Fair Work Australia investigation of the Health Services Union, the Hon. Mrs Bishop MP raised questions about the extent of the Commission's powers. During a number of exchanges with the Commission's representatives present she asserted that the Commission was not using the full extent of the powers it had in respect to compliance.
- 1.64. There have been some differences of view within the Commission about how broadly the compliance review powers of the Commission can be interpreted. Some have believed that the Commission was not approaching its obligations to police the financial disclosure provisions of the Electoral Act in a sufficiently robust fashion while others have considered that a more subtle approach was best.
- 1.65. Against the historical background to section 316(2A) outlined earlier, this review is satisfied that the provision provides adequate grounds for the use of the enforcement powers contained therein to expand the scope of the Commission's compliance activities in the manner outlined in this report. Part 2 of this report sets out a more detailed analysis of this issue from a legal perspective.

Recommendation 1:

The enforcement powers of the Commission under section 316(2A) of the Electoral Act should be relied upon to support an expanded program of compliance reviews aimed at extending their scope and depth.

The need for a new business model

- 1.66. To facilitate an expanded compliance review program, the consultants and I are of the view that the compliance activities need to be completely redesigned to establish a more proactive role that would represent a more positive expression of the Commission's compliance obligations, as well as better reflecting arrangements the community might reasonably expect to be in place. To do so in our view will involve a range of new strategies and approaches which will entail building a new business model for the function.
- 1.67. A new program of compliance reviews should include greater reliance on spot checks being undertaken on a random basis but informed by 'educated guesses' about organisations that might be worth targeting, for example those associated with large donations, the selection of a sample of smaller organisations, choice of bodies that have a history of lodgement of late or incorrectly completed returns and other related matters. Not only would inclusion of more randomly selected areas not regularly covered extend the scope of the compliance program, but the extra element of surprise and uncertainty in choice of entities for review would strengthen the disincentive factor.
- 1.68. A comprehensive database of the Commission's clients over time that provides a profile of their nature and characteristics built up from the accumulated experience gained in dealing with them, together with information drawn from other available official and public sources, should be developed as an intelligence database to aid the compilation of the annual compliance review program. This should be linked in with the determination of new IT requirements that will involve close communication between the FAD areas, to connect more closely the information needs with the work processes of both areas.
- 1.69. Should future compliance reviews aimed at checking on possible non-disclosure uncover suspect situations, providing that there is confidence that a 'reasonable grounds' test can be met, it should be standard practice to then cease the review and replace it with an investigation under section 316(3). This would ensure that the further investigation proceeds on a more formal basis and in a manner that would support a potential prosecution. It would also substantially increase the ambit from which corroborative evidence could be sought.
- 1.70. Greater reliance on the use of analytical skills and the recruitment of some experienced staff with more sophisticated financial forensic skills are clearly needed to add more 'bite' to the reviews. The Commission does not need to build up an excessively large investigative capacity but the present level of skill and the number of investigators currently employed are considered to be insufficient to support an expanded program in terms of breadth and depth.

- 1.71. As a start, at least two skilled analysts with financial investigative experience are needed if the Commission is to be able to achieve real change.
- 1.72. The recommendations in this report and the associated ones in the PwC's work are aimed at building up the Commission's investigative capacity. The implementation of the recommendations should give the Commission a greater degree of confidence in the future in assessing the level of compliance being achieved than is possible at present.
- 1.73. Even-handedness in a political party sense, in the choice of candidates for inclusion in the compliance review program, is still an important consideration in exercising the section 316(2A) powers, but ought not to dominate the selection process.

Associated entities

- 1.74. The FAD section undertakes a process annually whereby all registered political parties are contacted and asked to list their associated entities. There is no legislative power to conduct this process and a response cannot be compelled. As indicated elsewhere in this report, this is an imprecise exercise as often political parties themselves are not fully aware of all their associated entities.
- 1.75. In the course of conducting compliance reviews of political parties, where staff identify information that indicates a particular body may be an associated entity, it is used to determine whether there are reasonable grounds to exercise the power under section 316(3A) of the Electoral Act. The Commission has also in the past acted on complaints from individuals, media reports and information from other sources.²⁹
- 1.76. Given the inherent difficulties in comprehensively identifying all associated entities, the FAD section should consider incorporating directed measures in its practices, geared towards identifying comprehensively all associated entities of registered political parties. While it is recognised associated entities can change between financial years, the disclosure and compliance areas could collaborate to determine an appropriate strategy to improve the way in which the section identifies associated entities. One initial suggestion might to include some form of 'follow-up' of information received in response to the disclosure section's initial request for parties to inform the Commission of their associated entities, during the compliance review process. Where the circumstances warrant, section 316(3A) can then be invoked to obtain further information.

²⁹ See further http://www.aec.gov.au/Parties_and_Representatives/compliance/special-investigations.htm . This page includes links to formal decisions on special investigations undertaken by the Commission under section 316(3) and section 316(3A) of the Electoral Act.

Recommendation 2:

A new business model to facilitate the broadening of the compliance function should be developed involving:

- **a greater reliance on spot check reviews being undertaken on a random basis to broaden the scope and coverage of compliance reviews and supplement the regular compliance review program that has developed in the area,**
- **the conduct of reviews aimed specifically at enabling objective assessments to be made of the level of disclosure compliance being achieved,**
- **a direction of effort and resources to properly ensuring that all associated entities with disclosure obligations are captured by the Commission,**
- **continuation of the concept of even-handedness in coverage of the main political parties.**³⁰

Limitations of the proposed new approach

1.77. The new business model proposed in the preceding recommendations sets out a revised ‘scheme’ that aims to broaden the scope of coverage of organisations or persons included in the Commission’s compliance review program. However, there are a range of legislative limitations that will continue to apply. In enforcing compliance with the scheme, the Commission can still only:

- Under section 316(2A), serve a notice on an agent or other officer of a registered political party, a financial controller of an associated entity or a ‘prescribed person’ to determine whether they have complied with Part XX;
- Under section 316(3), serve a notice on ‘a person’ where there are reasonable grounds to believe that ‘person’ can provide information in relation to a contravention or possible contravention;
- Under section 316(2D), conduct an investigation of any gift of \$25 000 or more to a registered political party or a candidate. The Commission’s application of this power has been discussed elsewhere in the report, but it must be noted for the current purposes that section 316(2D) does not include a power to serve a notice on a donor of \$25 000 or more to compel information. This means the Commission’s scope to conduct an investigation under this power is limited to the information that is submitted to it in pursuance of the disclosure obligations.

1.78. The standard compliance review program is conducted under section 316(2A), which limits the ‘net’ of people that may be subject to a notice *without* the reasonable grounds proviso being satisfied to those that are covered by the disclosure scheme. This is the key distinction between the provisions.

³⁰ The PricewaterhouseCoopers report at Part 4 recommends a comprehensive risk management framework that the compliance section should adopt to underpin the selection of candidates for review.

- 1.79. Importantly, the development and application of the new business model for the Commission's compliance review function will not result in bodies that would not normally be captured by the terms of section 316 suddenly being included within the ambit of the Commission's compliance review program.
- 1.80. For example, the Commission has been subject to criticism for not including unions in its standard compliance review program conducted under section 316(2A), which, as mentioned above, extends only to individuals within political parties, associated entities and to prescribed persons.
- 1.81. The position of unions under Part XX of the Electoral Act is extremely complex. Unions are definitely not 'registered political parties' and they are not 'prescribed persons'.³¹ Thus, an individual union would only be captured by section 316(2A) if it met the 'associated entities' test.
- 1.82. Section 287 provides that an associated entity is:
- a) An entity that is controlled by one or more registered political parties; or
 - b) An entity that operates wholly, or to a significant extent, for the benefit of one or more registered political parties; or
 - c) An entity that is a financial member of a registered political party; or
 - d) An entity on whose behalf another person is a financial member of a registered political party; or
 - e) An entity that has voting rights in a registered political party; or
 - f) An entity on whose behalf another person has voting rights in a registered political party.
- 1.83. Union structures are many and varied. Some unions are associated entities of a major political party according to the definition of that term in section 287(1) of the Electoral Act and some are not.
- 1.84. Many unions that are not associated entities as per section 287 make donations to a political party or incur political expenditure, meaning they have a disclosure obligation under Part XX of the Electoral Act as an annual donor to a political party or a third party incurring political expenditure, not as an associated entity. Donors to political parties and third parties are not subject to the Commission's standard 'compliance review' power under section 316(2A). They may only be issued with a notice under section 316(3) where the 'reasonable grounds' requirement needs to be met as a pre-condition.

³¹ Unless they make a gift directly to a candidate or Senate group (as opposed to a political party) or a person or body (whether incorporated or not) specified, by legislative instrument, by the Commission and the gift is 'equal to or more than' the disclosure threshold during the disclosure period in relation to an election. See section 17(2A), section 305A(1A) and section 305A(1A) of the Electoral Act.

Impact of legislative change on the FAD area

- 1.85. Legislative change involving the Electoral Act has typically arisen from the outcome of inquiries by JSCEM or as a result of initiatives within government. Following the change of government in 2007 there was a focus on electoral reform that involved the preparation of two Green Papers. The first was entitled *Electoral Reform Green Paper – Donations, Funding and Expenditure*, the second was *Electoral Reform Green Paper - Strengthening Australia's Democracy*.
- 1.86. The management of major changes to electoral legislation is generally coordinated by an Electoral Reform Taskforce (ERT) which comprises representatives of the Department of the Prime Minister and Cabinet (PM&C), the Department of Finance and Deregulation (Finance) and the Commission.
- 1.87. The development of the Donations, Funding and Expenditure Green Paper was a collaborative affair primarily between PM&C and the Commission. This required the section head of the compliance area to be taken off-line for around four months in 2008 to work full time on the Green Paper. Because of the specialist nature of much of the work in FAD, particularly in the compliance area, temporary backfilling has normally not been possible.
- 1.88. After the Green Paper was released in late 2008 considerable work was still required by FAD staff in assessing submissions received and in discussions involving the Minister's Office about the possible production of a White Paper and/or the development of a Bill. FAD was required to prepare extensive material to assist this process, including modelling the impact of possible initiatives in tandem with the Green Paper which was canvassing wider, fundamental reform of the funding and disclosure schemes operated under Part XX of the Electoral Act.
- 1.89. The Commonwealth Electoral Amendment (Political Donations and Other Measures) Bill 2008 (the 2008 Bill) was introduced to Parliament to implement priority measures identified by the Government. Drafting instructions for this Bill were undertaken by FAD staff with the Legal Services Branch. FAD staff prepared detailed costings and, in conjunction with the Commission's finance section, conducted negotiations with the Department of Finance and Deregulation. Following the introduction of the Bill into Parliament, FAD staff were involved in a number of briefings, including to the crossbenches, and assisted in the development of Government amendments.
- 1.90. As was mentioned earlier, following the defeat of the 2008 Bill a new Commonwealth Electoral Amendment (Political Donations and Other Measures) Bill 2009 (the 2009 Bill), which was primarily the 2008 Bill consolidating the proposed Government amendments, was introduced to Parliament.

- 1.91. This 2009 Bill also did not pass into legislation and was reintroduced into the current Parliament as the Commonwealth Electoral Amendment (Political Donations and Other Measures) Bill 2010. It lays idle awaiting consideration by the Senate having passed through the House of Representatives in November 2010.
- 1.92. Overlaying this legislative activity the JSCEM conducted an inquiry into the 2008 Bill. It then conducted a round table on the Green Paper in 2009. In 2011 it held its *Inquiry into the Funding of Political Parties and Election Campaigns* that included the Green paper in its terms of reference. These inquiries required the involvement of FAD staff in preparing submissions and appearing before the Committee.
- 1.93. Outside the FAD area the Electoral Policy and Reform section that was relatively recently created in the Strategic Capability Branch, takes on the Joint Committee and longer term future reform work associated with the core electoral related business of the Commission. This group works with the Legal Services section where a close relationship has been forged due to the recognition that aspects of policy/legislation work need to be worked up in tandem to achieve the best result.
- 1.94. Traditionally, because of the limited understanding of FAD legislation and issues elsewhere in the Commission, FAD staff have had the burden of having to prepare their own reports (e.g. those required under section 17 of the Electoral Act), submissions to and appearances before the Joint Parliamentary Committee and Senate Estimates hearings, preparation of drafting instructions, ministerial briefings and a range of other detailed papers on top of their everyday work. This has occurred to a far greater extent than it has in relation to other subject matter areas within the Commission.
- 1.95. The latest example has been the recent JSCEM inquiry into the Commission's analysis of the Fair Work Australia report on the Health Services Union. This inquiry drew heavily on the Chief Legal Officer supported by the section head of the compliance section. It was a sensitive inquiry that raised some complex issues concerning the nature of the Commission's past performance of its compliance responsibilities and the interpretation of the legislation relating to associated entities.
- 1.96. This background is provided to illustrate the significant extent to which senior resources of the compliance group have often had to be diverted to policy development tasks. Inevitably this has had an impact on the time available for oversight of their ongoing responsibilities.

Proposed creation of a new Funding, Disclosure and Compliance Branch

- 1.97. The elements that cover the Funding, Disclosure and Compliance functions in the current Legal and Compliance Branch have had a chequered history in terms of their organisational placement within the Commission. At different times they have been attached to various branches, before joining their current home in the Legal and Compliance Branch in 2007. In addition there has been the separation of the Financial Compliance section from the Registration and Disclosure section since 2008.
- 1.98. This locational instability has left the Compliance Section with a legacy of uncertainty about its place in the organisation that has had an impact on staff morale. There is a feeling that they have not been regarded as a part of the main core of the Commission. Their physical separation from their closest neighbours from a functional viewpoint, the Registration and Disclosure Section, has also added to a sense of isolation from the mainstream at times.
- 1.99. These feelings or attitudes, while felt by staff to differing degrees, have not helped overall morale and have been a factor in the inability of the section as a whole to retain good staff.
- 1.100. Adoption of the recommendations in this report will involve a concentrated effort to implement and will require additional resources to be applied, both at the leadership and operational levels. It will also demand a strong commitment and involvement of managers at the section and branch level to drive the implementation process.
- 1.101. This will place additional demands on the existing branch head position which is already a heavily committed position ranging as it does across the whole organisation from a legal policy and advising point of view, while also holding down management and operational responsibilities for other unrelated functions.
- 1.102. The Commission has a history of being involved on almost a continuing basis with the development and management of a program of legislative change associated with the Electoral Act. This requires the close personal involvement of the Commission's Chief Legal Officer.
- 1.103. In addition activity connected with the work of parliamentary committees is also heavy. JSCEM is an active committee that has a charter that requires it to meet regularly. Senate Estimate hearings also involve the Chief Legal Officer in regular briefing of the Electoral Commissioner and appearing with him at public hearings which are heavily focussed on election issues particularly those associated with political party funding and disclosure.

- 1.104. I believe that there is a strong case to consider reducing the day to day management load on the Chief Legal Officer to allow him to concentrate his abilities on those matters that demand legal expertise by relieving him of most of his non legal related management responsibilities.
- 1.105. I am satisfied that the history of the Commission's frequent involvement with legislative developments touched on earlier and the complexity and uncertainty of the law in some respects, coupled with its political sensitivity, warrants providing the Chief Legal Officer with an increased capacity to concentrate more fully on the legal/legislative/parliamentary aspects of the Commission's responsibilities.
- 1.106. With this change the two FAD sections covering the registration and disclosure and financial compliance functions, would warrant a new branch head position. This person would be able to concentrate fully in leading the better integration of these two sections and developing more strongly the compliance review function in the directions recommended by this report.
- 1.107. The achievement of a closer integration of the different sections within the FAD area is an important goal and offers the prospect of acting as a key productivity multiplier if the various work procedures and practices are harmonised successfully.
- 1.108. The new branch that is proposed should have a commitment to actively seek to strengthen their client education and support role so that the level of confidence of the clients is raised in the hope that this will lead to a greater willingness to cooperate with the Commission. This objective will help to counteract, to some extent, the potential for some anxiety to be felt when the Commission embarks on a more proactive compliance program.
- 1.109. An additional matter that will warrant consideration should a new branch be constituted is the Commission's position on the results of compliance reviews being made public, for example, on the website. In its November 2011 *Report on the funding of political parties and election campaigns*, JSCEM recommended that details of compliance reviews be made publically available.³²
- 1.110. Should this measure be passed by the Parliament in the future, the Commission will need to ensure that the information it makes available to the public has been subject to a sufficient degree of internal accountability and that the information contained in the compliance review reports is sound and able to withstand the wider scrutiny that publication will entail.

³² Recommendation 29, Joint Standing Committee on Electoral Matters, *Report on the funding of political parties and election campaigns*, November 2011, p. 188.

- 1.111. The PwC report states that currently, the details of compliance reviews remain predominantly in-house within FAD. Accordingly, as an initial step towards greater transparency and accountability in the conduct of compliance reviews, each compliance review report ought to be submitted to the branch head of the newly constituted branch for approval before its release both to the clients and to the public. This will place the Commission in a position where it can confidently attest to the information it makes public and is a prudent safeguard against any suggestion of political partiality, given the sensitivity associated with compliance review activity.³³
- 1.112. The review considers that there is a need in a newly constituted branch for there to be a capacity for longer term research, analysis and policy reform covering the FAD functions. To date this has come from one of the section heads on an ad hoc basis. Under new arrangements it is considered that a dedicated position for this purpose should be established either in the new FAD branch or in the Strategic Capability Branch. This is an issue for the Commission to decide but the inclination of the review is that for at least until new arrangements have been developed and bedded down, the preferred location would be in the FAD Branch itself.
- 1.113. While there is the option of placing the two FAD sections under the control of another existing branch head, thus avoiding the need to create another SES position, this is not favoured. It would only perpetuate the sense of alienation the FAD staff has always felt due to its functions and culture being different to those involved in mainstream electoral related matters. More importantly, it would not provide the dedicated leadership necessary in a politically sensitive area that will be heavily involved in a significant change management program.

Recommendation 3:

A new branch should be established to encompass the party registration, political funding, public disclosure and related compliance functions of the Commission. The occupant of the new SES position would provide dedicated leadership to the group and in particular would pursue the closer integration of its work and the future development and redirection of the focus of the compliance review function.

- 1.114. Adoption of this recommendation will have consequential implications for the organisational placement of the remaining elements of the current Legal and Compliance Branch. This review makes no recommendations in this regard.
- 1.115. Aside from the establishment of a dedicated FAD branch, an immediate priority is the need to link the direct accountability of the function to the agency's Senior Executive reporting scheme.

³³ In some overseas jurisdictions, compliance review reports are considered to be sufficiently sensitive that their contents are reviewed by an independent body or group before release. This may warrant further examination by the Commission in the future.

1.116. A monthly ‘Balanced Scorecard’ that goes to the Executive for consideration covering all other business areas of the agency, such as Enrolment and Elections. The party registration area within FAD is included in the Balanced Scorecard, but the disclosure and compliance areas currently are not. Their inclusion would increase direct Senior Executive engagement, support and oversight of the area and would provide a regular accountability mechanism consistent with what applies elsewhere in the Commission. A set of meaningful, measurable indicators need to be developed for inclusion on the Commission’s corporate Balanced Scorecard. As a starting point, some items for inclusion might be:³⁴

- Number of disclosure returns lodged electronically (where relevant);
- Number of hard copy returns lodged (where relevant);
- Number of compliance reviews incomplete at beginning of the month;
- Number of compliance reviews completed during the month;
- Number of compliance reviews on hand at the end of the month;
- Applications for internal review in relation to compliance notices issued;
- Breakdown of the types of organisations on which compliance reviews have been conducted (e.g., unions, corporations, other);
- Number of investigations underway.

It is recognised that some of these would only be relevant at certain points of the disclosure cycle.

Improved information management system

1.117. The compliance program would be enhanced if the team had access to a comprehensive information management system which allows a history of each client to be accessed from a single source. Currently some information about clients is stored in the Returns Management System (SuperFAD) but this system has been developed to manage the disclosure functions and is of limited benefit for the compliance function. If the system was progressively expanded to include all records and knowledge about clients, it would provide a valuable tool to assist in identifying those to be selected for ‘random’ compliance reviews based on a risk assessment and management framework.

1.118. Further development of the SuperFAD system to meet the intelligence and other needs of the compliance group would be necessary for this purpose as well as to create a common information technology capability for the whole branch.

1.119. Part 3 of this report contains more detailed observations and suggestions relating to the FAD group of functions and how they might be better integrated under the revised arrangements recommended in this report.

³⁴ These are based on the indicators currently reported by the party registration area of FAD in its Balanced Scorecard.

1.120. These comments are provided particularly for the assistance and guidance of the person who becomes responsible for future arrangements in this area.

Recommendation 4:

The SuperFAD system should be developed further as an integrated information management system serving the needs of all of the elements of the FAD group.

Summary of conclusions arising out of the PwC performance audit

1.121. The performance audit conducted by PwC identified issues and recommendations in relation to the Commission's compliance review function. Four major areas were examined and the key themes reflected in the recommendations in relation to each are summarised below. The full report on the performance audit conducted by PwC, which contains a number of detailed recommendations aimed at improving the future performance of the compliance function, is included at Part 4.

Governance

1.122. The PwC performance audit determined that there needs to be a clearer definition of strategic direction and enhanced Executive support for the Commission's disclosure and compliance function than has previously been the case, as the section currently operates, at least to a degree, in isolation from the rest of the Commission. This situation may have developed, at least in part, because the function is seen as ancillary to core responsibilities of the Commission such as conducting federal elections and referendums, and maintaining the Commonwealth electoral roll.

1.123. In addition, the establishment of an effective governance framework to ensure objectives are communicated and being achieved, the oversight of outcomes, resource allocation and monitoring of performance are necessary for the Commission to improve outcomes in carrying out the disclosure compliance function. The governance issues are partly evidenced by the number of previous audit recommendations relating to the function that have been partially implemented and not subject to an effective follow-up process to ensure the effectiveness of actions and confirm the progress achieved.

1.124. There exists a need for engagement and representation at the Executive level which will involve dedicated senior leadership for the function, strategic alignment with the AEC, oversight of objectives, and increased accountability.

Risk management framework

1.125. There is currently no risk management framework encapsulating both the overall compliance review function and a risk-based sampling methodology to ensure efficient and effective coverage of political parties and associated entities. The absence of a risk management framework has resulted in the compliance function being reactive and reliant on the existing corporate knowledge of its management team with risks being identified and managed in a haphazard manner.

1.126. Political parties and associated entities are subject to coverage on a cyclical basis through a routine schedule which results in the selection process not being risk-based.

- 1.127. This approach to compliance review coverage reduces the need to apply professional judgement and can result in staff time being unnecessarily allocated to compliance review activities that are less risky whilst providing insufficient attention to higher risk organisations and situations.
- 1.128. The risk management framework needs to be integral to the Commission's approach to conducting compliance reviews as a key input for decision-making, and determining the appropriate allocation of resources and methodology. An effective risk management framework will assist with identifying and establishing a range of compliance review approaches to present an element of unpredictability to the process. In summary terms, potential approaches should involve:
- Test checking the accuracy of a sample of annual disclosure returns following improvements to the existing compliance methodology;
 - Use of specialists and appropriate expertise to more forensically research books, records and other available material to get "behind the scenes" and identify potential misstatements by applying sensibility tests in a more structured manner;
 - Random checking a sample of organisations selected on the basis of potential disclosure misstatements, instinct and other intelligence gathering techniques to maintain unpredictability; and
 - Limited review of a sample of annual disclosure returns that are considered lower risk involving a reasonableness review of the information provided prior to publication on the AEC web site.

Audit methodology

- 1.129. The compliance review methodology requires improvement across key phases of the process including planning, fieldwork, reporting, quality assurance and documentation. The function would also benefit from access to specialist investigative services to provide capacity and directly relevant expertise for the conduct of compliance investigations.
- 1.130. The existing methodology is focussed on detailed checking of the accuracy of all information already provided by the political parties and associated entities in their annual disclosure returns. Efficiencies could be gained by testing a smaller sample of transactions in this manner, and directing the additional time available towards the risk of understatement to ensure that the information presented is not missing items that require disclosure in the annual return.
- 1.131. Testing of completeness is being performed on a haphazard basis and there is inadequate evidence or appropriate documentation to support whether these procedures are being satisfactorily performed.

Human resource management

- 1.132. The compliance team has encountered challenges with attracting, training and retaining suitably experienced or qualified staff with the requisite skills required to perform roles during the key phases of the compliance review process. The function would benefit from supplementation of more contemporary audit and financial accounting skills, experience and qualifications in conjunction with some 'fresh thinking' and investigation proficiencies.
- 1.133. Prior to approaching the market for these types of staff resources, a comprehensive workforce planning process of the compliance function needs should be conducted that will inform a strategy to attract, recruit, train and retain the optimal staffing mix with suitable qualifications, experience, skills.
- 1.134. The function also requires access to appropriate subject matter specialists and technical expertise to provide assistance across certain aspects of the scheme including the provision of in-house training. Assignments that utilise external specialists should involve working directly with a compliance team member(s) to facilitate knowledge transfer as an additional training opportunity to build on lessons learned and improve the existing methodology.

Concluding remarks

- 1.135. Organisations like the Australian Electoral Commission and indeed government agencies generally with regulatory powers that are exercised to help keep community bodies accountable for their actions and compliant with the law, are particularly at risk of having their reputations tarnished if they are found to not be meeting the high standards of professional conduct they are expected to follow in the performance of their responsibilities.
- 1.136. Implementation of the recommendations in this report is designed to provide the Commission with a more effective compliance program and a more developed and competent in house investigative capability to deal with any future significant investigations across the Commission as a whole. In so doing, the Commission will be better able to provide a stronger sense of assurance to the community and the Parliament that the integrity of the funding and disclosure provisions of the Electoral Act are being protected properly.

Part 2: An analysis of the investigatory powers of the Commission associated with the disclosure and compliance provisions of Part XX of the Electoral Act

2.1. The Commonwealth disclosure and compliance scheme operates in pursuance of two key outcomes through two different means:

- It seeks to obtain the voluntary compliance of the willing by educating them about their obligations (for example through guides and the website) and relationship building.
 - This also involves a ‘deterrence element’ in that the willing will comply with legislation and meet their obligations in part because of a fear or awareness that if they do not, there could be enforcement action.
- It seeks to obtain the enforced compliance of the unwilling using the enforcement powers in Part XX of the Electoral Act.³⁵

The way in which the Commission balances these two aspects of obtaining compliance with the scheme should be a central consideration in its overall administration of the disclosure and compliance function.

The Commission’s enforcement powers

2.2. There are three key provisions through which the Electoral Act seeks to effect enforcement action:

- First, there is a general power in section 316(2A) that can be exercised to determine whether a prescribed person, financial controller of an associated entity or a political party agent has complied with Part XX;³⁶
- Second, there are powers in section 316(3) and section 316(3A) that allow the Commission to undertake investigations where it has ‘reasonable grounds’ to do so, in relation to a contravention or possible contravention of the part or regarding whether an entity is or was at a particular time, an associated entity.³⁷

2.3. If an attempt is made to link each of the enforcement provisions to the means by which the scheme attempts to operate as described above (voluntary compliance of the willing and forced compliance of the unwilling), section 316(3) and section 316(3A) would be classified as working to achieve the forced compliance of the unwilling.

³⁵ A similar distinction was originally identified in B. Edgman, ‘Political Funding: Challenges of Enforcement and Compliance’, Paper prepared for the Challenges of Electoral Democracy Workshop, University of Melbourne, July 2011, p. 2.

³⁶ Section 316(2A) is a compulsive power that may be exercised to require the production of documents and other material and obliging persons to provide oral or written evidence from the persons specified in the provision.

³⁷ Section 316(3) and section 316(3A) are compulsive powers that can be exercised to require the production of documents and other material in relation to a contravention or possible contravention where there are reasonable grounds to believe that ‘a person’ is capable of doing so.

Importantly, the reasonable grounds limitation of section 316(3) often leads to disconnect between expectations as to:

- Enforcement actions that *should* be taken in light of the broader aims of the scheme; and
- Enforcement actions that *can* be taken in light of the limitation on the Commission's powers by the 'reasonable grounds' requirement.³⁸

- 2.4. It is here that the agency has been subject to criticism throughout the operation of Part XX of the Electoral Act.³⁹
- 2.5. In contrast, section 316(2A), which was inserted into Part XX as a measure included in the *Political Broadcasts and Political Disclosures Act 1991*, states that a notice to produce documents or appear at a time and place to give evidence can be issued to determine 'whether someone has complied with Part XX'. That is, while the powers in section 316(3) and section 316(3A) are tempered by the need to have 'reasonable grounds' before they can be exercised and seemingly relate to potential 'wrongdoing' that may lead to prosecution action. Section 316(2A) contains no such limitation or reference.
- 2.6. Section 316(2A) does, however, limit the Commission's power to serving a notice on an agent or officer of a registered political party, a financial controller or officer of an associated entity and a 'prescribed person'.⁴⁰ That is, people or organisations other than these do not come within its scope. This would include any donors to political parties and third parties incurring political expenditure. These bodies and individuals may only be issued with a notice under section 316(3) where the 'reasonable grounds' proviso is met'.
- 2.7. An attempt to link section 316(2A) to a single limb of the voluntary and forced compliance dichotomy is not as straightforward as with section 316(3) and section 316(3A). The compliance power could act as a deterrent so as to encourage the voluntary compliance of the willing by providing an opportunity to make contact and educate the relevant actors on how best they can meet their obligation. However, it could also be used as a means by which the perceived unwilling could be forced to comply where the reasonable grounds threshold may not necessarily be met in a legal sense.

³⁸ B. Edgman, 'Political Funding: Challenges of Enforcement and Compliance', Paper prepared for the Challenges of Electoral Democracy Workshop, University of Melbourne, July 2011, p. 3.

³⁹ See generally *Committee Hansard* 6 July 2012 and *Committee Hansard* 16 July 2012.

⁴⁰ A 'prescribed person' is a person named in an election report prepared under section 17(2A) of the Electoral Act. A 'prescribed person' is a person that 'has or may have' a disclosure obligation under section 305A(1) or section 305(1A) of the Electoral Act. Donors to candidates and Senate groups have a disclosure obligation under section 305A(1) and donors to persons or bodies specified by legislative instrument by the Electoral Commission have a disclosure obligation under section 305A(1A).

- 2.8. The issue that subsequently arises is whether section 316(2A) should be used at least in part, as a means to bridge the apparent disconnect between enforcement actions that can and should be taken through exercising the power conferred by the provision in a focused manner based on sound risk assessment frameworks and considered internal policies. This is not to suggest the targeted exercise of the power would replace the current approach of reviewing each political party once in an electoral cycle. The extent to which the two operate alongside each other is a question of degree and is a matter to be resolved during the implementation stages of a revised approach.
- 2.9. The decision of the agency as to the way in which the section 316(2A) power is to be applied is paramount in determining the best way in which the agency can perform its disclosure and compliance function. In making this decision, there is a range of competing considerations including:
- The purpose of the scheme in Part XX, including the way in which this purpose relates to the specific exercise of the agency’s enforcement powers in section 316;
 - The impact that a change in the use of enforcement powers would have on the organisation, in terms of resources and other areas of identified risk; and
 - The maintenance of political neutrality.

What is the purpose of Part XX of the *Commonwealth Electoral Act 1918*

- 2.10. One of the key principles underpinning the effective administration of legislation is the development of policies and procedures and the conduct of administrative tasks in accordance with the purpose of the legislation in question.
- 2.11. The disclosure and compliance provisions that were inserted into the Electoral Act in 1983 were introduced as a part of a range of broader electoral reforms in areas including Senate voting, redistribution and the timing between the calling of an election and the close of rolls. The provisions have never been afforded a clear, explicit ‘purpose’ by the parliament in relation to their content and operation.
- 2.12. The reason for the absence of a clear purpose is most likely, at least in part, because the disclosure and compliance scheme was introduced primarily as a component of new public funding arrangements. It was stated in the second reading speech:

An essential corollary of public funding is disclosure-they are two sides of the same coin. Unless there is disclosure the whole point of public funding is destroyed...⁴¹

⁴¹ Senator Hill, ‘Second reading speech: Commonwealth Electoral Legislation Amendment Bill 1983’, Senate, *Debates*, 30 November 1983, p. 3050.

2.13. The introduction of an accountability mechanism in the form of a disclosure scheme simply as the ‘other side of the coin’ to public funding arrangements contrasts the introduction of many other enforcement or integrity mechanisms, which are introduced solely in response to an identified problem.

2.14. Additional guidance on the purpose of the scheme relating to this need for accountability that results from political parties receiving public funds can be afforded from the 1983 Joint Select Committee on Electoral Reform (JSCER) Report, where it was stated:

The majority of the Committee accepts the view that the receipt of significant donations provides the potential to influence a candidate or party and that to preserve the integrity of the system the public need to be aware of the major sources of party and candidate funds of any possible influence.”⁴²

2.15. The FAD section has developed its own purpose in relation to Part XX by applying existing sources relating to the introduction and continued amendment of Part XX of the legislation:

[the Commonwealth disclosure and compliance scheme is] helping guard against corruption by requiring those involved in the political process to publicly disclose relevant financial dealings.

2.16. It appears then that the disclosure and compliance scheme essentially involves attempting to prevent corruption by releasing accurate and complete information about the finances, including the sources of finances, of key political actors in the process. That is, the scheme operates on the despatch of information into the public domain, and it achieves its purpose just by making accurate and complete information available to the community. Where the information reveals some form of potential ‘wrongdoing’ or influence (undue or otherwise), the agency’s actions in addressing the actual or potential ‘wrongdoing’ will naturally be subject to intense scrutiny. This highlights the importance of transparent policies and procedures to govern the application of enforcement powers.

2.17. The disclosure and compliance role that has been conferred upon the Commission is somewhat different to the other responsibilities that the Commission administers. Disclosure and compliance naturally play a role in the integrity of the electoral system, which the Commission is responsible for maintaining. However, where other important areas of the Commission’s business, such as elections and enrolment, are concerned, the integrity lies predominantly in the very application of established processes and procedures developed to facilitate legislative purpose and requirements.

⁴² Joint Select Committee on Electoral Reform, *First Report*, September 1983, Commonwealth Parliament of Australia, paragraph 10.9

- 2.18. Where disclosure and compliance are concerned, while processes and procedures are important, the *manner* and *target* of their application involves an exercise of discretion on the part of those responsible for the function and a consideration of external, sometimes political, factors not present in other areas of the Commission's core business. This needs to be accounted for when deciding the way in which the Commission can best perform this function.
- 2.19. Given the potential for scrutiny of the agency's actions where possible wrongdoing or undue influence is identified, as well as the amount of discretion in the application of disclosure and compliance provisions, it is increasingly important that the enforcement powers that have been conferred upon the Commission in relation to Part XX are exercised in a manner that takes into account the range of competing considerations in this area.

A targeted application of section 316(2A)

- 2.20. In 1985 during the Joint Select Committee on Electoral Reform's (JSCER) inquiry into the conduct of the 1984 federal election, the Commission informed the committee that its power to undertake 'random compliance audits' of political parties under section 316 had been rejected by two political parties.
- 2.21. Following this, the Commission sought legal advice from the Attorney-General's Department and was advised that section 316 did not enable 'an authorised officer to require the production of party records relating to gifts that are not required to be set out in a Part XX return'.⁴³
- 2.22. In its submission to JSCER in its inquiry into the 1984 election, the Commission argued that it believed that it had always been the parliamentary intention that the powers conferred upon it by section 316 would allow it to conduct random compliance audits. The JSCER report regarding the inquiry into the conduct of the 1987 federal election and 1988 referendums stated:

*As [the Commission] was unable to conduct such audits (except in cases where a breach of the Electoral Act was suspected) the [Australian Electoral Commission] considered its ability to administer and enforce the disclosure provisions of the Electoral Act was severely limited.*⁴⁴

- 2.23. However, JSCER in 1984 concluded that the existing powers were sufficient for the Commission to perform its role and that there was no need for spot audits. JSCER also stated in its report that it was able to use its own investigative functions to help enforce the disclosure provisions in the Electoral Act.

⁴³ Joint Standing Committee on Electoral Matters, *Who pays the piper calls the tune – minimising the risks of funding political campaigns*, June 1989, Commonwealth Parliament of Australia, p. 72.

⁴⁴ Joint Standing Committee on Electoral Matters, *Who pays the piper calls the tune – minimising the risks of funding political campaigns*, June 1989, Commonwealth Parliament of Australia, p. 72.

2.24. In 1989 JSCEM recommended, as a response to the Commission's indication that it could not confidently say that political parties were complying with Part XX of the Electoral Act in light of the existing powers that the Commission be given the power to conduct spot audits of 'electoral activities' of registered political parties. It also recommended that the Commission publish a record of all spot audits undertaken but with detailed information on audits provided only where there has been a breach of the Electoral Act. This indicates that the initial intent of the insertion of the provision in to the legislation was for a targeted use of the power.

2.25. The second reading speech when the provision containing the general compliance review power was introduced into the Electoral Act potentially supports a more targeted approach to the use of section 316(2A):

The Government is determined that the Electoral Commission should be armed with the powers necessary to enforce the disclosure requirements of the Act. The Commission has for some time had the power to conduct investigations where it has reasonable grounds to believe that an offence relating to the disclosure provisions of the Act has been committed. The [new] provisions amount to the ability to conduct a spot audit of a political party or a candidate's financial affairs to ensure the Act has not been breached.

While the Commission retains confidence in the efficacy of such compliance audits as an enforcement tool, the current provisions require the Commission to have reasonable grounds to believe that a breach of the Act may have occurred in order to activate an audit. This has prevented the Commission from conducting random audits.

The Government's amendments will remove the deficiencies in the Act and provide the Electoral Commission with the power to subject political and third parties to random audits to ensure compliance with the disclosure requirements of the Act. The Commission will be able to do so at any time and will not be required to have a reasonable ground to suspect an offence under the Act has been committed. Political and third parties will be subject to a random audit at any time.⁴⁵

2.26. Importantly, representatives from the FAD area have noted that there has been a tendency away from a 'risk-based', targeted approach to applying section 316(2A) because the term 'risk' tends to indicate some level of actual or suspected wrongdoing, before inquiries have even been undertaken. This in itself is thought to be potentially damaging to the relationship between political parties, associated entities and the Commission, as well as the educative function that is sought to be performed as a part of obtaining the voluntary compliance of the willing.

⁴⁵ The Hon. Kim Beazley, 'Second reading speech: Political Broadcasts and Political Disclosures Bill 1991', House of Representatives, *Debates*, 9 May 1991, p. 3477.

2.27. It is clear then that a new, targeted approach to the application of section 316(2A) to complement the current program involving each political party being subject to a compliance review once in an electoral cycle, involves a significant shift in rationale for the way in which the power is applied. It also has a number of subsequent implications.

Impact of a targeted application of section 316(2A)

2.28. In order to protect the Commission's status as a politically neutral body responsible for the conduct of fair and impartial elections, consistent and transparent policies in relation to the application of section 316(2A) would need to be devised.

2.29. The targeted application of section 316(2A) could potentially expose the Commission to criticism on the basis that the agency is essentially trying to broaden their powers of investigation. The responses to such propositions are all outlined above. It is also of note that many other Commonwealth agencies, including those performing investigative functions, for example, Fair Work Australia, have frameworks that provide for the pursuit of inquiries without the need for a 'reasonable grounds' threshold to be met.

2.30. Where a targeted application of the section 316(2A) power takes place and information is uncovered that would meet a 'reasonable grounds' test, the initial 'compliance review' should cease and be replaced by an 'investigation' including more in-depth analysis under section 316(3). This will then provide the Commission with the power to require documents and evidence to be given by any 'person' as opposed to the limitation in section 316(2A) which is only restricted to particular people and office bearers identified under the disclosure scheme.

2.31. Short of legislative change to create a link between the provisions specifically stating the circumstances that will cause a process to shift from a 'compliance review' under section 316(2A) to an investigation under section 316(3), transparent policies and processes need to be devised. The policies and procedures need to outline the circumstances in which the discovery of a particular issue in examination of financial information under section 316(2A) could prompt a consideration of whether there are 'reasonable grounds' to then progress the 'inquiry' under section 316(2A) into full investigation under section 316(3).⁴⁶

2.32. There are implications as to the resources that will need to be directed towards disclosure and compliance regardless of the approach that is taken to applying section 316(2A).

⁴⁶ The 'Australian Government Investigation Standards' (2011) is the minimum standard that should be followed by government agencies in the administration of legislation for which they are responsible. The standards apply both to inquiries and more formal investigations. This should be the basis of development of investigative arrangements suitable to the Commission's needs.

- 2.33. A revised team structure where one team follows the standard compliance review program and another conducts the targeted reviews seems fundamental. The teams would need to develop their targets and programs in collaboration to avoid overlap.
- 2.34. The approach that is taken also has significant implications for the depth and nature of analysis undertaken on the financial records of those subject to an exercise of the powers under section 316.

Depth of analysis of financial records

- 2.35. The current approach to the application of section 316(2A) means that the process followed when political parties are ‘reviewed’ involves a lesser degree of rigour than is generally applied as part of a ‘full’ audit under accepted definitions. This is a decision that has likely to have been made based on the resources that have traditionally been available for FAD work and the absence of technical skill and expertise that has traditionally existed in FAD. A major influencing factor in determining this approach has been the section’s experience that the records kept by many organisations captured by the disclosure provisions would never be sufficient to allow for a complete audit.
- 2.36. Where an investigation is conducted on the basis of section 316(3) or (3A), the depth of analysis on financial records is much more detailed and requires a higher level of skill and expertise, which potentially does not exist within the current staff. If arguments suggesting more focused application of section 316(2A) are accepted, this deeper level of analysis will need to be undertaken in each instance in which section 316(2A) is applied, which is naturally more resource intensive than the current approach.
- 2.37. There is detailed guidance on the use of the word ‘audit’ in the public sector, but it is worth noting that the term was used extensively in the second reading speech and committee discussions and reports regarding the broadening of the Commission’s investigation power. The current guidance on the use of the term and the capacity of the Commission to conduct compliance work under section 316 so as to meet that definitional guidance or another comparable standard, in light of resources and other constraints, will be important in determining the scope of the section 316(2A) powers.

Part 3: Suggestions and observations to improve outcomes in the FAD section

Background

- 3.1. The FAD section is responsible for administering four distinct yet conceptually linked functions in Part XI and Part XX of the *Commonwealth Electoral Act 1918* (Electoral Act). These are:
- The payment of election funding by the Commission following an election;
 - The registration of political parties and related processes such as the recognition of state and territory branches, which are central to determinations regarding the payment of election funding and disclosure obligations under Part XX;
 - The annual financial disclosure obligations of political parties, associated entities, donors to political parties and third parties incurring political expenditure in defined categories, as well as election based disclosure by candidates, Senate groups and donors to candidates and Senate groups; and
 - The compliance and investigations powers to ensure those captured by Part XX comply with the provisions.
- 3.2. Upon its inception, the financial disclosure, election funding and compliance functions were administered by a single FAD section, with a separate team responsible for party registration. The section was overseen by one Director. The Director was supported by at least two EL 1s and a number of junior staff.
- 3.3. In 2008, an additional position at Director level was created, which led to the section being split into two. One Director was to oversee the disclosure and party registration functions, with a second Director responsible for the payment of election funding following a federal election and the administration of section 316.

Current situation

- 3.4. While the division of responsibilities has proven to be effective in providing two separate directors with a more manageable set of responsibilities, the way in which the section has developed has rendered the conceptual linkage between the functions increasingly difficult to maintain in its administration. The relationship between the disclosure and compliance areas, as well as the overall relationship with the party registration area has become weaker over time.⁴⁷

⁴⁷ For example, the party registration area has involvement in resolving contentious issues such as disputes within political parties on office bearer matters and a range of other issues. It would be useful to have a structured mechanism in place to facilitate communication on these issues so the compliance area are aware when developing their compliance program and can determine whether it will have an impact.

- 3.5. The lack of integration in the FAD section as a whole is attributable to a number of interrelated historical and other factors. FAD staff indicated that the extent to which the whole section worked together and interacted with each other did decline when the areas moved in 2010. For example, regular whole of section meetings with standing and other items on the agenda used to take place, as well as other joint social activities. Conversations between staff in the two areas were also more frequent. A number of staff stated that currently, conversations between staff in the areas were increasingly infrequent and tended to only take place where an error or omission had already occurred.
- 3.6. The Directors overseeing each area felt that they did collaborate where this was warranted, but acknowledged that many staff would seek more and better collaboration between the two areas. One Director also indicated that there was frequent poor communication between the areas from the EL 2 level and down, and this was particularly likely to occur where there was disagreement between the two Directors on a particular matter.
- 3.7. It is important to note that communication issues and lack of effective integration in the public sector between areas that need to work together is not uncommon. However, a more collaborative approach to administering Part XX of the Electoral Act between the different areas that comprise FAD will result in improved outcomes and increased efficiency in the conduct of the Commission's role in this area.

Suggestions for increased integration between the three FAD functions: a strategic purpose and section objectives

- 3.8. During the course of the review, staff stated that they felt at times as though they were operating in a 'vacuum' with no overall aim or objective guiding their work or providing them with a clear sense of purpose and direction.
- 3.9. Administration of the Commonwealth disclosure and compliance scheme is an inherently complex task, given the nature of the introduction of that scheme. The financial disclosure and compliance scheme was introduced as a 'corollary' to the introduction of public funding, but there was little elucidation of the purpose and objectives beyond it being a necessary accountability for those that were to receive public money. In more recent times the compliance section of FAD has defined its own purpose to guide its administration of the legislation in the following terms:

Helping guard against corruption by requiring those involved in the political process to publicly disclose relevant financial dealings

- 3.10. Along these lines, the whole FAD section should work towards defining its own strategic purpose and objectives to complement the legislative purpose the compliance area has developed for approval at Executive level.

3.11. In order to effectively provide a sense of purpose and direction to those that work within it, a strategic purpose and set of objectives need to be devised and agreed to by the staff in the area. It is important that the strategic purpose capture all functions performed by the FAD area and that its role within the agency as a whole is also determined and stated.

3.12. To assist this process the review has developed a possible approach as follows:

[The purpose of FAD is] To play a role in guarding against corruption and the exercise of undue influence in the electoral and democratic process and contribute to creating an informed and aware electorate by administering a disclosure scheme that ensures relevant political financial dealings are transparent by:

- Maintaining an accurate Register of Political Parties and undertaking the process of recognition of state branches of political parties to act as a basis from which to determine which political parties have obligations to disclose relevant financial dealings;⁴⁸
- Playing a proactive role to ensure that all participants in the democratic process that have a legislative obligation to disclose particular financial dealings are aware of the nature of the obligation; the ways by which they meet the obligation and the consequences if they fail to meet the obligation;
- Publicly releasing the required information on political financing by the statutory deadline in a manner that is widely accessible by and available to the community;
- Using the powers conferred in section 316 and sound risk assessment frameworks to conduct analysis of the financial records of political parties and associated entities, according to best practice methodologies in the auditing field to guarantee the accuracy and completeness of disclosure; and
- Undertaking prosecution actions against those that commit an offence under Part XX of the Electoral Act.

During and following an election period, to:

- Maintain an accurate Register of Political Parties;
- Play a proactive role in ensuring that candidates, Senate groups and donors to candidates and Senate groups are aware of their legislative obligation to disclose particular financial dealings, the nature of that obligation and the ways by which they can meet their legislative obligation;

⁴⁸ Party registration, appointment of office bearers (particularly registered officers and deputy registered officers) and the recognition of state branches process is also very important for candidate nominations during an election, the use of the electoral roll by political parties and the printing of ballot papers. For the purposes of the review, only the role of the function within the FAD section has been captured.

- Undertake prosecution actions against those that commit an offence under the Electoral Act in relation to financial disclosure following an election; and
- Following an election, manage and undertake the payment of election funding according to the official rate to those that are entitled to its payment under Part XX of the Electoral Act in a timely and accurate manner.

3.13. The above statement establishes the links between the processes administered by each of the areas of FAD and connects these processes to the overarching purpose of guarding against corruption and undue influence through ensuring transparency in political financing. An approved strategic aim and objectives along these lines would provide staff with some context and purpose to their roles that would definitely be of benefit. It would ideally also operate to improve work processes and equip staff to recognise the instances in which some broader contextual factors may need to be taken into account and in the application of standard procedures.

Administration of the disclosure and compliance scheme

3.14. The paper at Part 2 of this report puts forward the argument that the disclosure scheme at the Commonwealth level was introduced primarily as an ‘essential’ or ‘necessary’ accountability mechanism for political actors, given that a public funding scheme (which meant that political parties were going to be receiving taxpayer money) was to be introduced. This is in contrast with many other enforcement and accountability schemes in a range of other areas, which have predominantly been introduced as stand-alone measures in response to an identified or perceived problem.

3.15. Part 2 refers to obtaining ‘voluntary compliance of the willing’ as one way in which the disclosure scheme seeks to promote transparency in political financing. The ability to obtain voluntary compliance of the willing is reliant partially on the deterrent effect that the existence of penalties for wrongdoing is intended to have, but also on the relationship used to educate, encourage and equip them to meet their obligations in an effective and efficient manner. In devising strategies to effect the relationship-building and educative component in administering the Commonwealth disclosure and compliance scheme, recognition of the close conceptual integration between the aspects of the scheme (that is, party registration, disclosure and compliance) is important.

3.16. The process of obtaining compliance with the Commonwealth disclosure and compliance scheme in the Electoral Act can be separated into three steps that accord with the legislative themes across Parts XI and XX of the legislation. The payment of election funding is not considered here as it is a function that is only performed following an election:

- Registration of a political party and the accompanying appointment of office bearers. Once the party has been registered the relationship between the

Commission and the political party commences at the point at which office bearers are changed;

- Contacting and liaising with stakeholders to inform them of their disclosure obligations and to obtain lodgement of a disclosure return that contains all items required under the legislation; and
- Ensuring that the information is complete and accurate and that all information has been disclosed.

- 3.17. The report recommends a more targeted use of the compliance powers available to the Commission. A serious attempt at administering the legislation in an holistic manner and ‘relationship building’ with clients means the targeted, focused and ‘individualised’ approach needs to permeate the whole section’s business and not just parts of it.
- 3.18. For example, the current approach to contacting clients in FAD is to use template letters that are not significantly tailored or amended on an individual basis. Template letters are very useful for the disclosure, compliance and party registration areas when sending bulk correspondence informing people that they have a disclosure obligation, issuing a notice under section 316(2A) or informing a person that they have been successfully appointed as an office bearer of a political party and other administrative matters.
- 3.19. The Director of the compliance area stated that his staff contact clients via phone prior to issuing a notice under section 316(2A) to discuss the process of the review, timeframes and other issues and use this information to tailor letters to the client. Likewise, the Director of the Disclosure and Party Registration section stated that her two areas included where relevant and possible, include information on each of the subject areas in correspondence.
- 3.20. However, it is clear that the development of processes to manage the use of information and knowledge gathered through interactions with clients to influence the nature of contact and information conveyed in correspondence in *all* areas of FAD (for example, through increased tailoring of template correspondence on disclosure, compliance *and* party registration matters to target specific issues within particular parties regarding the meeting of a disclosure obligation) is one way in which *all* areas of FAD could collaborate with each other to a much greater extent to improve outcomes.

Collaboration when a new political party is registered or a new office bearer is appointed

- 3.21. The first point of contact that the FAD section has with a political party is through its office bearers (usually the secretary and/or party agent) at the point the party is registered.
- 3.22. The party registration area already sends information about annual disclosure and compliance reviews to party office bearers when a party is first registered. A brief reference is made to the disclosure obligation, the electronic lodgement facility, compliance reviews and the guides to assist with meeting the disclosure obligation. The letter to a new party agent upon their appointment includes information about the disclosure obligation, reference to the electronic lodgement system and guides but is considerably less detailed than the letter to a newly registered political party.
- 3.23. An initial suggestion could be that the contents in letters to a new party agent of a newly registered political party are made more similar as far as is relevant. The party registration team could also liaise with the disclosure and compliance areas to obtain specific information from the other teams' perspectives that would be useful to communicate to a newly registered political party or to a new office bearer upon their appointment. The letter used for each purpose could also assist in FAD playing a more proactive role in stakeholder education and engagement by including reference to:
- An offer to provide on-site assistance or do a presentation on the nature of the disclosure obligation and the use of the electronic lodgement system to help boost the poor uptake rates to date and proactively engage with the stakeholders;
 - Where a new office bearer is concerned, a reference to any specific information in the party's compliance record, such as consistent late lodgement, consistent omission of particular information on disclosure returns, accompanied by an offer to provide assistance to help and a reminder of any penalties; and
 - Information about the types of financial records that would be useful to maintain to allow for the timely lodgement of annual returns and to allow for compliance reviews to be performed in as short as possible a timeframe and an offer to provide on-site assistance or a presentation in this respect. There is reference to the need to keep records to meet the financial disclosure obligation but there are no specific details in this respect.
- 3.24. The disclosure section and compliance section could then follow-up this initial contact with a phone-call or other additional contact and work together to meet the political party's request.

3.25. The Director of the compliance area asserted that he and his staff have conducted presentations on disclosure and compliance matters in combination with ‘exit interviews’ as part of a compliance review. However this practice is seemingly reactive rather than proactive and there is room for broader application throughout the areas that comprise the FAD section.

Collaboration when stakeholders are informed of their disclosure obligations

3.26. The information listed above could also be reiterated in the letters outlining the disclosure obligations of clients as well as in the reminder letter that is sent as the statutory deadline is approaching. Overall the information in letters sent out when a party is first registered, when a new party agent is appointed and when clients are informed of their disclosure obligation the information should be consistent as far as is possible and relevant. Correspondence should also include information about all areas of FAD business. For example, the letter sent to political parties informing them of their financial disclosure obligations currently makes no mention of the fact that they may be subject to a compliance review.

3.27. Mechanisms would need to be put into place to manage this and to guide the use of information on past history with meeting disclosure obligations.

Collaboration in the administration of the compliance scheme

3.28. In a practical sense, the disclosure area has considerable interaction with the clients until the point at which the statutory deadline approaches and clients lodge their returns. The contact often continues after the return is lodged to ensure it includes all the legislatively required information.

3.29. In many cases, staff in the disclosure area have the opportunity to obtain familiarity with the office bearers and the nature of the organisation in a manner that the compliance area do not experience. The information and insight the disclosure team obtain would be particularly useful to the compliance team in formulating their strategies and informing the determination of their review ‘targets’ if a more targeted approach to the use of section 316(2A) is taken.

3.30. For example, if the disclosure team encounters a political party or associated entity that is particularly resistant to meeting its disclosure obligation or appears to purposely omit legislatively required information, this may warrant consideration of their inclusion in compliance review targeting.

3.31. Additionally, an important process that the disclosure section undertake each year involves writing to political parties to ask them to ‘declare’ their associated entities.⁴⁹

⁴⁹ This is an administrative measure undertaken by the disclosure area – there is no specific power in the Electoral Act to compel political parties to respond to such a request.

- 3.32. The Director of the disclosure area stated that this was not a precise exercise because many political parties were not aware of any or all of their associated entities, but that there was still value in the process to use the information received at least as a guide to attempt to reach all associated entities that may have a disclosure obligation.
- 3.33. Section 316(3A) of the Electoral Act confers upon the Commission the power to compel documents and other forms of evidence to determine whether a body is an associated entity under the legislation. It seems that the information gathered by the disclosure section, while not completely determinative, would be useful for the compliance area in determining whether the exercise of the section 316(3A) power is necessary.

Collaboration in enhancing the FAD educative role

- 3.34. This more proactive and targeted model of administering the disclosure and compliance function needs to be complemented by an enhanced educative component as a part of the section's business. One potential option for enhanced educative measures to encourage voluntary compliance with the scheme could involve (in addition to the proactive measures outlined above) developing a strategy to engage political parties in the distribution of short summaries of disclosure obligations (developed by the FAD section) to people, organisations and other bodies that make donations to them.⁵⁰ This would assist with building a relationship with some clients outside of the standard obligation letter sent annually which could potentially improve understanding of the obligations and assist with compliance.
- 3.35. The development of an engagement and communications strategy is an important first step in implementing these measures. Such a strategy needs to be developed collaboratively involving all areas that comprise the FAD section to ensure its effectiveness and it must be a whole of section priority for it to achieve its ends.
- 3.36. The matters discussed above are in no means an exhaustive list of the ways in which the section can better collaborate. However, it does seem clear that closer integration and collaboration between the areas would significantly increase capability in terms of effectively administering the Commonwealth disclosure and compliance scheme.

⁵⁰ The precise approach and model to be used here requires careful consideration. Some NSW political parties issue receipts to their donors that have information on the disclosure obligation printed on them. A similar concept could be pursued at the federal level.

The FAD IT System

3.37. In approximately early 2009 the Director of the Disclosure section initiated a project to develop and implement an online lodgement system for those with disclosure obligations. The IT system also includes a work management system for FAD staff intended to be used for their day-to-day tasks.

3.38. During the course of the review, it also became clear that the main internal users of the new IT system were junior staff in the disclosure area. Outside of this, the take-up within the FAD as a whole has been also low.

3.39. Accordingly, there are two separate issues where encouraging use of the IT system is concerned:

- Encouraging take-up by external stakeholders such as political parties, associated entities and donors (this issue needs to be addressed through a concerted effort by the section and the development of workable strategies and policies).
 - The take-up of the online lodgement system by those with disclosure obligations was initially low, and is now reportedly sitting at approximately 45-50% with each year showing an increase in the use of this facility;
 - If legislative changes in the area of disclosure and compliance, current and proposed, are passed, there will be a clear move to electronic lodgement purely because the frequency of disclosure means the legislation cannot be administered without this. An additional measure that would assist in the other issue of encouraging take-up by key stakeholders of the electronic lodgement facility would be to legislatively provide that electronic lodgement was compulsory.
- Encouraging take-up by internal FAD staff.

3.40. The reasons for the poor take-up of the new work management system internally are many and varied. Some reasons that were cited during the review follow:

- Staff in the compliance area indicated that their reluctance to use the IT system stemmed from a belief that their needs were not prioritised when the system was developed. The Directors of the section said that this was a budgetary decision. \$2.3 million has now been spent on developing the system with some compliance features having been incorporated.
- It was also stated that the compliance area has two existing systems/software packages necessary for their work. To then be required to use a third system to fit in with the disclosure area was impractical for their needs.

- 3.41. The audit report by PwC indicates that there is potentially a duplication of effort in some compliance activities due to different software and computer systems and methodology being used by the three areas that make up the Funding and Disclosure Section. The compliance area are still using Microsoft Excel spread sheets and re-keying some financial information they receive from those they review, which adds to their workload.
- 3.42. Some compliance staff have started using the system but are still under-skilled in its use. The disclosure staff members stated that since the system went live in July 2010, there have been ‘three or four’ training sessions for compliance staff.
- 3.43. If the Commission implements the recommendation in this report for a dedicated branch head position to oversee the Funding and Disclosure function, a key responsibility will be to oversight and drive a change management process to achieve unanimity in relation to the IT system functionality and future development to meet joint and individual needs of all three areas of the new FAD branch.
- 3.44. This unanimity can be achieved through some initial steps.
- 3.45. The Director of the compliance area highlighted that section 316(2D) of the Electoral Act, which requires that an ‘investigation’ be conducted of gifts of \$25 000 or more, was applied ‘incidentally’ as a part of compliance procedures in applying section 316(2A). A step in the compliance teams processes involves extracting a ‘donor discrepancy report’ from the current IT system which shows every ‘mismatch’ between disclosures of donors and those of political parties and associated entities. He stated that the compliance area follows up all discrepancies both above and below \$25 000. However, he also indicated that the report brought up erroneous data and required enhancement to remove this to be fully useful to the compliance area. This could be an area of focus and an opportunity for initial engagement and collaboration between two of the FAD areas to achieve a common end.
- 3.46. Despite the ‘incidental’ description of the nature of the checks undertaken of gifts of \$25 000 or more as part of the electronic matching that occurs as a matter of course with all disclosure returns and the specific follow-up of all that indicate ‘mismatches’, this process meets in a minimum fashion the ‘investigation’ obligation in section 316(2D).⁵¹
- 3.47. A second, more fundamental step in this respect is for staff in the area to be involved closely with putting together a new list of IT requirements that reflect a more integrated model of operations.

⁵¹ Senator The Hon. John Faulkner has stated that an ‘audit process’ under section 316(2D) would be straightforward, as the processes outlined above appear to be. See further Senator The Hon. John Faulkner, ‘In Committee Speech’, 18 September 2002, Accessed from http://parlinfo.aph.gov.au/parlInfo/genpdf/chamber/hansards/2002-09-18/0013/hansard_frag.pdf;fileType=application%2Fpdf

Part 4: PricewaterhouseCoopers report