Federal Election Commission

Performance and Accountability Report
Fiscal Year 2007

FEDERAL ELECTION COMMISSION

Performance and Accountability Report
Fiscal Year 2007

Released November 2007

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(cont.)

Message From The Chairman

November 15, 2007

I am pleased to present the Federal Election Commission's (FEC) Performance and Accountability Report for fiscal year 2007, as required by the Accountability of Tax Dollars Act of 2002. The Commission received an unqualified opinion from its outside auditors on the agency's 2007 annual financial statements. This is a significant improvement over the Commission's prior years' performance. This improvement reflects a commitment by the Commissioners and staff of this agency to ensure that our internal controls are adequate to safeguard the tax dollars with which we have been entrusted.

As the 2008 Presidential election nears, we are reminded of the importance of our goal: to effectively and fairly administer the federal campaign finance laws. The FEC applies three objectives – transparency, enforcement, and development of the law – to achieve its goal. The strategies to achieve these objectives are outlined in our Strategic Plan.

The financial and performance data presented in this report are reliable, accurate, and complete. Section I of this report provides an overview of the FEC's mission and accomplishments. The FEC's financial and performance data is more fully discussed in Sections II and III. We are continually assessing the efficiency and effectiveness of the Commission's processes and when we perceive a way to improve our operations, we are committed to working to implement those improvements. Accordingly, the FEC is committed to the continued improvement of its management and fiscal processes, and the resolution of the remaining weaknesses identified by the Inspector General and our auditors, Clifton Gunderson, LLP. These items are discussed in Section III of this report.

The FEC places a high priority on sound financial management, information technology, human resources, and administrative support services. The FY 2007 Performance and Accountability Report demonstrates how well the FEC performed during the year and highlights our commitment to providing the high level service the regulatory community expects and deserves from the Federal Election Commission. I am very pleased to be able to share the Commission's progress with all of our stakeholders. We believe that given the path we are on, we will be able to report more success in the years ahead.

Sincerely,

Robert D. Lenhard
Chairman

How To Use This Report

This Performance and Accountability Report (PAR) presents comprehensive performance and financial information on the Federal Election Commission's ("FEC" or "Commission") operations. The report was prepared pursuant to the *Accountability of Tax Dollars Act of 2002* and Office of Management and Budget (OMB) Circular A-136, revised, *Financial Reporting Requirements,* and covers activities from October 1, 2006 through September 30, 2007.

The FEC places a high importance on keeping the public informed of its activities. To learn more about who we are and what we do to serve the American public, visit FEC's website at www.fec.gov to access this report (click on "About the FEC" and then "Budget").

The FY 2007 Performance and Accountability Report is organized into four sections:

Section I – Management's Discussion and Analysis (MD&A) provides an overview of the FEC. It describes our mission, organizational structure and regulatory responsibility.

Section II – Performance Information summarizes the FEC's strategic goal and related objectives and provides a forward-looking discussion of future challenges.

Section III – Financial Information, including Auditor's Report details the FEC's financial performance by highlighting the financial position, audit results and describing the FEC's compliance with key legal and regulatory requirements.

Section IV – Other Accompanying Information includes the agency's Inspector General's assessment of the FEC's management challenges.

Appendix A – List of Acronyms

SECTION I

Management's Discussion and Analysis

Section I.A – Mission and Organizational Structure

The Commission was created in 1975 as an independent regulatory agency to strengthen the integrity of the electoral process under the *Federal Election Campaign Act* (*FECA*) *of 1971*, 2 U.S.C. 431 *et seq.*, as amended by the *Bipartisan Campaign Reform Act* of 2002 (*BCRA*), P.L. 107–155 (the *Act*). The Commission is also responsible for administering the public funding program for Presidential campaigns and conventions, as outlined in Title 26 Internal Revenue Code.

The *Act* provides the foundation of the FEC's mission to **"prevent corruption in the federal campaign process by administering, enforcing and formulating policy with respect to federal campaign finance statutes."** The primary objectives of the FEC are to: (1) disclose campaign finance information; (2) educate stakeholders and enforce the provisions of the *Act* such as the limits and prohibitions on contributions; and (3) interpret and administer the *Act*.

The FEC Today

The FEC strives to foster compliance with the rules of the federal campaign process by administering, enforcing and formulating policy with respect to federal campaign finance statutes. It is headquartered in Washington, DC and does not have any regional offices. The FEC's authorized funding and staffing levels for fiscal year (FY) 2007 were $54.8 million and 375 full-time equivalent (FTE) positions. This amount was a slight increase from FY 2006, where the funding was authorized at $54.2 million and 375 FTE. The FEC is funded primarily by a single annual appropriation for salaries and expenses. The FEC is also authorized to collect fees to offset the costs of its conferences.

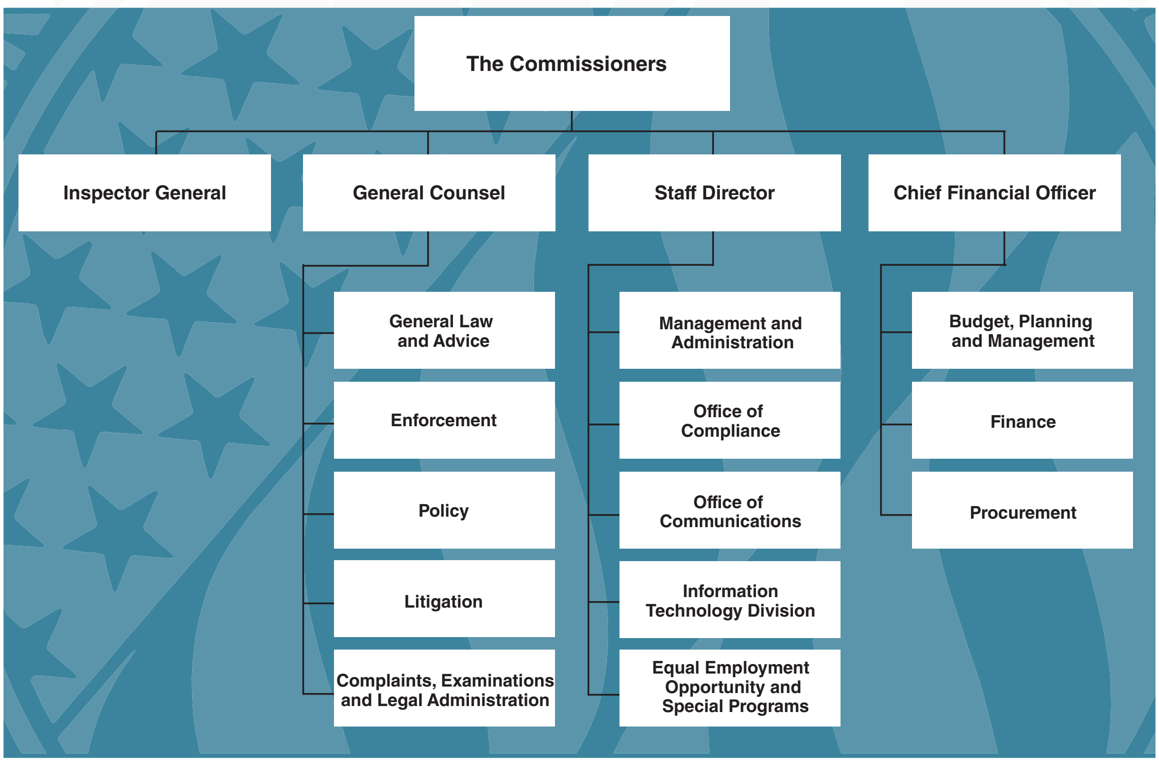
How the FEC is Organized

The FEC is structured to foster bipartisan decision-making. To accomplish its legislative mandate, the FEC is directed by six Commissioners, who are appointed by the President with the advice and consent of the Senate. By law, no more than three Commissioners can be members of the same political party. Each member serves a six-year term and two seats are subject to appointment every two years. The Chairmanship of the Commission rotates among the members, with no member serving as Chairman more than once during his or her term. The Commissioners meet regularly to formulate policy and to vote on significant legal and administrative matters. The *Act* requires at least four votes for the Commission to adopt any official action or policy.

The Offices of the Chief Financial Officer, General Counsel, and Staff Director support the agency in accomplishing its mission. During FY 2007, the FEC restructured to align its divisions and offices to operate more effectively and efficiently. The restructuring included the addition of the Deputy Staff Director for Management and Administration, and the Chief Communications Officer. The Commission also realigned the Chief Financial Officer (CFO) to report directly to the Commission. These changes were made to afford the Commission a higher level of oversight of management throughout the agency; thereby increasing objectivity and strengthening internal controls.

The Office of the Inspector General, established within the FEC in 1988 under amendments to the *Inspector General Act*, is independent and reports to both the Commissioners and the Congress. The FEC's Inspector General has two major responsibilities: (1) to conduct audits and investigations to detect fraud, waste and abuse within the agency; and (2) to improve the economy and effectiveness of agency operations. The Inspector General is required to report its activities to Congress on a semiannual basis. These reports include descriptions of any serious problems or deficiencies in agency operations, as well as corrective actions taken by the agency.

The specific roles and responsibilities of each office are described in greater detail at http://www.fec.gov/about.shtml. The following chart represents the organizational structure as of September 30, 2007.



As illustrated in the organizational chart above, the FEC is structured to administer the *FECA* effectively and efficiently. The FEC's primary objectives in administering the *FECA* are to disclose campaign finance information, enforce the law, and interpret and administer the provisions of the law, including administering the public funding of Presidential elections. The following provides a summary of the activities performed by the agency to ensure these objectives are achieved.

Disclosing Campaign Financing

One of the most important responsibilities of the FEC's Office of Communications is to make available to the public campaign finance reports disclosing the sources and amounts of funds used to finance federal elections. These reports are accessible through the FEC's website at http://www.fec.gov/finance/disclosure.shtml. By providing easy, online access to disclosure reports, the FEC provides an added incentive for the regulated community to comply with the campaign finance law. The Office of Communications consists of the following offices/divisions:

(1) Information Division; (2) Public Disclosure Division; (3) Press Office; and (4) Congressional, Legislative and Intergovernmental Affairs. While the Commission continues to make available printed copies of reports, brochures and publications, they are also available on FEC's website.

In addition to making campaign finance reports available to the public, the FEC works to ensure that the information disclosed is accurate and complete. The Office of Compliance's Reports and Analysis Division (RAD) reviews all reports to track compliance with the law and to ensure that the public record provides a full and accurate representation of campaign finance activity. If the FEC's review of the report identifies an apparent violation or raises questions about the information disclosed on a report, the Commission sends a request for additional information (RFAI) to the committee, affording the committee an opportunity to correct the public record, if necessary. If the committee is able to resolve the FEC's concerns, it may avoid an enforcement action. Should the committee not sufficiently address the FEC's concerns, the FEC begins its enforcement efforts on the apparent violation.

Education and Enforcement

Encouraging Compliance

Helping the regulated community understand their obligations under the *Act* is an essential component of improving voluntary compliance. In recent years, the Commission's website has become the single-most important source of instantly accessible information about the *Act* and Commission regulations. Members of the regulated community and the general public can use the website to track Commission rulemakings, search advisory opinions and closed enforcement matters, view campaign finance data and find reporting dates. Moreover, while the Commission continues to make available printed copies of its educational brochures and publications, these materials are available and easy to access on the FEC's website along with other instructional information, such as the FEC's *Tips for Treasurers*.

The Commission also encourages voluntary compliance through a number of activities including outreach programs. The FEC hosts instructional conferences in Washington, DC, and in other cities across the country, where Commissioners and staff explain how the *Act* applies to candidates and political committees. These conferences specifically address recent changes in the campaign finance laws and focus on fundraising and reporting regulations. Additionally, the Commission responds to telephone inquiries and written requests from political committees seeking information about the law and assistance in filing disclosure reports.

Enforcement of the FECA

The FEC has exclusive jurisdiction over civil enforcement of violations of the *Act* and coordinates with the Department of Justice, as appropriate, on matters involving both civil and criminal enforcement of the *Act*. Under the Commission's traditional enforcement program, the Commission learns of possible election law violations primarily through:

- The complaint process, whereby anyone may file a sworn complaint alleging violations of the *Act*;
- The Commission's review of a committee's reports or through a Commission audit;
- Voluntary self-reporting, sua sponte, by a candidate or political committee representative who believes that they may have violated the *Act*; and
- The referral process, whereby other government agencies may refer possible violations of the *Act* to the FEC.

Whether initiated by outside complaint or internal referral, the most complex and legally significant enforcement matters are handled by the Office of General Counsel (OGC).

Specifically, the Enforcement Division, within the OGC:

- Recommends to the Commission whether to find "reason to believe" that the *Act* has been violated, a finding that formally initiates an investigation;
- Investigates potential violations of the *Act* by requesting, subpoenaing, and reviewing documents and interviewing and deposing witnesses;
- Conducts settlement negotiations on behalf of the Commission to reach conciliation agreements with respondents;
- Recommends to the Commission whether to find "probable cause" to believe the *Act* has been violated; and
- Recommends to the Commission whether to sue a respondent in federal district court if conciliation cannot be reached.

Although swift resolution of enforcement matters is one of the highest priorities for the Commission, efficiency cannot come at the expense of fairness to the regulated community. Accordingly, the Commission remains focused on providing respondents with a fair opportunity to make appropriate presentations to the Commission on enforcement matters.

Other FEC Enforcement Programs

To augment OGC's enforcement role, the Office of Compliance manages several programs to improve the efficiency and effectiveness of the Commission's enforcement efforts. These programs include: (1) Administrative Fine; (2) Alternative Dispute Resolution; and (3) Audit. The following provides a summary of each of these programs.

The Administrative Fine (AF) program, implemented in July 2000, helps the Commission enforce the timely filing of financial disclosure reports in a more streamlined manner than the traditional enforcement process. This program, which is administered by the Office of Compliance's Office of Administrative Review (OAR) and RAD, assess monetary penalties for late and non-filed reports.

The Alternative Dispute Resolution (ADR) program, implemented in October 2001, is designed to promote compliance with the *Act* by encouraging settlements outside the traditional enforcement or litigation processes. The ADR program aims to expedite resolution of certain less complex enforcement matters and to reduce the cost of processing complaints through streamlined procedures. The ADR program is also aimed at promoting future compliance through settlements reflecting primarily remedial measures for candidates and political committees, such as training, audits and the hiring of compliance staff.

Additionally, the Commission enforces the *Act* through audits of candidates and political committees. The Commission conducts "for cause" audits, under Title 2, in those cases where political committees have failed to meet the threshold requirements for substantial compliance with the *Act* and have voluntarily failed to correct errors or omissions in their disclosure reports. In addition, the Commission conducts mandatory audits, under Title 26, as discussed in the section on Public Funding. The Commission's audit presence not only contributes to its enforcement efforts, but also encourages voluntary compliance within the regulated community.

Development of the Law

In fulfilling its statutory mission, the Commission often finds itself in a delicate balancing act. On the one hand, the Commission must administer, interpret and enforce the *Federal Election Campaign Act*, which the Supreme Court has said serves a compelling governmental interest. On the other hand, the Commission must remain mindful of the constitutional freedom of speech and association, and the practical implication of its actions. These tensions between valid governmental interests and certain constitutional guarantees were keenly evident in the significant litigation involving the Commission.

To further its outreach and responsiveness to the public and regulated community, the Commission provides formal interpretation of the *Act* by promulgating regulations and issuing advisory opinions (AOs). Specifically, the Commission issues AOs to clarify how the statute and regulations apply to real-life situations brought to the Commission by candidates, political committees and others in the regulated community. Although the *Act* allows the agency 60 days to respond to most requests, the Commission has placed special emphasis in the last year on expediting its processing and consideration of AO requests.

Furthermore, Congressional action, judicial decisions, petitions for rulemaking or other changes in campaign finance law often necessitate that the Commission update or adopt new regulations. Consequently, the FEC undertakes rulemakings either to write new Commission regulations or revise existing regulations.

Funding Presidential Elections

Public Funding

The Commission's responsibilities also include administering the public funding of Presidential elections, as outlined in 26 U.S.C. Although this program is administered by the FEC, it is funded by dollars voluntarily checked off by taxpayers on their income tax returns. Since 1993, the taxpayer check-off amount has been $3 per return. These monies are collected by the Internal Revenue Service (IRS) and maintained by the U.S. Treasury. Also, the Treasury is responsible for the accounting and reporting of these funds. Through the public funding program, the federal government provides: (1) matching funds to candidates seeking their party's Presidential nomination; (2) financing for Presidential nominating conventions; and (3) grants to Presidential nominees for the general election campaigns.

Under the Presidential public funding program, the Commission: (1) determines a candidate's eligibility to participate in the program, (2) certifies the amount of public funds to which the candidate or convention committee is entitled; and (3) conducts a thorough examination and audit of the qualified campaign expenses of every candidate who receives payments under the program.

Section I.B – FEC Performance Goals, Objectives, and Results

In addition to the previously discussed restructuring, the FEC also updated its strategic plan during FY 2007. Changes to the FEC's strategic plan were driven by two primary considerations. First, the FEC's previous strategic plan did not reflect current FEC operations. Second, the plan did not fully address reporting requirements under the *Government Performance and Results Act* (GPRA), as emphasized by the OMB under the Performance Assessment Rating Tool (PART) process. The revised strategic plan defines more clearly the FEC's objectives and consolidates its strategic goals into one primary goal.

The revised strategic plan also incorporates the means and strategies used to achieve the strategic goal, which includes: (1) operational processes; (2) the development and use of technologies; and (3) human resources. The revised strategic plan developed long-term and annual performance goals to improve accountability and better align performance to the strategic goal.

Based on the revisions to the strategic plan, this report aligns the FEC's reporting requirements, under GPRA and OMB Circular A-136. The revised strategic plan was also the basis for the structuring of the FY 2009 budget request. The revised strategic plan served as the foundation with respect to implementing and achieving the strategic goal and objectives for the year. Given the revisions to the strategic plan, the format of the Statement of Net Cost was revised. Accordingly, FEC's results and accomplishments relate to a single goal and the related costs are reflected under one program on the Statement of Net Cost (see Section III).

The revised strategic plan is currently under review by the Commission. Final approval is expected during the first quarter of FY 2008.

The FEC has one primary strategic goal – **To protect the integrity of the federal campaign process by providing transparency, enforcing contribution restrictions, and fairly administering the FECA and related statutes**. This goal is pursued by three strategic objectives and by underlying activities that guided the FEC's operations during FY 2007. The strategic objectives are:

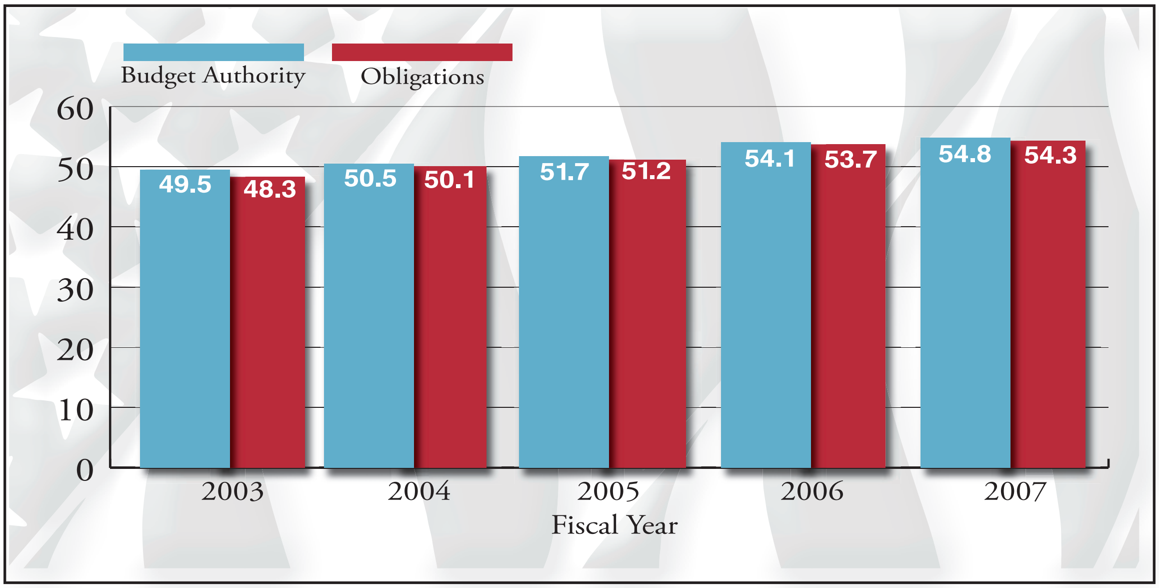
- **Transparency** – Receiving Accurate and Complete Campaign Finance Disclosure Reports and Making Them Available to the Public
- **Compliance** – Education and Enforcement
- **Development of the Law** – Interpreting and Administering the *Act*

Sources of Funds

The FEC receives an annual appropriation for Salaries and Expenses. In FY 2007, the appropriation was $54.5 million. In addition, the FEC is authorized to collect registration fees for the costs of carrying out FEC-hosted conferences. These amounts, which were estimated at $300,000, represent offsetting collections and are included in the FEC's authorized funding level (i.e., budget authority).

The FEC's total budget authority level in FY 2007 was $54.8 million. Figure 1 shows the agency's funding and obligations from FY 2003 to 2007.

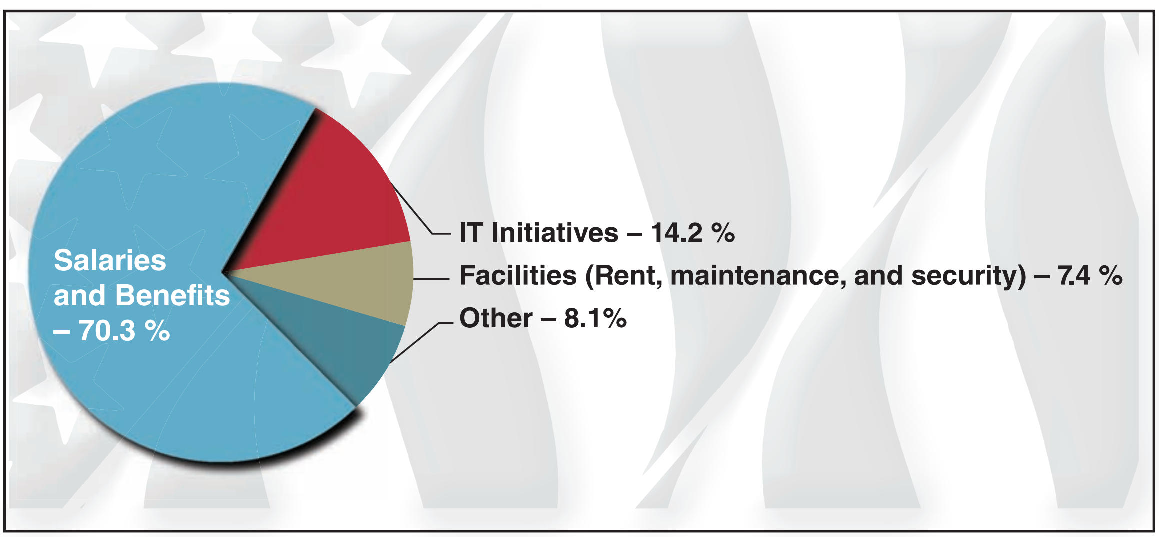
Figure 1 – Summary of Funding (in millions)



Personnel vs. Non-Personnel Costs

Figure 2 represents the Commission's actual expenditures broken out between personnel and non-personnel costs for FY 2007. Personnel costs comprised 70.3 percent of the FEC's costs; the other 29.7 percent was spent primarily on building rent, capital items and information technology (IT) software and hardware.

Figure 2 – Fiscal Year 2007 Costs by Major Category



The remainder of this section provides a summary of the results of FEC's key performance objectives, which are discussed in greater detail in Section II of this report.

Summary of Significant Performance Results

The FEC actively communicates its experience and expertise to interested individuals, political committees, and state and local governments. The FEC achieved its goal of conducting educational campaign finance conferences and seminars throughout the U.S. and anticipates expanding its outreach efforts in the future.

Disclosing campaign finance information of federal elections is a key responsibility of the FEC. The FEC continues to encounter an increase in the number of filings related to Congressional and Presidential elections, which occur in even-numbered calendar years. Despite the continued growth in the number of filings and information related to the filings, the FEC made 98.5 percent of these filings available to the public within 48 hours of receipt, just shy of its 100 percent goal. The portion of the filings that were not processed within the 48 hours is attributed, in part, to the extended processing time for paper filings, thereby preventing the achievement of this goal.

In addition to making campaign finance data readily available to the public, the FEC reviews all reports, amendments and statements for accuracy, completeness and compliance with the law. New and amended reports for the current and past elections are received at the Commission on a daily basis. In FY 2007, the Commission reviewed 55,748 reports, 73 percent of which were reviewed within 90 days of the date received. The Commission's performance goal is to review 60 percent of reports within 90 days of receipt. The Commission exceeded its performance goal by 13 percent in FY 2007. Because of the 90-day processing period and the fact that a filing deadline falls ten days before the end of the fiscal year, a small percentage of reports received in a fiscal year cannot be reviewed before that fiscal year ends. In FY 2007, this was 3.7 percent (see Figure 6 in Section II). Although the Commission does review 100 percent of all filings received, when the fiscal-year-end performance measure was developed there was no meaningful time-related goal associated with it. The FEC is in the process of updating its strategic plan to incorporate a more accurate, time-related goal.

The results of the review of the filings fall, generally, into the following categories:

- No instance of non-compliance;
- Request for Additional Information (RFAI); or
- Non-compliance is noted. In this case, the matter of non-compliance is referred to ADR, OGC or Audit for further consideration.

The outcome of the FEC's enforcement efforts resulted in the Commission assessing a total of $4.37 million in fines and civil penalties in FY 2007. Although this is a 25.8 percent decrease from FY 2006, this amount reflects the FEC's continued efforts in enforcing the *FECA*, while also highlighting the fact that there is a continued need to educate the regulatory community about the *Act*'s requirements.

Another focus of the FEC has been to address enforcement "matters under review" more quickly and in greater numbers. The FEC established a goal of having at least 50 percent of its cases in "active" status, meaning that the complaint has been assigned to an attorney for review. OGC exceeded this goal for "active" status cases by achieving an average rate of 88 percent as of September 30, 2007.

With respect to the number of cases closed, OGC established a goal to close 75 to 100 enforcement cases per year, requiring no more than 40 percent be closed through dismissal. The OGC achieved this goal by closing 160 cases, 39 percent of which were dismissed. With respect to the agency as a whole, the number of cases closed from FY 2006 to FY 2007 increased by 220, representing a 79.4 percent improvement (see Figure 9 in Section II). The increase can be attributed to many factors, including the significant emphasis that the Commission placed on the review process to improve the FEC's ability to process cases more timely. Another major factor relates to the AF and ADR programs handling of the less-complex cases, which not only improved the timeliness of addressing the cases, but also reduced the number of cases that may have previously been dismissed by OGC.

Additional enforcement efforts included completing 25 audits this fiscal year, which consisted of seven Presidential campaign and convention committee audits and 18 "for cause" audits. Title 26 Presidential audits, which are mandatory, demand more time and resources than Title 2 "for cause" audits because of their complexity and the scope of the audit. The number of Title 2 audits depends upon the number of referrals received by RAD as a result of its review of each filing. This pace is on schedule to meet the two-year goal of 40 to 45 Title 2 audits per election cycle. One factor that might preclude the FEC from obtaining its goal is that, by statute, audits of candidates that participate in the Public Funding program take precedence over Title 2 audits.

The FEC did not meet its goal of completing all Presidential audits within two years of the 2004 Presidential election. Out of the 15 audits related to that election, six (40%) were completed within the two-year timeframe. As of September 30, 2007, of the remaining nine audits, seven had been completed, leaving two outstanding. Presidential audits are extremely complex. There has been an increase in the volume of expenditures, which impacted the scope and length of time it took to complete these audits.

Federal election law permits all eligible national committees of major and minor parties to receive public funds to help pay the official costs of their Presidential nominating conventions. Consistent with its goal, the FEC certified payment for each of the two major political parties' convention committees in a timely and accurate manner. The initial payments of $16,356,000 were made in July 2007 for planning and conducting the 2008 Presidential nominating conventions. Thus far in the 2008 Presidential election cycle, the Commission has certified two candidates for eligibility under the Primary Matching Fund program, and anticipates that a number of other candidates will apply for Public Funding. This expectation is based on inquiries received from several committees.

Section I.C – Analysis of FEC Financial Statements and Stewardship Information

The FEC's FY 2007 financial statements and notes are presented in the required format in accordance with OMB Circular A-136, revised, *Financial Reporting Requirements*. The FEC's current year financial statements and notes are presented in a comparative format.

The following table summarizes the significant changes in the FEC's financial position during FY 2007.

Net Financial Condition	FY 2007	FY 2006	Increase/ (Decrease)	% Change
Assets	$18,819,667	$19,346,109	($526,442)	(2.7%)
Liabilities	$5,125,513	$5,248,940	($123,427)	(2.4%)
Net Position	$13,694,154	$14,097,169	($403,015)	(2.9%)
Net Cost	$56,377,561	$55,906,556	$471,005	.8%
Budgetary Resources	$57,295,859	$56,527,231	$768,628	1.4%
Custodial Revenue	$5,031,538	$6,602,398	($1,570,860)	(23.8%)

The following is a brief description of the nature of each required financial statement and its relevance. Certain significant balances or conditions are explained to elaborate on the impact on the FEC's operations.

Balance Sheet

The Balance Sheet presents the total amounts available for use by the FEC (assets) against the amounts owed (liabilities) and amounts that comprise the difference (Net Position). As a small independent agency, about 96 percent of the FEC's assets consist of Fund Balance with Treasury (FBWT) and Property and Equipment (P&E). Fund Balance with Treasury (e.g., Cash) is available through the Department of Treasury accounts from which the FEC is authorized to make expenditures (i.e., obligations) and payments. FBWT increased by about $182,000, or 1.8 percent, from FY 2006, largely due to obligations incurred in the fiscal year but not paid as of September 30, 2007. P&E consists of capitalized property. Net P&E decreased by approximately $1.0 million, or 11.6 percent, from FY 2006. The decrease is primarily due to the timing of when the leasehold improvements were capitalized and the expiration of the FEC's lease on September 30, 2007. The expiration of the lease accelerated the depreciation of the remaining balance associated with leasehold improvements, bringing the net book value of leasehold improvements from $1.3 million in FY 2006 to zero in FY 2007.

Finally, accounts receivable increased from FY 2006 by approximately $300,000 primarily due to the assessment of one penalty occurring at the end of FY 2007.

Statement of Net Cost

The Statement of Net Cost presents the annual cost of operating FEC programs. Gross costs less any earned revenue is used to arrive at the total net cost of operations. The FEC's total budget in FY 2007 was $54.8 million. Roughly $38.2 million, or 70 percent, of the budget was dedicated to personnel costs. The remaining costs were related to rent, information technology initiatives, and general operating expenses. Overall, costs increased by approximately one percent, which relates primarily to an increase in depreciation expense.

As previously mentioned, and consistent with OMB guidance, the FEC revised the format of the Statement of Net Cost to be consistent with its draft strategic plan. This change affected the presentation of the Statement of Net Cost to reflect one responsibility segment in FY 2007, rather than the three responsibility segments that were reported in FY 2006.

Statement of Changes in Net Position

This statement presents in greater detail the net position section of the Balance Sheet, which includes Cumulative Results of Operations and Unexpended Appropriations. The statement identifies the activity that caused the net position to change during the reporting period. The total net position decreased by approximately $400,000 which is primarily due to an increase in depreciation expense.

Statement of Budgetary Resources

The Statement of Budgetary Resources provides information on the source and status of budgetary resources made available to the FEC during the reporting period. It presents the relationship between budget authority and budget outlays, as well as the reconciliation of obligations to total outlays. Total Budgetary Resources and Status of Budgetary Resources increased by approximately $770,000, or 1.4 percent, over FY 2006. The slight increase is due primarily to the fact that the federal government operated under a full-year continuing resolution (P.L. 110-5), which held funding at the prior year's level while providing for about half the cost of living increase for federal employees in FY 2007.

Statement of Custodial Activity

The Statement of Custodial Activity represents an accounting of funds accrued and collected by the FEC that are owed to the U.S. Treasury's general fund. These monies are not available for FEC's use. Total custodial revenue decreased from the prior year approximately $1.6 million, or 23.8 percent. The decrease is primarily due to one unusually large civil penalty received in FY 2006. The FEC does not maintain any stewardship assets.

Section I.D – Analysis of FEC's Systems, Controls, and Legal Compliance

I.D.i – Management Assurances

The *Federal Managers' Financial Integrity Act (FMFIA) of 1982* is implemented by OMB Circular A-123*,* revised*, Management's Responsibility for Internal Control*. The FEC management is responsible for establishing and maintaining effective internal control and financial management systems that meet the objectives of the *FMFIA* and performing a self-assessment under the guidance of the FEC Directive 53, *Implementation of OMB Circular A-123*, *Internal Control Review*. Directive 53 outlines the process and describes roles and responsibilities for conducting risk assessments and internal control reviews.

Section 2 of the FMFIA requires federal agencies to report, on the basis of annual assessments, any material weaknesses that have been identified in connection with its internal and administrative controls. The reviews that took place during FY 2007 provide reasonable assurance that FEC systems and management controls comply with the requirements of the *FMFIA*. The FEC has no material weaknesses to report for FY 2007 relating to Section 2 of the *FMFIA*.

Section 4 of the FMFIA requires that agencies' financial management systems controls be evaluated annually. The FEC evaluated its financial management systems for the fiscal year ending September 30, 2007 in accordance with the *FMFIA* and OMB Circular No. A-127, *Financial Management Systems*, as applicable. The results of management reviews provide reasonable assurance under Section 4 of the FMFIA that the FEC's financial systems controls generally conform to the principles and standards required.

The FEC conducted its assessment of internal control over the effectiveness and efficiency of operations and compliance with applicable laws and regulations in accordance with OMB Circular A-123 and FEC Directive No. 53. No material weaknesses were identified under the *FMFIA* in recent years by the FEC.

Although there were no material weaknesses identified from the Internal Control Review, several areas for improvement were noted. Managers in all divisions continue to review specific procedures on an ongoing basis and improve internal controls, where possible. As noted in the Chairman's Letter, assurance is given that management controls are in place and the Commission's financial systems conform to government standards articulated in OMB Circulars A-123 and A-136.

FEDERAL ELECTION COMMISSION
WASHINGTON, D.C. 20463

OFFICE OF THE CHAIRMAN

Annual Assurance Statement on Internal Control

The Federal Election Commission (Commission) is responsible for establishing and maintaining effective internal control and financial management systems that meet the objectives of the Federal Managers' Financial Integrity Act (FMFIA), and the Office of Management and Budget (OMB) Circular A-123, *Management's Responsibility for Internal Control*. Internal control is an integral component of the Commission's management that provides reasonable assurance that the following objectives are being achieved: effectiveness and efficiency of operations, reliability of financial reporting, and compliance with applicable laws and regulations.

The Commission conducted its evaluation of internal control over the effectiveness and efficiency of operations and compliance with applicable laws and regulations in accordance with OMB Circular A-123. Based on the results of this evaluation, the Commission provides reasonable assurance that its internal control over the effectiveness and efficiency of operations, and compliance with applicable laws and regulations, as of September 30, 2007, were operating effectively and no material weaknesses were found in the design or operation of these internal controls.

Robert D. Lenhard
Chairman
October 24, 2007

The following table summarizes the results of this year's financial statement audit, performed by FEC's independent auditors, Clifton Gunderson:

Audit Opinion	Unqualified				
Restatement	No				
Material Weaknesses	Beginning Balance	New	Resolved	Consolidated	Ending Balance
Program Cost Allocation	1	0	1	0	0
General Property and Equipment	1	0	1	0	0
Integrated Financial Management System	0	1	0	0	1
Total Material Weaknesses	2	1	2	0	1

In addition to the one material weaknesses, Clifton Gunderson also observed one significant deficiency, as defined by American Institute of Certified Public Accountants (AICPA), Statement on Auditing Standards (SAS) 112: *Communicating Internal Control Related Matters Identified in an Audit*. The FEC is developing a corrective action plan to address the weaknesses identified during the annual audit.

Prompt Payment Act

The *Prompt Payment Act* requires federal agencies to make timely vendor payments and to pay interest penalties when payments are late. The FEC's on-time payment rate for FY 2007 was effectively 100 percent.

Improper Payments Information Act (IPIA) of 2002 Reporting

The *IPIA of 2002* and OMB guidance requires agencies to identify those programs that are susceptible to significant erroneous payments, and determine an annual estimated amount of erroneous payment made in its operations.

The FEC reviewed all of its programs and activities to identify those susceptible to significant erroneous payments. Approximately 70 percent of the FEC's expenditures pertain to salaries and benefits, which represents a low risk for improper payments, based on established internal controls. The FEC recently implemented additional review procedures surrounding its procurement and disbursement processes for non-personnel costs. Accordingly, the FEC is unaware of any improper payments. The FEC continues to monitor and look for additional ways to improve the payment process to ensure that the risk of improper payments remains low.

I.D.ii – Management's Response to the Inspector General's Management and Performance Challenges

Human Capital Management

The Commission is committed to enacting the *President's Management Agenda* (PMA) to make government more citizen-centered, market-based and results-oriented. The FEC has already met the PMA's transparency requirements and is dedicated to maintaining and strengthening its commitment to a diverse federal workforce that is skilled, flexible, and focused on results and service.

The Inspector General's report in Section IV observes that the Commission confronts the same long-standing challenge facing the rest of the federal government: developing and implementing a consistent strategic approach to managing and maintaining an appropriately skilled workforce. To address this challenge, the Commission undertook a comprehensive human capital management initiative. This initiative included changes in recruitment; strategic hiring; and evaluating and training the current workforce. The Commission made strides in succession planning and diversity in the hiring of several senior leaders to fill critical top-level positions.

The FEC also implemented a newly devised performance management system, which better aligns individual performance with the agency's strategic goal and objectives. The new leadership can now develop the Human Capital Strategic Plan. Because of the resulting recognition of its outstanding work in this area, the FEC was invited to participate in a pilot program with the Partnership for Public Service, which promotes public service and fosters excellence in the federal government through its "Best Places to Work" initiative.

Information Technology Security

As the Inspector General points out, computerized systems enable the FEC to carry out its mandate to ensure that the campaign process is fully disclosed. To address the ever-present threats of data misuse, destruction, or inappropriate disclosures, as well as to ensure continuity of operations in the event of a disaster, the Commission has taken aggressive actions to secure its IT infrastructure, such as its mandatory security awareness training program for its employees and contractors. This year, the FEC began several initiatives as security enhancements relating to risk assessments of operations, disaster recovery, and continuity of operations in the event of a disaster.

The FEC remains vigilant in its IT security efforts and continues to monitor and evaluate applicable policies. The agency appreciates the comments and recommendations from the Inspector General on IT security issues.

Financial Reporting

The FEC is committed to producing timely, accurate, and useful financial information, which is essential for making day-to-day operating decisions and managing the government's operations more efficiently and effectively. The FEC is also committed to fully complying with all financial management laws and standards.

The FEC made considerable progress in financial reporting, with many steps taken to improve upon prior years. First, as previously mentioned, the CFO position was restructured to report directly to the Commission. Second, the management and administrative functions previously performed by the CFO were realigned to a newly created position under the Staff Director. Finally, the procurement function was separated from Administration and moved under the CFO. These organizational changes formalized and streamlined reporting processes and empowered the FEC to place more emphasis on financial management, thereby strengthening internal controls.

The FEC has begun the process of replacing its accounting system to meet the demands of the federal government's reporting requirements, including an integrated financial management system. Toward the end of FY 2007, the Commission entered into an agreement with the General Services Administration (GSA), an OMB-certified federal Line of Business (LOB) provider for financial management services. The conversion of financial data is expected to be completed by mid-FY 2008. Achieving this aggressive goal depends, in large part, on the successful development of an electronic interface between the FEC's payroll provider (National Finance Center) and the GSA's financial system.

Although significant progress was achieved in this area, the FEC understands the challenges ahead. In FY 2008, the FEC will continue to work with the Inspector General to eliminate the material weakness and significant deficiency identified as part of the annual audit.

I.D.iii – FEC Integrated Internal Control Framework Legal Compliance

The Commission is subject to numerous legislative and regulatory requirements that promote and support effective internal control. Applicable laws and regulations the FEC adheres to, as applicable, include:

- Annual Appropriation Law – establishes the FEC's budget authority;
- *Inspector General Act of 1978*, as amended (IG Act);
- *Government Performance and Results Act* (GPRA) *of 1993*;
- *Federal Financial Management Improvement Act of 1996* (FFMIA);
- *Clinger-Cohen Act of 1996*;
- *Debt Collection Improvement Act of 1996*, as amended; and
- *Chief Financial Officers (*CFO*) Act*, as amended by the *Accountability of Tax Dollars Act of 2002*.

The proper stewardship of federal resources is a fundamental responsibility of the FEC. These laws help the FEC improve the management of its programs and financial operations, and assure that programs are managed in compliance with applicable law.

Section I.E – Possible Future Effects of Existing Events and Conditions

There are several existing events and conditions that may affect the FEC in the future. Any amendments to the *FECA* may significantly impact the Commission. Amendments to the *Act* may require changes in internal processes or procedures and require that implementing regulations be adopted.

For example, proposed legislation in the House and Senate, if enacted, will significantly affect the FEC in the future. S. 436, the *527 Reform Act of 2005*, amends the *FECA* to clarify when organizations described in section 527 of the *Internal Revenue Code of 1986* must register as political committees. The House has similar legislation pending, H.R. 420, the *527 Reform Act of 2007*. At the end of FY 2007, both bills were still pending in Congress. Two other bills proposing to reorganize the FEC by replacing the six commissioners with one Chairman were also pending.

The solvency of the Presidential Election Campaign (PEC) Fund may impose major burdens on the FEC. For the 2004 elections, eight candidates were certified for matching funds. With the participation of three additional major party candidates, the program could experience severe shortfalls. The PEC Fund is likely to continue to face major deficits in timely payments for the 2008 election. This fund will likely be short of the monies necessary to meet the objectives of the public financing program because primary matching funds will once again be unavailable in the early months of 2008.

The Commission has consistently made legislative recommendations to Congress to address this issue. The FEC is concerned that a totally open primary in both major parties in 2008 (with the presumed participation of a number of candidates in both primaries) will further exacerbate this potential shortfall. At some point, without a legislative remedy, the shortfall may affect payments to general election candidates as well as to primary candidates. The perceived impact of spending ceilings, along with the effects of increased individual contribution limits, has for the first time caused some 2008 candidates to consider refusing the general election grant. This change, while benefiting the PEC Fund balance, would diminish the effectiveness of the program by eliminating one of its major components.

Congressional approval for the AF program has been received through 2008. The Commission is recommending that Congress make permanent the authority for the AF program or provide an extension. If this program is not approved beyond 2008, the Commission's enforcement operations, which have been streamlined as a result of the AF program, could be affected. By making the program permanent, Congress would ensure that the Commission would retain one of the most cost-effective and successful programs in its history.

Section I.F – Other Management Information, Initiatives and Issues

e-Review

The Commission continues to use technology to manage more effectively its ever-increasing workload. One such initiative is the implementation of e-Review, which is a web-based review system that will allow the FEC to review campaign finance reports, generate, circulate and image outgoing RFAI letters to committees, and to provide management with reports detailing key performance metrics. Once fully implemented, it is anticipated that e-Review will better allow the FEC to keep pace with the increasing number, size, and complexity of financial reports submitted by the regulated community.

House and Senate Map

Building on the success of the Presidential Campaign Finance Map which was launched in June 2007, the FEC is building a House and Senate campaign finance research tool based on the same map interface that has made the Presidential Map research tool so successful. The House and Senate Map will be a new addition to the FEC website that uses state and district maps to lead the user to campaign finance data for House and Senate candidates. It allows the user to select candidates for comparison using bar charts to display such financial categories as contribution and disbursement totals, debts and cash on hand. It will also present itemized contributions and disbursements by category and includes links to images of reports filed by the candidate and the candidate's committees.

This application lays the groundwork for similar presentations of political action committee (PAC) and party committee data, contributor histories and historical data for all committee types. In summary, the goal is to provide user-friendly public access to a large, comprehensive database of campaign finance information. These database presentation tools achieve the goal of presenting key disclosure data in an attractive, useful and comprehensible way on the Web.

Intranet

The FEC is also developing an Intranet that will eventually serve as a portal for all FEC employees to access any and all applications and collaboration tools to facilitate greater communication within the agency. The Intranet, scheduled for launch during the second quarter of FY 2008, will feature a rich suite of products and deliver productivity and efficiency gains immediately. Specific benefits will include:

- Improved internal communications;
- Document management efficiencies;
- Improved search capabilities;
- Fast and easy access to information;
- A reduced number of hard-copy internal policies and procedures;
- A digital assets library;
- RSS newsfeeds;

- Employee quick polls; and
- Non-technical staff's ability to publish and contribute content to the intranet site.

The first feature to be developed will be a Human Resources portal, with additional features added throughout the year. As additional features are added, the Intranet will become the main navigation point for FEC employees.

The Commission Secretary is responsible for all administrative matters relating to Commission meetings and voting matters. In keeping with the Commission's tradition of staying as current as possible with technology, three initiatives are underway in the Office of the Commission Secretary: (1) the creation of an electronic tally vote database; (2) an electronic document work flow project; and (3) electronic voting by the Commissioners. The objectives of these initiatives are to provide the FEC with accessible, searchable, electronic versions of documents circulated for Commission approval and the means to access a database to cast a vote electronically. The electronic document workflow project is expected to bring needed efficiencies not just for the staff in the Secretary's Office, but for the Commission as a whole.

The Office of Human Resources (OHR) moved to a generalist staffing model to be as a viable, long-term solution for the agency. The FEC believes that it is imperative to retain the following core human capital functions: (1) human capital strategy; (2) employee relations; (3) labor relations; (4) organization and position management; (5) staff acquisition; (6) employee development; and (7) performance management. To ensure effective and efficient results in these core functions, it is essential to automate the administrative functions of the OHR. These functions include time and attendance and processing personnel and benefits actions. The FEC is automating these functions, with a LOB service provider, which will enable OHR to offer the results-oriented, strategic services needed to support the FEC in achieving its mission.

Section I.G – Limitations of the Financial Statements

The principal financial statements have been prepared to report the financial position and results of operations of the FEC pursuant to the requirements of 31 U.S.C. 3515 (b). While the statements have been prepared from the books and records of the FEC in accordance with U.S. generally accepted accounting principles (GAAP) for federal entities and the formats prescribed by the OMB, the statements are in addition to the financial reports used to monitor and control budgetary resources which are prepared from the same books and records. The statements should be read with the realization that they are for a component of the U.S. Government, a sovereign entity.

SECTION II
Performance Report

Section II.A – Performance Purposes, Objectives, and Results

This section serves as the Commission's Annual Performance Report as specified in OMB Circular A-11, Part 6, *Preparation and Submission of Strategic Plans, Annual Performance Plans, and Annual Program Performance Reports*, as amended. In addition, this section fulfills the FEC's requirements under the *Government Performance and Results Act*.

The FEC defines much of its work in the context of election cycles, which represents two calendar years. For example, the 2008 election cycle includes calendar years 2007 and 2008, which also spans parts of three fiscal years–the last three quarters of FY 2007, all of FY 2008, and the first quarter of FY 2009. Accordingly, certain data is most meaningful in measuring the FEC's performance by election cycle, making it difficult to provide meaningful performance data on a fiscal-year basis. Therefore, the results of the FEC's performance, as discussed in this section, includes data by either fiscal year or by election cycle, depending on which option presents the results in the most informative manner.

Strategic Goal and Objectives for FY 2007

To achieve its mission, as detailed in Section I, the FEC has identified one overarching strategic goal. This goal is supported, in turn, by three strategic objectives and underlying activities that guide the operations of the FEC and its staff on a day-to-day basis.

STRATEGIC GOAL

To protect the integrity of the federal campaign process by providing transparency, enforcing contribution restrictions, and fairly administering the FECA and related statutes.

Objective 1: Transparency – Receiving Accurate and Complete Campaign Finance Disclosure Reports and Making Them Available to the Public

Objective 2: Compliance – Education and Enforcement

Objective 3: Development of the Law – Interpreting and Administering the Act

Management excellence is a key strategy by which the Commission strives to ensure these objectives are met in the most efficient and effective manner. Consistent with the President's Management Agenda (PMA), the Commission is updating its human capital plan to better address the following elements: (1) strategic alignment; (2) workforce planning; (3) leadership development; and (4) knowledge transfer and results-oriented performance. The Commission believes that, in addition to investing in its people, strong financial management and up-to-date technology are critical means to achieving its strategic goal.

Section II.B – FY 2007 Results

Objective 1: Transparency – Receiving Accurate and Complete Campaign Finance Disclosure Reports and Making Them Available to the Public

The FEC provides the public with the data to make educated, informed decisions in the political process based, in part, on information concerning where candidates for federal office derive their financial support. The FEC gauges its effectiveness through a series of indicators designed to measure performance in areas that promote confidence in the campaign finance process.

Performance Measures

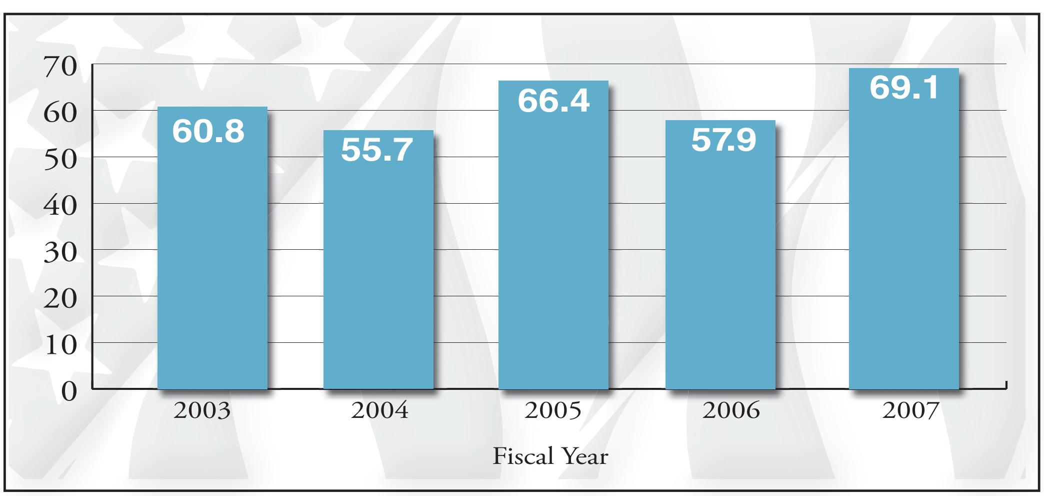
- Maintaining a state-of-the-art electronic filing system for collecting financial disclosure reports from federal candidates and political committees;
- Making financial disclosure reports available to the public in a timely, efficient and useful manner;
- Reviewing financial disclosure reports to ensure that the reports are accurate and complete; and
- Encouraging candidates and political committees to correct inaccurate or incomplete reports.

The FEC promotes voluntary compliance by fully disclosing campaign finances for federal elections. The following provides a discussion on the results achieved in carrying out these objectives and activities.

The Commission's mandatory electronic filing (e-filing) rules require any committee that receives contributions or makes expenditures in excess of $50,000 in a calendar year, or that has reason to expect to do so, must submit its reports electronically. These mandatory e-filing provisions (11 CFR § 104.18) apply to any political committee or other person required to file reports, statements and/or designations with the FEC. These requirements do not apply to Senate candidate committees (and other persons who support Senate candidates only), who file with the Secretary of the Senate.

The primary function of the e-filing system is to act as the point of entry for submission of electronically filed campaign finance reports, providing faster access to reports and streamlining operations. Specifically, the system provides for public disclosure of electronically filed reports, via the FEC website, within minutes of being filed. When a

Figure 3 – Total Reports and Statements Filed (in thousands)



committee files a financial disclosure report on paper, FEC staff scan and enter the information disclosed in the report into the FEC electronic database. The Commission's Public Records Office ensures that a copy is available for public inspection at the FEC's headquarters, located at 999 E Street, N.W., Washington, DC or electronically within 48 hours of receipt.

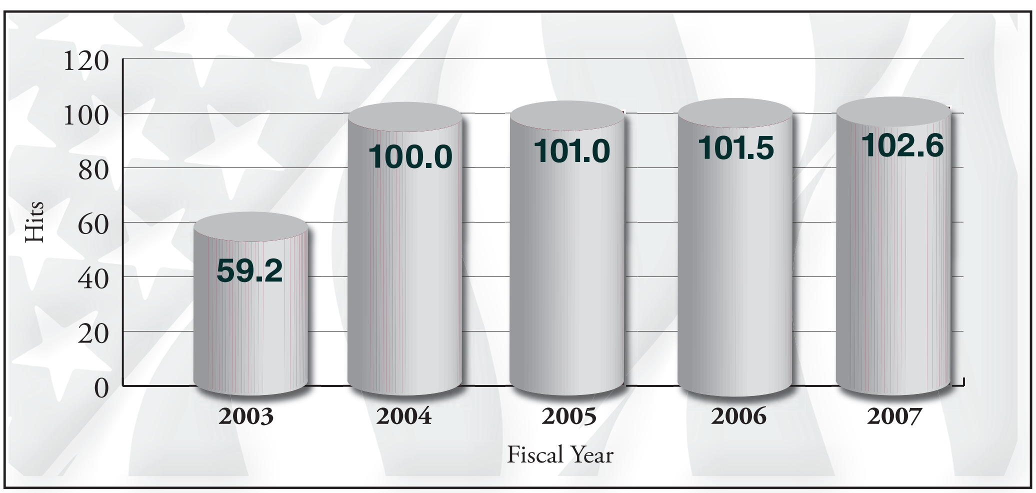
Figure 3 shows the total number of campaign finance reports and statements filed with the FEC each fiscal year since 2003. The public can access the campaign finance reports and data at http://www.fec.gov/disclosure.shtml.

As illustrated in Figure 3, election years (the odd fiscal years), show a spike in the number of filings received by the FEC. Despite an increase in the number of filings, the FEC achieved a success rate of 98.5 percent in making the financial disclosure reports and statements available to the public within 48 hours of receipt. The percentage of filings that was not processed within the 48-hour period is attributable, in part, to the extended processing time required for paper filings, thereby preventing the achievement of this goal.

After the reports are imaged for disclosure purposes, the data is coded and entered into the FEC's database for review to assess accuracy and completeness of disclosure of campaign finance information. The agency's goal is to code and enter 95 percent of the reports within 45 days of receipt. For FY 2007, the FEC was able to process 95 percent of the reports within 40 days of receipt.

The FEC's website (www.fec.gov) represents the major source of federal campaign finance information. For both political committees and the public, the Commission's website has become the single-most important source of instantly accessible information about campaign finance, the *FECA* and Commission regulations. The FEC website provides access to over tens of millions of pages of campaign finance data that have been submitted by candidates and committees and posted on-line by the FEC staff. The public's interest in finance campaign information is illustrated in Figure 4, which shows a continued high number of hits on the FEC's website by users seeking campaign finance data and other information.

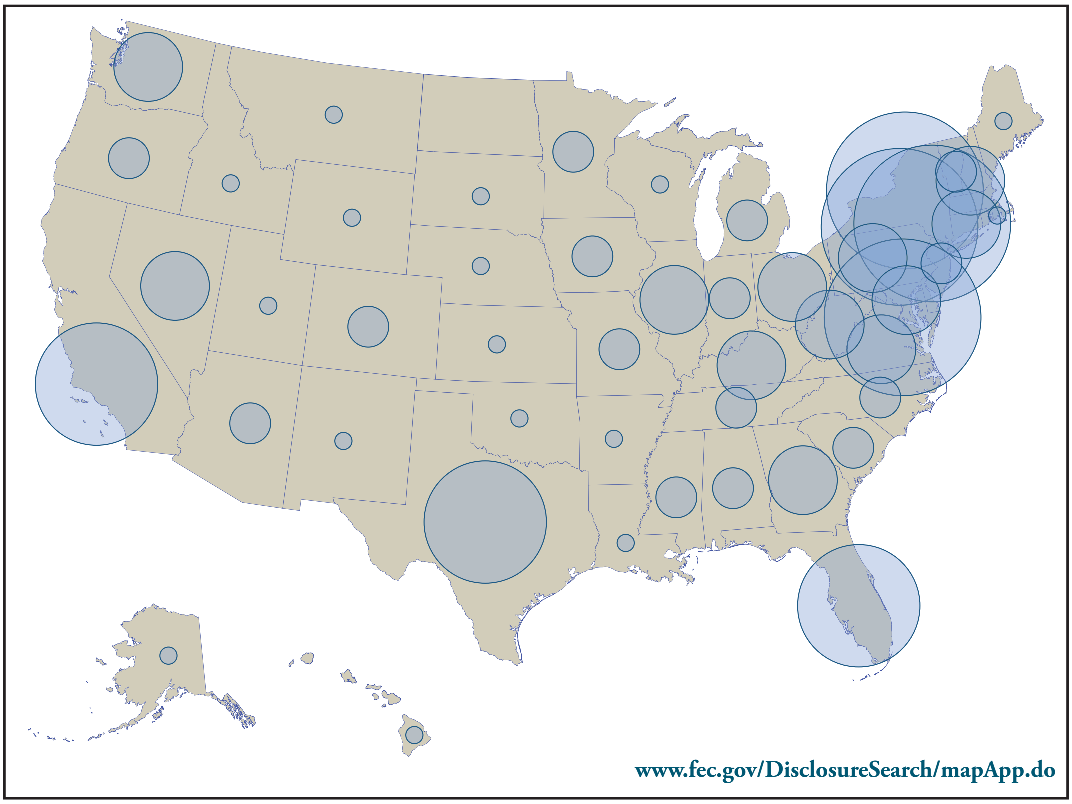
Figure 4 – Total Website Hits (in millions)



During FY 2007, the website received nearly 102.6 million hits, with an average of 10,000 visitors per day.

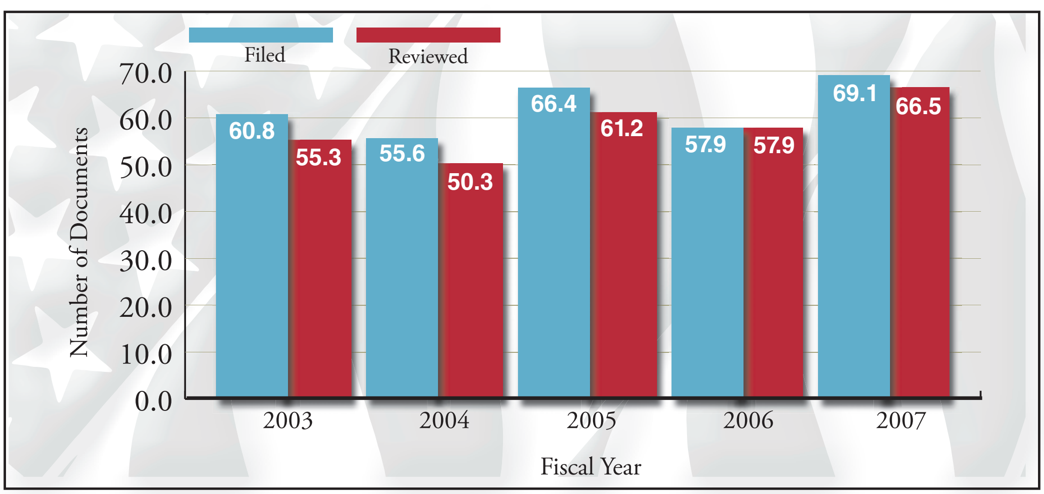
To make campaign finance data even more accessible to the public, the FEC launched a new interactive map (see Figure 5) in June 2007 to provide users with immediate access to contribution information for the 2008 Presidential election. With a simple click, users can access the amount of funds raised on a state-by-state basis, contributions, cash-on-hand, and the distribution of contributions by amount.

Figure 5 – Presidential Campaign Finance Map



Furthermore, users can access lists of contributors by name, city, and amounts of contributions within the first three digits of any zip code. Contribution data is updated within one day of the FEC's receipt of electronically filed Presidential disclosure reports.

Figure 6 – Document Volume and Review Efficiency (in thousands)



The FEC reviews each report filed to ensure the accuracy and completeness of the information received and to monitor compliance with the law. Figure 6 illustrates the continued efficiency with which campaign finance reports are being reviewed. This rapid rate of reviewing is especially noteworthy given the growth in the number of reports and statements filed, as shown in Figure 3.

The FEC reviews all reports, amendments and statements for accuracy, completeness and compliance with the law. New and amended reports for the current and past elections are received at the Commission on a daily basis. In FY 2007, the Commission reviewed 55,748 reports, 73 percent of which were reviewed within 90 days of the date received. The Commission performance goal is to review 60 percent of reports within 90 days of receipt. The Commission exceeded its performance goal by 13 percent in FY 2007. Because of the 90-day processing period and the fact that a filing deadline falls ten days before the end of the fiscal year, a small percentage of reports received in a fiscal year cannot be reviewed before that fiscal year ends. In FY 2007, this was 3.7 percent. Although the Commission does review 100 percent of all filings received, when a fiscal-year-end performance measure was developed there was no meaningful time-related goal associated with it. The FEC is in the process of updating its strategic plan to incorporate a more accurate, time-related goal.

A Presidential election cycle includes expenditures related to the election of: (1) the President; (2) all seats in the House of Representatives; and (3) one-third of the Senate seats. Figure 7 illustrates that expenditures related to federal elections are on the rise, especially as they relate to a Presidential election year. As illustrated below, total federal election expenditures increased by approximately 63 percent from the Presidential election in 1996 to the 2004 Presidential election year. To date, over $800 million has been expended under the 2008 Presidential election cycle. This amount is nearly $300 million more than the funds expended at the same point in time for the 2004 Presidential election cycle.

Figure 7 – Expenditures in Federal Elections (in billions)

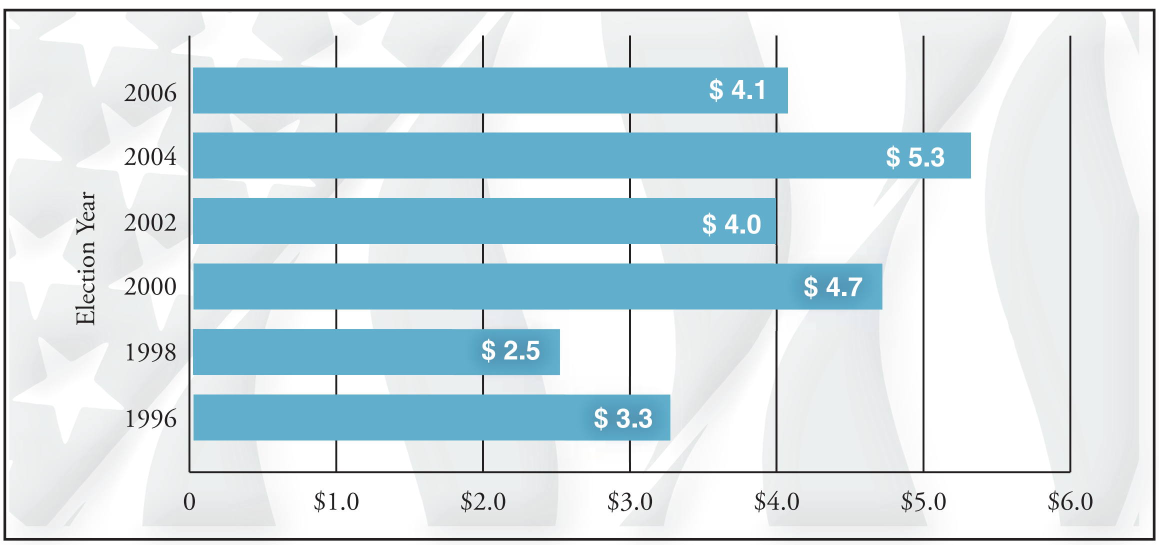


Figure 7 also illustrates that expenditures related to Congressional elections are substantially increasing. Specifically, these expenditures increased approximately 62 percent between the 1998 and the 2006 Congressional election. As a result of the rising expenditure amounts, the FEC assumes a greater workload relating to: (1) its disclosure and review efforts; (2) the identification of instances of non-compliance; (3) its response to requests for advisory opinions; and (4) the likelihood that filings are more complex, which increases the potential for misappropriation of funds.

Objective 2: Compliance – Education and Enforcement

Helping the regulated community understand its obligations under the *Act* is an essential component for improving voluntary compliance. The Commission continues to promote compliance with the law by educating political committees and the public about the requirements of the *Act*.

The FEC has exclusive jurisdiction over the civil enforcement of the federal campaign finance law. In exercising that authority, the Commission uses a variety of methods to uncover possible election law violations. Instances of non-compliance may lead to a FEC enforcement case or Matter under Review (MUR). In some cases, respondents may be given the option to participate in the Commission's Alternative Dispute Resolution program, which seeks to resolve matters more swiftly through mediation. Violations involving the late submission of FEC reports or failure to file reports are subject to the Administrative Fine program. By law, all these matters must remain confidential until they are closed.

Performance Measures

- Expanding awareness of the campaign finance laws through creation and dissemination of educational materials, and instructional conferences and workshops;
- Responding to complaints alleging violations of the campaign finance laws;
- Imposing civil penalties for late-filed and non-filed disclosure reports;
- Making findings in completed compliance matters available to the public in a timely and useful manner; and
- Conducting audits in a timely and efficient manner.

Results achieved in carrying out these objectives and activities are detailed below.

Expanding Awareness

In addition to its website, the FEC operates a press office and maintains a toll-free line (1-800-424-9530) to respond to inquiries regarding campaign finance data. The FEC has also achieved its goal of responding to information requests within 72 hours.

The Commission encourages voluntary compliance by hosting conferences across the country, where Commissioners and staff explain how the *Act* applies to candidates and political committees. These conferences address recent changes in campaign finance law and focus on fundraising and reporting regulations. The FEC established a target to hold a total of four conferences during FY 2007. This target was achieved by holding three conferences in the District of Columbia and one in the state of Washington.

Although we are unable to determine the immediate effect that these conferences will have on voluntary compliance, we believe that the regulated community's awareness of the law has been expanded by the FEC's educational programs and that the results of the efforts will be far reaching into the future. The success of these efforts is evidenced by the favorable ratings received for each conference. The overall rating exceeded a 4.0 rating out of a possible 5.0 for each conference.

The FEC also hosts state outreach seminars, which are held throughout the country to brief PACs, party committees and candidate committees on areas of the law specific to their needs. In FY 2007, meetings were held in Colorado, Arizona, and Georgia.

Responding to Complaints

In the last several years, the FEC has responded to a variety of enforcement matters through its Office of General Counsel (OGC), Administrative Fine (AF) and Alternative Dispute Resolution (ADR) programs. Under the

Commission's traditional enforcement program, the Commission learns of possible election law violations primarily through:

- The Commission's review of a committee's reports or through a Commission audit;
- The complaint process, whereby anyone may file a sworn complaint alleging violations of the *Act*;
- Voluntary self-reporting, sua sponte, by a candidate or political committee representative who believes that they may have violated the *Act*; and
- The referral process, whereby other government agencies may refer possible violations of the *Act* to the FEC.

The most complex and legally significant enforcement matters are handled by the OGC that:

- Recommends to the Commission whether to find "reason to believe" the *FECA* has been violated, a finding which formally initiates an investigation;
- Investigates potential violations of the *FECA* by requesting, subpoenaing and reviewing documents and interviewing or deposing witnesses;
- Conducts settlement negotiations on behalf of the Commission, culminating in "conciliation agreements" with respondents on the assessment of fines; and
- Files suit in federal district court when conciliation is unsuccessful.

Office of General Counsel

Enforcement matters handled by the OGC are pursuant to the procedures set forth in §437g of the *FECA*. Over the past several years, the General Counsel has initiated a number of management and organizational changes to increase the quality and efficiency of the FEC's enforcement work, and has implemented policy initiatives to facilitate the processing of matters under review. The result is a more objective and expeditious process, with meaningful penalties and other remedies proportionate to the violation.

In recent years, the FEC has steered resources to the most significant violations, leading to a steep increase in civil penalties for serious violators. From FY 2003 to 2007, the OGC negotiated conciliation agreements providing for civil penalties totaling more than $16.2 million. In FY 2007 alone, civil penalties amounted to more than $4.1 million, a decrease of 30.6 percent from civil penalties assessed last year. The decrease is attributable to the $3.8 million civil penalty negotiated in one matter in 2006. Not only was this penalty more than four-times greater than any civil penalty obtained in Commission history, but it alone was more than the aggregate amount obtained in any previous year. Excluding this one penalty, FY 2007 reflects an increase over FY 2006 of approximately $2.2 million, or 127 percent.

In terms of efficiency, on average cases closed 32 percent, faster in FY 2007 compared to FY 2002. In FY 2002, it took, on average, 730 days to close an enforcement matter. By FY 2007, the Commission reduced this number by 230 days to an average of 500 days. This productivity is derived from the implementation of the AF and ADR programs, as well as better management of personnel, improved information technology, and the shifting of priorities.

The percentage of "substantive" closings for the FEC, as a whole, over the past 10 years has climbed to 74 percent, with only 26 percent of the matters being dismissed. In the mid-1990s, it was not unusual for the Commission to dismiss over half of its enforcement caseload with no action. A significant portion of those cases were dismissed as "stale" (i.e., cases that went unassigned for at least 12 months). From FY 1995 to 2000, the FEC dismissed 21 percent of its cases as stale. Importantly, the General Counsel has all but eliminated the practice of dismissing stale cases. FY 2007 was the fourth year in a row in which the FEC did not dismiss a single case as stale.

Figure 8 – Enforcement Cases Opened

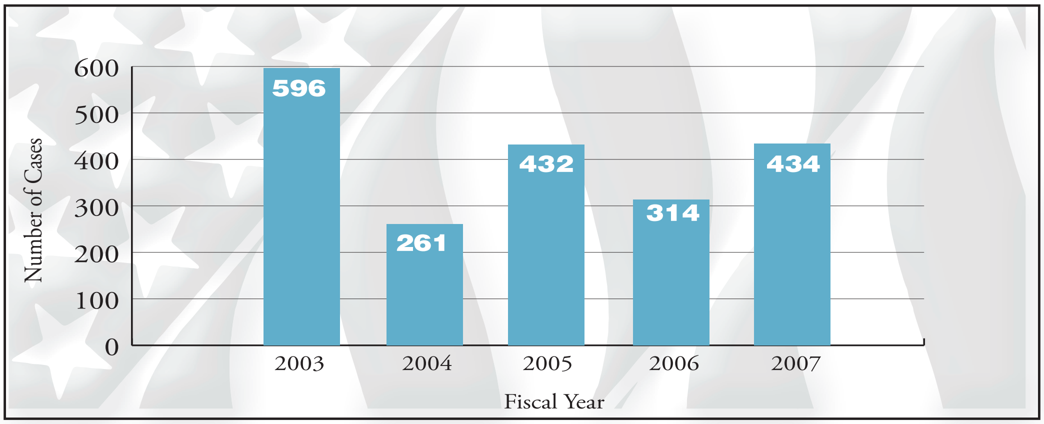


Figure 8 shows the number of cases opened for enforcement action. The number of cases opened, 434 in FY 2007, increased by 38.2 percent from FY 2006. This increase is due primarily to the increase in the number of filings and the cyclical nature of the AF program.

Alternative Dispute Resolution

The ADR program was implemented in FY 2001 to facilitate settlements outside of the traditional enforcement or litigation processes. The program's primary objective is to enhance the agency's overall effectiveness through more expeditious resolution of enforcement matters with fewer resources required to process complaints and internal referrals. In FY 2007, ADR formally closed 71 cases, with substantive action taken in 58 percent of those cases. This is an increase of 16.4 percent over the number of cases closed in FY 2006.

Administrative Fine Program

In response to a legislative mandate, the AF program was implemented in July 2000 to address failures to timely filing or non-filing of disclosure reports in a more efficient and effective manner. During FY 2007, the AF program closed 266 cases in an average of 128 days, which is nearly a 200 percent increase in the number of cases closed over FY 2006. This program is administered by the Office of Administrative Review and RAD, which are within the Office of Compliance.

Figure 9 – Enforcement Cases Closed by Program

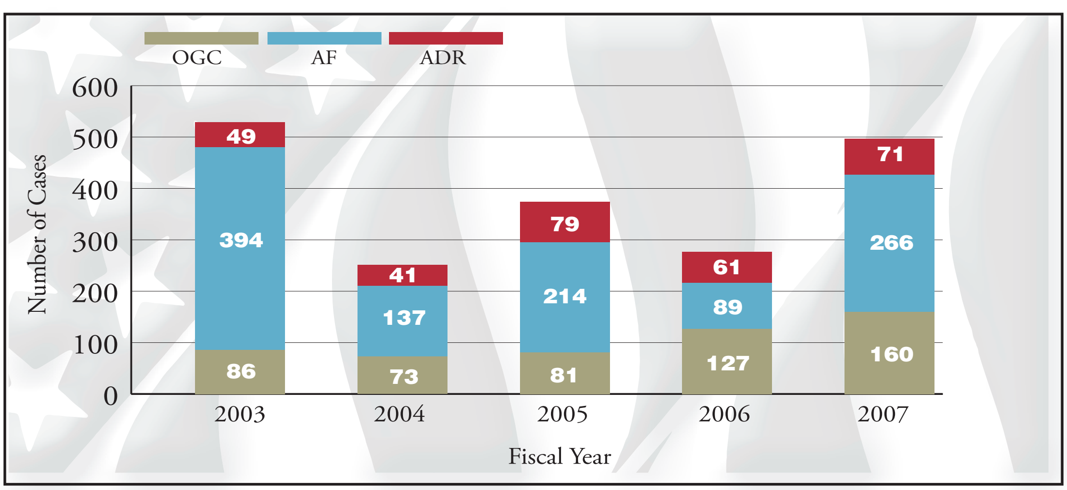
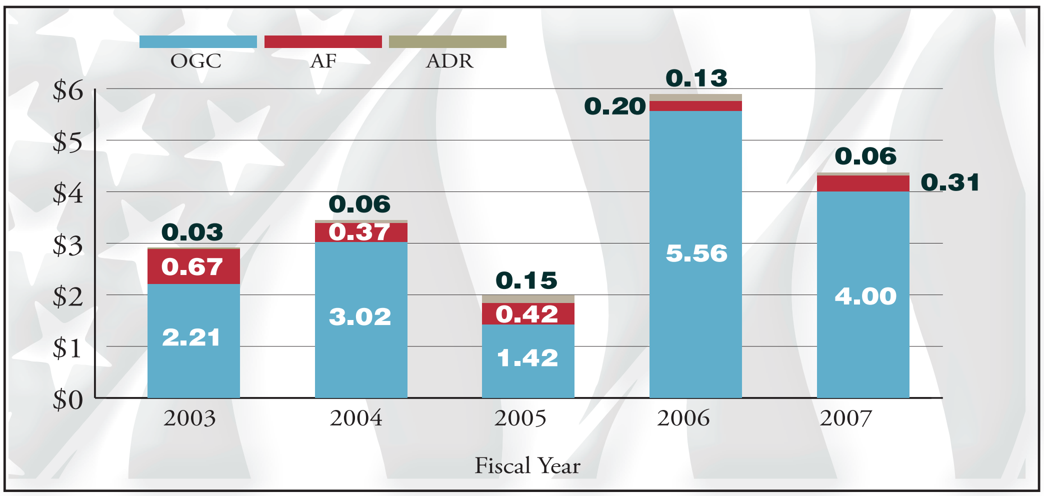


Figure 9 shows the number of cases closed from FY 2003 to FY 2007. The efforts by OGC, AF, and ADR led to an increase in case closings from 277 in FY 2006 to 497 in FY 2007, a 79.4 percent increase. The increase in the number of cases closed is not only attributable to the cyclical nature of the AF program but also to a management decision to prioritize the closing of cases in a more efficient and effective manner.

As the discussion and figures in this section demonstrate, the FEC has improved its performance in timeliness and quantity. The improved overall performance, in part, is due to the implementation of the AF and ADR programs. These programs enable the FEC to focus its resources on more substantive cases thereby improving the effectiveness and efficiency of processing cases. Closed enforcement matters are available online through the Commission's Enforcement Query System at http://eqs.sdrdc.com/eqs/searcheqs.

Figure 10 illustrates how the combination of OGC, ADR, and AF increased fines by a significant 50.2 percent, from $2.91 million in 2003 to $4.37 million in FY 2007. The amount of fines is dependent upon the nature of the violation.

Figure 10 – Fines/Penalties Assessed by Program (in millions)



Conducting Audits

The Audit Division's major responsibilities concern the public funding of Presidential campaigns and audits of various political committees. This division evaluates the Presidential primary candidates' applications for matching funds and determines the amount of contributions that may be matched with federal funds. As required by law, the FEC audits all recipients of public funds. In addition, the Commission audits those committees that, according to FEC determinations, have not complied with the law. The Audit Division publishes its findings in audit reports, which can be found at http://www.fec.gov/audits/audit_reports.shtml.

During FY 2007, the Audit division completed 25 audits, of which 18 were performed under Title 2. For each election cycle, the FEC's target is to conduct 40 to 45 audits, pursuant to 2 U.S.C. §438(b). An election cycle spans two calendar years. This pace is on schedule to meet the two-year goal of 40 to 45 Title 2 audits per election cycle.

In addition to the Title 2 "for cause" audits, the FEC is responsible for completing mandatory audits pursuant to Title 26. There were 15 audits associated with the 2004 Presidential election. The FEC has a goal to complete all Title 26 Presidential audits within two years after the Presidential elections. The FEC did not achieve this goal. Out of the 15 audits, six (40%) were completed within the two-year timeframe. As of the end of FY 2007, of the remaining nine audits associated with the 2004 Presidential election, seven had been completed, leaving two outstanding. Presidential audits are extremely complex, and as stated earlier, the increased volume of expenditures affects the scope and length of time it takes to complete an audit. In FY 2008, the FEC will reevaluate its audit process to determine how to achieve this goal, given the increased complexities of Title 26 audits.

Figure 11 illustrates the number of audits started over the past five years.

Figure 11 – Audits Approved to be Started

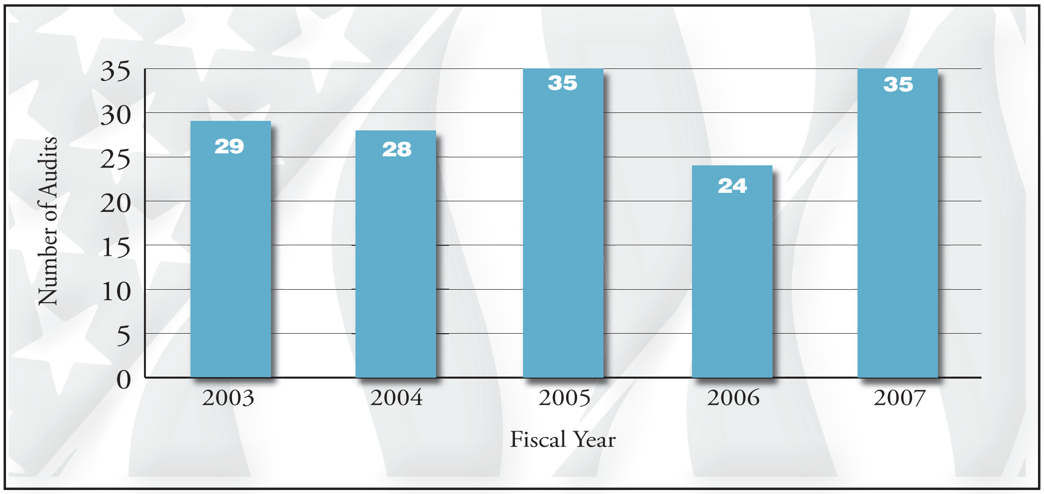
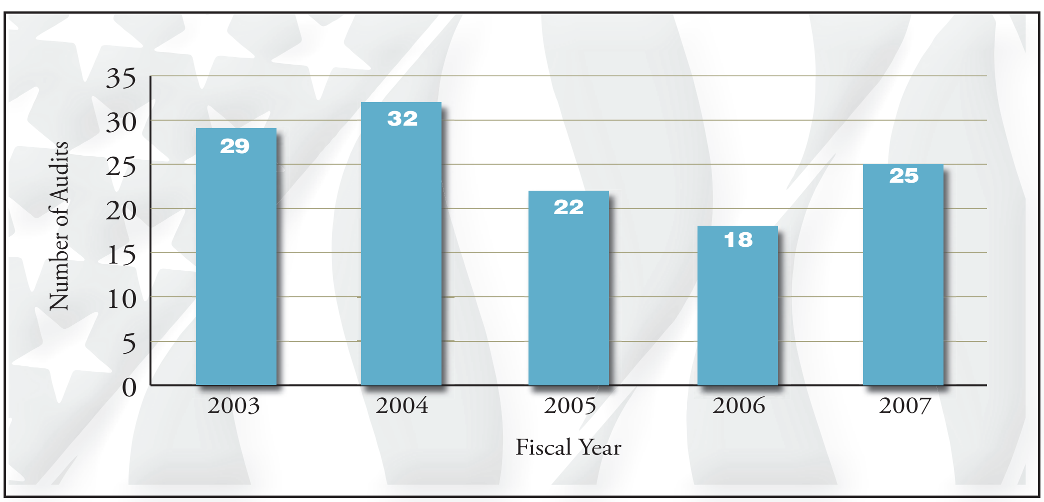


Figure 12 shows the number of audits completed between FY 2003 and 2007. Presidential committee audits demand more time and resources than Title 2 "for cause" audits because of their complexity. The number of audits is dependent on the Presidential election cycle, along with the number of candidates that participated in the public funding program.

Figure 12 – Audits Completed by the Commission



Federal election law permits all eligible national committees of major and minor parties to receive public funds to help pay the official costs of their Presidential nominating conventions. The FEC certified payments for each of the two major political parties' convention committees, with initial payments of $16,356,000 made in July 2007 for planning and conducting their respective 2008 Presidential nominating conventions. In exchange for public funding of the conventions, committees agree to certain requirements, including spending limits, the filing of periodic disclosure reports, and detailed audits.

Objective 3: Development of the Law – Interpreting and Administering the Act

The Commission provides formal interpretation of the *Act* through the promulgation of regulations and the issuance of advisory opinions (AOs).

Performance Measures

- Conducting rulemaking proceedings to promulgate Commission regulations consistent with revisions to the *FECA* and judicial decisions related to the *Act*;
- Issuing advisory opinions providing specific guidance to the regulated community;
- Defending challenges to the *Act*, Commission regulations or actions; and
- Certifying all Presidential public funding payments in a timely and efficient manner.

Results achieved in carrying out these objectives and activities are detailed below.

The FEC publishes its regulations annually, which are codified in Title 11 of the Code of Federal Regulations (CFR). The Policy Division of the OGC drafts Notices of Proposed Rulemaking (NPRMs), which are then adopted by the Commission and are published in the *Federal Register*. NPRMs are also made available on the FEC's website at http://www.fec.gov/law/law_rulemakings.shtml and on the U.S. Government website, www.regulations.gov. NPRMs provide an opportunity for members of the public and regulated community to review proposed regulations, submit written comments to the Commission and testify at public hearings, which are held at the FEC when appropriate. The Commission then considers the public comments and testimony and deliberates publicly regarding the adoption of the final regulations. The text of final regulations and the corresponding *Explanation and Justification* (E&J), once adopted by the Commission, are published in the *Federal Register*.

The FEC issued several rulemaking documents during FY 2007, a summary of which can be reviewed at http://www.fec.gov/law/cfr/cfr.shtml. The number of rulemakings is dependent upon many factors, such as the complexity of the issues to be addressed, the need for clarification, the passage of new legislation, or the outcome of litigation efforts.

Advisory Opinions are official Commission responses to questions regarding the application of federal campaign finance law to specific factual situations. The FEC's Advisory Opinion brochure at http://www.fec.gov/pages/brochures/ao.shtml provides a complete description of the AO process and explains how to request an advisory opinion.

Consistent with the *Act*, when the Commission receives a request for an AO, it generally has 60 days to respond. For AO requests from candidates in the two months leading up to an election, the time for the Commission to respond to the request is reduced to 20 days. Nevertheless, the Commission instituted an expedited process last year for handling certain time-sensitive requests in even shorter timeframes. The Commission has placed special emphasis in the last year on expediting its processing and consideration of certain highly significant AO requests. Although the *Act* allows the agency 60 days to respond to most requests, the Commission issued some of its recent opinions within as little as two weeks.

During FY 2007, the FEC issued 24 advisory opinions, with an average response time of 48 days. A summary of the AOs can be reviewed at http://saos.nictusa.com/saos/searchao. Of these AOs, 18 (75%) were completed within the required 60-day response period. The number of AO requests that the Commission receives depends largely on election cycles. Additionally, the complexity of the topics addressed in these AOs has increased, primarily because of *BCRA*, which required a number of new Commission regulations and which is the subject of recent litigation.

Defending Challenges to the Act

The Commission exclusively represents itself before the federal district and circuit courts, and before the Supreme Court with respect to cases involving publicly-financed Presidential candidates, and has primary responsibility for defending the *Act* and Commission regulations against court challenges. The Commission brings enforcement suits in U.S. District Courts when matters are not satisfactorily resolved through the administrative enforcement process and sues to enforce administrative subpoenas. The agency also defends suits contesting its dismissals of administrative complaints, petitions for review of Commission decisions regarding the Presidential public funding program and civil suits challenging the constitutionality of provisions of the *FECA* and the validity of the Commission's regulations. When the Commission brings enforcement suits seeking civil penalties, it must initiate such actions within the applicable statute of limitations and adhere to all other applicable court rules.

The outcome of litigation is unpredictable and can take several years to reach final resolution, especially if cases proceed all the way to the Supreme Court. Once a final decision is reached, it can often require the Commission to promulgate more regulations and issue additional advisory opinions.

For example, the Commission is in the process of defending its "political committee" rulemaking. Although the Commission recently received a favorable decision from the district court, the plaintiffs may decide to appeal that ruling. Depending upon the outcome of the case, the Commission may consider additional rulemaking or will be implementing the statute and applicable regulations on a case-by-case basis in advisory opinions and through the enforcement process. Generally speaking, pending and likely litigation represents a substantial likelihood of additional work for the Commission. The FEC's rules implementing *BCRA* are still subject to litigation (e.g., *Shays III* and *EMILY's List* – see http://www.fec.gov/law/litigationrecent.shtml for details) and could result in orders to rewrite extensive portions of the FEC's regulations. As a measure of significance, post-*BCRA* rulemakings have expanded the FEC's regulations by at least 40 percent. In addition, implementation and probable future "as applied" challenges following a recent Supreme Court decision (*Wisconsin Right to Life)* could require considerable expense and effort.

Public Funding

In addition to enforcing the *FECA*, the Commission is responsible for administering the public funding of Presidential elections, as outlined in 26 U.S.C. To be eligible for public funds, a Presidential candidate or a party convention committee must first submit a letter of agreement and a written certification in which the candidate or committee agrees to:

- Spend public funds only for campaign-related expenses or, in the case of a party convention, for convention-related expenses;
- Limit spending to amounts specified by the campaign finance law;
- Keep records and, if requested, supply evidence of qualified expenses;
- Cooperate with an audit of campaign or convention expenses;
- Repay public funds, if necessary; and
- Pay any civil penalties imposed by the FEC.

Primary candidates must additionally certify that they have met the "threshold requirement" for eligibility by raising in excess of $5,000 in each of 20 states.

The Commission certifies a candidate's eligibility to participate in the program, establishes eligibility for payments, and conducts a thorough examination and audit of the qualified campaign expenses of every candidate who receives payments under the program. For the 2004 Presidential election, the Commission certified the eligibility for ten candidates and two convention committees. For the FY 2008 Presidential election, the FEC has certified two candidates for eligibility under the program so far. However, the total number of eligible candidates is dependent upon the number of applicants.

Legislative Recommendations

Every year, the Commission forwards to the President and Congress recommendations for improvements to the federal campaign finance law. On April 12, 2007, the Commission approved five legislative recommendations, which were to:

- Require electronic filing of Senate campaign finance reports;
- Expand the prohibitions on fraudulent misrepresentation of campaign authority to encompass all persons purporting to act on behalf of candidates or political organizations;
- Add the FEC to the list of Agencies authorized to issue "use" immunity orders under Title 18 with the permission of the Attorney General, providing added flexibility in pursuing information in enforcement investigations;
- Require political committees to include FEC identification numbers, for standardization purposes, on contribution checks sent to other political committees and to disclose the identification numbers of other political committees when itemizing contributions from them and contributions to them on reports filed with the Commission; and
- Increase certain monetary registration and reporting thresholds related to actions by individuals and small groups involved in political campaigns to adjust amounts for inflation experienced over the last thirty years.

Greater detail concerning the Commission's legislative recommendations can be found at http://www.fec.gov/law/legislative_recommendations_2007.shtml#id.

Improving management efficiency and effectiveness remains a key focus of the Commission. Consistent with the PMA, the Commission seeks to continue to provide a greater focus on performance that better aligns with results, and provides a framework for greater transparency of its operations.

SECTION III

Auditor's Report and Financial Statements

Message From the Chief Financial Officer

November 15, 2007

I am pleased to present the Commission's financial statements for fiscal year 2007. Our financial statements are an integral component of the Performance and Accountability Report, as required under the *Accountability of Tax Dollars Act of 2002*. This is the fourth year that the FEC has prepared and submitted audited financial statements.

The Commission is committed to financial management excellence, and sound stewardship and management of the public funds to which we have been entrusted. The following highlights the results of the fiscal year 2007 audit:

- Received an unqualified opinion on the principal financial statements; and
- Reduced the number of audit findings from seven to two, as identified as part of the Auditor's Report on Internal Control.

The success of this year's audit is attributable to the efforts of our employees, who have made financial management a priority; thereby ensuring that the highest quality financial data is reported. The Commission continued its high standard of financial management and reporting during fiscal year 2007. As a result, we observed significant improvements in financial management, including overcoming a qualified audit opinion that was received for the past two years.

We recognize more needs to be done to further strengthen internal controls, as outlined by the recommendations made in the Auditor's Report on Internal Control. To date, we have begun to address several of the recommendations, including:

- Signing an agreement with the General Services Administration (GSA) for financial management services;
- Awarding several contracts to resolve the need for risk assessments, continuity of operations, and a disaster recovery plan;
- Updating documentation of current financial management processes and systems; and
- Identifying training needs for employees to further enhance awareness of financial management.

We will continue to emphasize improving financial management. A key focus for FY 2008 includes continuing the same high level of quality financial management that resulted in our unqualified opinion and improving upon it. We also will focus on continuing to implement our Strategic Plan. In the past year, we took steps to develop our requirements for a line of business provider for financial management services that will improve operations and permit us to better integrate financial, program, and performance data. We have brought our stakeholders into the process and will work closely with them to improve upon our ability to produce timely, reliable, and useful data.

Sincerely,

Erin D. Singshinsuk
Chief Financial Officer

Independent Auditor's Report

FEDERAL ELECTION COMMISSION
WASHINGTON, D.C. 20463

Office of Inspector General

MEMORANDUM

TO: The Commission

FROM: Inspector General

SUBJECT: Audit of the Federal Election Commission's Fiscal Year 2007 Financial Statements

DATE: November 15, 2007

Pursuant to the Chief Financial Officers Act of 1990, commonly referred to as the "CFO Act," as amended, this letter transmits the Independent Auditor's Report and accompanying Independent Auditor's Reports on Internal Control and Compliance and Other Matters issued by Clifton Gunderson LLP (CG-LLP) for the fiscal year ending September 30, 2007. The audit was performed by CG-LLP under a contract with and monitored by the Office of Inspector General (OIG) in accordance with *Government Auditing Standards* and Office of Management and Budget (OMB) Bulletin No. 07-04, *Audit Requirements for Federal Financial Statements*, as amended.

Opinion on the Financial Statements
The audit included an examination, on a test basis, of evidence supporting the amounts and disclosures in the financial statements. The audit also included assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall principal statements' presentation.

The CG-LLP report concluded that the Federal Election Commission's (FEC) financial statements present fairly, in all material respects, the financial position of the FEC as of September 30, 2007 and 2006, and its net cost, changes in net position, budgetary resources, and custodial activity for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In the Independent Auditor's Report for the prior fiscal year, dated November 7, 2006, CG-LLP expressed a qualified opinion on the FY 2006 statement of net cost because the auditors were not able to obtain sufficient competent audit evidence to support the FEC's allocation of program costs. Since the FEC has changed the presentation of program costs in its statement of net cost, the present opinion on the FY 2006 financial statements is different from that expressed in the previous report.

Report on Internal Control

CG-LLP's planning and performance of the audit included consideration of the FEC's internal control over financial reporting as a basis for designing audit procedures for the purpose of expressing an opinion on the financial statements and to comply with OMB Bulletin 07-04. The auditors did not test all internal controls relevant to operating effectiveness, such as those controls relevant to ensuring efficient operations, and consequently CG-LLP did not express an opinion on the agency's internal control over financial reporting.

The American Institute of Certified Public Accountants (AICPA) established standards on communicating deficiencies related to an entity's internal control over financial reporting identified by the auditors. As defined by the AICPA, a control deficiency exists when the design or operation of a control does not allow the agency's management or its employees, in the normal course of performing their assigned duties, to prevent or detect misstatements on a timely basis.

Auditors determine whether an internal control deficiency is a significant deficiency or a material weakness based on the factors of likelihood and magnitude. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affect the agency's ability to initiate, authorize, record, process, or report financial data reliability in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the agency's financial statements that is more than inconsequential will not be prevented or detected by the agency's internal control. A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the agency's internal controls.

CG-LLP identified a significant deficiency in the area of:

- Information Technology (IT)

CG-LLP identified a material weakness in the area of:

- Integrated Financial Management System

Report on Compliance and Other Matters

FEC management is responsible for complying with laws and regulations applicable to the agency. To obtain reasonable assurance about whether the FEC's financial statements are free of material misstatements, CG-LLP performed tests of compliance with certain provisions of laws and regulations, non-compliance with which could have a direct and material effect on the determination of financial statement amounts, and certain laws and regulations specified in OMB Bulletin No. 07-04, such as the Anti-Deficiency Act and the Prompt Payment Act.

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The results of CG-LLP's tests of compliance with laws and regulations described in the audit report disclosed no instances of noncompliance with the laws and regulations that are required to be reported under *Government Auditing Standards* and OMB Bulletin No. 07-04.

Audit Follow-up

The report on internal control contains recommendations to address weaknesses found by the auditors. Management was provided a draft copy of the audit report for comment and generally concurred with the findings and recommendations. In accordance with OMB Circular No. A-50, *Audit Followup*, revised, the FEC's corrective action plan is to set forth the specific action planned to implement the recommendations and the schedule for implementation. The Commission has designated the Chief Financial Officer to be the audit follow-up official for the financial statement audit.

OIG Evaluation of Clifton Gunderson LLP's Audit Performance

In connection with the OIG's contract with CG-LLP, we reviewed CG-LLP's report and related documentation and inquired of its representatives. The OIG's review, as differentiated from an audit in accordance with U.S. generally accepted government auditing standards (GAGAS), was not intended to enable us to express, and we do not express, opinions on the FEC's financial statements or internal control or on the FEC's compliance with laws and regulations. CG LLP is responsible for the attached auditor's report and the conclusions expressed in the report. However, the OIG review disclosed no instances where CG-LLP did not comply, in all material respects, with GAGAS.

We appreciate the courtesies and cooperation extended to Clifton Gunderson LLP and the OIG staff during the audit. If you should have any questions concerning these reports, please contact my office on (202) 694-1015.

Lynne A. McFarland

Lynne A. McFarland
Inspector General

Attachments

Cc: Chief Financial Officer
Staff Director
General Counsel
Chief Information Officer
Accounting Officer

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Clifton Gunderson LLP
Certified Public Accountants & Consultants

Independent Auditor's Report

To the Inspector General of the
Federal Election Commission

We have audited the balance sheets of the Federal Election Commission (FEC) as of September 30, 2007 (FY 2007) and 2006 (FY 2006), and the related statements of net cost, changes in net position, budgetary resources, and custodial activity for the years then ended (hereinafter collectively referred to as the "financial statements"). These financial statements are the responsibility of the FEC's management. Our responsibility is to express an opinion on these financial statements based on our audits

We conducted our audits in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and applicable provisions of Office of Management and Budget (OMB) Bulletin No. 07-04, *Audit Requirements for Federal Financial Statements*. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statements' presentation. We believe our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the FEC as of September 30, 2007 and 2006, and its net cost, changes in net position, budgetary resources, and custodial activity for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In our report dated November 7, 2006, we expressed a qualified opinion on the FY 2006 statement of net cost because we were not able to obtain sufficient competent audit evidence to support the allocation of program costs. As described in Note 1, FEC has changed the presentation of program costs in its statement of net cost. Accordingly, our present opinion on the FY 2006 financial statements, as presented herein, is different from that expressed in our previous report.

In accordance with *Government Auditing Standards*, we have also issued our reports dated November 13, 2007 on our consideration of the FEC's internal control over financial reporting, and on our tests of the FEC's compliance with certain provisions of laws and regulations and other matters. The purpose of those reports is to describe the scope of our testing of internal

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control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. Those reports are an integral part of our audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The information in the Management Discussion and Analysis section is not a required part of the consolidated financial statements, but is supplementary information required by U.S. generally accepted accounting principles and OMB Circular No. A-136, *Financial Reporting Requirements*. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of this information. However, we did not audit this information and, accordingly, we express no opinion on it.

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements taken as a whole. The information in the Message from The Chairman, Performance Section, and Other Accompanying Information is presented for purposes of additional analysis and is not required as part of the consolidated financial statements. This information has not been subjected to auditing procedures and, accordingly, we express no opinion on it.

Clifton Gunderson LLP

Calverton, Maryland
November 13, 2007

Clifton Gunderson LLP
Certified Public Accountants & Consultants

Independent Auditor's Report on Compliance and Other Matters

To the Inspector General of the
Federal Election Commission

We have audited the financial statements of the Federal Election Commission (FEC) as of, and for the year ended September 30, 2007, and have issued our report thereon dated November 13, 2007. We conducted our audit in accordance with the auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards,* issued by the Comptroller General of the United States; and, applicable provisions of Office of Management and Budget (OMB) Bulletin 07-04, *Audit Requirements for Federal Financial Statements.*

The management of FEC is responsible for complying with laws and regulations applicable to FEC. As part of obtaining reasonable assurance about whether FEC's financial statements are free of material misstatements, we performed tests of FEC's compliance with certain provisions of laws and regulations, non-compliance with which could have a direct and material effect on the determination of financial statement amounts and certain other laws and regulations specified in OMB Bulletin 07-04. We limited our tests of compliance to these provisions and we did not test compliance with all laws and regulations applicable to FEC. Providing an opinion on compliance with certain provisions of laws and regulations was not an objective of our audit, and, accordingly, we do not express such an opinion.

The results of our tests of compliance with laws and regulations described in the preceding paragraph disclosed no instances of reportable noncompliance or other matters that are required to be reported under U.S. generally accepted *Government Auditing Standards* or OMB Bulletin No. 07-04.

This report is intended solely for the information and use of the management of FEC, FEC Office of Inspector General, Government Accountability Office, OMB and Congress, and is not intended to be and should not be used by anyone other than these specified parties.

Clifton Gunderson LLP

Calverton, Maryland
November 13, 2007

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Independent Auditor's Report on Internal Control

To the Inspector General of the
Federal Election Commission

We have audited the financial statements of the Federal Election Commission (FEC) as of and for the year ended September 30, 2007 and have issued our report thereon dated November 13, 2007. We conducted our audit in accordance with the auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards,* issued by the Comptroller General of the United States; and, applicable provisions of Office of Management and Budget (OMB) Bulletin No. 07-04, *Audit Requirements for Federal Financial Statements.*

In planning and performing our audit, we considered FEC's internal control over financial reporting as a basis for designing our audit procedures for the purpose of expressing our opinion on the financial statements and to comply with OMB Bulletin 07-04, but not for the purpose of expressing an opinion on the effectiveness of FEC's internal control over financial reporting. We did not test all internal controls relevant to operating effectiveness as broadly defined by the *Federal Managers' Financial Integrity Act (FMFIA)* (31 U.S.C. 3512), such as those controls relevant to ensuring efficient operations. Accordingly, we do not express an opinion on the effectiveness of FEC's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. As discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affect the entity's ability to initiate, authorize, record, process, or report financial data reliability in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal controls.

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Our consideration of the internal control over financial reporting was for the limited purpose described in the second paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weakness. However, we believe that the significant deficiency in Integrated Financial Management System described below is a material weakness.

Finally, with respect to internal control related to performance measures reported in the FEC's Performance and Accountability Report as of September 30, 2007, we obtained an understanding of the design of significant internal controls relating to the existence and completeness assertions, as required by OMB Bulletin 07-04. Our procedures were not designed to provide assurance on internal control over reported performance measures, and, accordingly, we do not provide an opinion on such controls.

****

MATERIAL WEAKNESS

I. Integrated Financial Management System (Modified Repeat Finding)

A single, integrated financial management system is a unified set of financial systems linked together electronically in an efficient and effective manner to provide agency-wide financial management support. An integrated system should maintain an interrelationship between software, hardware, personnel, procedures, controls and data contained within the systems which allows users to obtain necessary information efficiently and effectively through electronic means. It does not necessarily mean having only one software application covering all financial management needs within an agency. Interfaces are acceptable as long as the supporting details are maintained and accessible to managers. Interface linkages must be electronic unless the number of transactions is so small that it is not cost beneficial to automate the interface. Easy reconciliation between systems, where interface linkage is appropriate, must be maintained to ensure data accuracy.

The FEC does not have an integrated financial management system. Its general ledger and core financial management system are housed in PeopleSoft (PS). However, significant financial activity, such as Obligations, Revenue, Accounts Receivable, Property, Plant and Equipment (PPE) and payroll transactions, originate outside of PS. Of these transactions, only the Payroll activity processed through the National Finance Center's (NFC) payroll system is automatically interfaced with the FEC's core financial system. Obligations, Revenue, Account Receivable and Property transactions are recorded in subsidiary schedules maintained in multiple excel spreadsheets and then manually posted to the general ledger. These spreadsheets support the flow of transactions throughout the year.

As a result of a lack of an integrated system, FEC goes through a process of compiling financial data in separate spreadsheets in a complex and time-consuming process to generate the financial statements. Although FEC reviews these spreadsheets, the risks of error increase due to the inherent risk and limitations of a spreadsheet based application in an agency's financial management system. Some of these risks include:

- Substantial manual intervention is necessary, thereby increasing the risk of human error not being detected.
- Difficulty in tracking changes made to spreadsheets, including formula changes, preventing an adequate audit trail.
- Difficulty in verifying change controls and error correction changes made.
- Unique, new or non-recurring transactions are difficult to incorporate.
- Difficulty in performing automatic checks and balances on the transactions in the spreadsheets.
- Delay in recording transactions in the general ledger.
- Increase in the use of journal vouchers as a means for posting transactions to the general ledger.
- Substantial resources are spent processing transactions resulting in fewer resources for financial analysis and reporting.

These risks for errors were substantiated through our audit testing that identified the following control deficiencies:

- Accounting entries posted to the general ledger were not always sufficiently documented or documentation to support the entries was not always properly maintained.
- Accrued expenses reported on the June 30, 2007 financial statements were misstated due to a posting error.
- The change in gross accounts receivable transactions were not recorded in the interim statements of custodial activity (March 2007 and June 2007).
- Multiple budgetary accounting related issues occurred resulting in:
    - The Recoveries of Prior Year Obligations and Obligations Incurred line items of the June 30, 2007 and September 30, 2007 draft financial statements being misstated. The reconciliation between the fourth quarter SF-133 and Statement of Budgetary Resources (SBR) as of September 30, 2007 was performed using incorrect SF-133 data. Accordingly, the reconciliation did not reveal significant adjustments needed to the SBR and related financial statements, including a routine year-end adjusting entry of cancelling the 2002 fund.
    - FEC has not established the posting logic prescribed by Treasury for recording budget authority received under a continuing resolution. Furthermore, the FEC did not record apportionments in accordance will OMB Circular No. A-11, *Preparation, Submission and Execution of the Budget*. Specifically, FEC recorded the entire requested appropriation of $54 million as budget authority in February 2007 even though the entire budget authority did not become available until April 2007. The incorrect entries increased the risk that the system's fund control may not have been effective, increasing the possibility that funds could have been obligated/expended in a manner that could have caused a violation of the Anti-Deficiency Act.
- FEC's obligating documents contained errors or were inconsistent with supporting documentation; thereby increasing the risk for disbursements to be applied to the

incorrect appropriation account or obligation. Specifically, we noted 2 out of 45 disbursements that were applied to the incorrect appropriation account.

- FEC did not prepare and submit to OMB an analysis of significant financial statement line item fluctuations between March 31, 2006 and March 31, 2007. Moreover, our review of the analyses performed in subsequent reporting quarters showed that the analyses were not performed timely and/or were not complete.
- FEC did not complete the Statement of Budgetary Resources (SBR) reconciliation to SF-133 Report on Budget Execution and Budgetary Resources for the quarters ending December 31, 2006, March 31, 2007 and June 30, 2007 as required by OMB Circular A-136.

FEC is aware of these risks and the need for an integrated financial management system. Accordingly, they plan to migrate a significant portion of their accounting function to the General Services Administration (GSA) during fiscal year 2008. In preparation for the migration, FEC is working with GSA to determine the feasibility of linking external systems not yet integrated to PeopleSoft.

Recommendations:

1. Assess the extent of financial management system integration needed for existing systems while outsourcing the accounting operations to a third party service provider.

2. Implement control activities to compensate for the lack of an integrated financial management system and to ensure that accounting transactions are recorded correctly, timely, reviewed, and with adequate supporting documentation. Some of these control activities should include, but not limited to:
   - Improving preparation and review of procurement documents, including purchase requests, purchase orders/contracts, and related supporting documentation.
   - Improving analytical and quality control review of journal vouchers, reconciliations and the financial statements, including interim financial statement.
   - Implementing proper and timely cut-off controls for processing transactions and in preparing the financial statements to allow for management's timely analysis of financial data and for audit purposes.
   - Establish a timeline for timely receipt of completed accounts receivable schedules by the finance office from the program offices.

3. Ensure that the general ledger setup and posting model definitions are in compliance with the latest transaction posting consistent with USSGL guidance and policies for recording and classifying transactions.

4. Provide employee training on procurement, appropriation law, budget execution, and financial reporting requirements, as applicable, to ensure financial reporting and fund control policies are consistently and accurately executed.

5. Ensure that FEC complies with regulatory agencies' reporting requirements.

Management Response:

Management generally concurs with the finding and recommendations. FEC management is committed to resolving the issues noted and has begun to address the recommendations. For example, FEC has entered into an agreement with GSA, an OMB-certified Line of Business provider, for financial services. FEC management has also begun to identify training opportunities for its staff to enhance awareness of sound financial management practices. FEC management will develop a corrective action plan addressing issues identified.

SIGNIFICANT DEFICIENCY

II. Information Technology (IT) (Modified Repeat Finding)

A. Commission-Wide Security Administration

An entity-wide security program should be in place to establish a framework and continuing cycle of activity to manage security risk, develop security policies, assign responsibilities, and monitor the adequacy of computer security related controls. Without a well-designed program, security controls may be inadequate; responsibilities may be unclear, misunderstood, and improperly implemented; and controls may be inconsistently applied. Such conditions may lead to insufficient protection of sensitive or critical resources and disproportionately high expenditures for controls over low-risk resources.

During our Fiscal Year 2007 review of FEC's security program, we noted that FEC made progress in addressing prior years' findings, notably a contract was recently awarded to conduct a risk assessment of FEC's major applications and general support systems. The information obtained from this risk assessment will be used to adjust and fully implement its information classification, certification and accreditation policies.

However, at the time of this review, FEC's existing security program revealed weaknesses in controls that expose the FEC's financial management systems and data to unauthorized access and/or modification. Security weaknesses noted included:

- Risk assessments have not been performed as part of FEC's overall strategy to mitigate risks associated with its IT environment. **(Repeat Finding)**
- FEC has not fully implemented a framework of policies and standards to mitigate risks associated with the management of its information resources. Although FEC has implemented the majority of its information security policies, it has not fully implemented all of the related procedures and standards. FEC has not finalized and implemented an information classification policy, as well as its certification and accreditation policy. **(Repeat Finding)**
- FEC has created security plans for all of its major applications and mission critical general support systems. However, these security plans are not consistent with best practices "Risk Management Cycle", as they are not based on an assessment of the risks to FEC systems. **(Repeat Finding)**

- Major applications and mission critical general support systems have not been certified and accredited to ensure that they are operating according to FEC's security requirements. **(Repeat Finding).**
- FEC could not provide evidence to show that background investigations were performed timely for 3 out of the 10 newly hired employees that we sampled (30%). **(New Finding).**

Recommendations:

6. Perform risk assessments, as part of FEC's overall strategy to mitigate risks associated with its IT environment.

7. Finalize and implement FEC's information classification policy and certification and accreditation policy along with any accompanying standards.

8. Incorporate the results of risk assessments into FEC security plans.

9. Certify and accredit all major applications and mission critical general support systems.

10. Refine procedures to ensure that all newly hired employees undergo the appropriate background investigations commensurate with the risk level of their position. FEC should also ensure these investigations are initiated within a reasonable time of employment start date.

Management Response:

FEC agrees with the majority of elements within this finding and believes that conducting a comprehensive risk assessment is a prudent course of action and consistent with its Risk Management Policy. To that end, FEC has re-issued a previous "Request for Proposal" (RFP). The contract was recently awarded to conduct a risk assessment of FEC's major applications and general support systems. The information obtained from this risk assessment will be utilized to adjust and fully implement its information classification, and certification and accreditation policies. The data sensitivity and criticality information obtained will be incorporated into the appropriate FEC system security plans. This risk assessment contract deliverables include a risk remediation plan and strategy. This remediation plan will be incorporated into the overall ITD Corrective Action Plan (CAP).

The modified system security plans, risk assessment and the resulting risk remediation plan will be included as major components of the certification and accreditation package for senior management to analyze in its decision to provide either an Authorization To Operate (ATO) or an Interim Authorization To Operate (IATO).

B. Disaster Recovery and Continuity of Operations

Losing the capability to process and protect information maintained on FEC's computer systems can significantly impact FEC's ability to accomplish its mission. The purpose of disaster recovery and continuity of operations controls is to ensure that, when unexpected events occur, critical operations continue without interruption or critical operations are promptly resumed.

To achieve this objective, FEC should have procedures in place to protect information resources and minimize the risk of unplanned interruptions and a plan to recover critical operations should interruptions occur. These plans should consider activities performed at FEC's general support facilities (e.g. FEC's local area network, wide area network, and telecommunications facilities), as well as the activities performed by users of specific applications. To determine whether the disaster recovery plans will work as intended, FEC should establish and periodically test the capability to perform its functions in disaster simulation exercises.

Our review of the service continuity controls identified weaknesses that could affect FEC's ability to respond to a disruption in business operations after a disaster or other interruption. Details of the matter are as follows:

- FEC has not performed a business impact analysis (BIA) to formally identify and prioritize all critical data and operations on its networks and the resources needed to recover them if there was a major interruption or disaster. In addition, FEC has not established emergency processing priorities that will help manage disaster situations more effectively for the network. **(Repeat Finding)**
- FEC has not established an alternate processing site for its operations in the event of a disaster. **(Repeat Finding)**
- FEC's contingency plan is not comprehensive, as it does not include steps for recovering all FEC's major applications and mission critical general support systems. Additionally, the plan does not prioritize resources or set a timeframe for recovery. **(Repeat Finding)**
- FEC has not developed a continuity of operations plan (COOP) to support the continuation of its core mission in the event of a disaster that renders FEC's facilities unusable. **(Repeat Finding)**

Recommendations:

11. Perform a BIA to formally identify and prioritize all critical data and operations on FEC's networks and the resources needed to recover them if there is a major interruption or disaster.

12. Establish an alternate processing site and incorporate the results of the BIA into the contingency plan.

13. Develop a comprehensive contingency plan that incorporates the results of the BIA and includes the procedures and resources necessary to restore FEC systems in the event of a disaster. Ensure emergency processing priorities are established to assist in managing disaster situations, and ensure once developed, the plan is tested annually and updated based on the results of these tests.

14. Develop a COOP that addresses measures and procedures to follow in the event of a long-term interruption.

***Management* Response:**

FEC agrees that a formal BIA would be useful and recently awarded a contract to develop a comprehensive disaster recovery plan. A component of this contract is to assist FEC in formally identifying and prioritizing all critical data and operations on its networks and the resources needed to recover them in the event of a disaster. Determine gaps in current plans and strategies to close the identified gaps on a priority basis (i.e. risk, value derived, cost, time). The vender will then assist FEC with utilizing the data gleamed from this analysis to validate (and/or modify) its already established emergency processing priorities. FEC will ensure that all emergency processing priorities are prominently indicated in the resulting disaster recovery plan. The proposed plan will also include a testing plan and maintenance mechanism to ensure that the plan stays current.

Two additional components of this contract are to identify and prioritize those resources needed to develop a COOP and define the requirements needed to establish an alternate processing site.

C. Logical Access, System Software and Change Management Controls

Achieving an adequate level of information protection is highly dependent upon maintaining consistently effective access controls, system software and configuration management controls. Access controls limit and monitor access to computer resources (i.e., data files, application programs, and computer-related facilities and equipment) to the extent necessary to provide reasonable assurance that these resources are protected against waste, loss, unauthorized modification, disclosure, or misappropriation. Access controls include logical controls, such as security software programs designed to prevent or detect unauthorized access to sensitive files. Similarly, system software controls limit and monitor access to powerful programs and sensitive files that control computer processing and secure the application and data supported by the system, while change and configuration controls ensure all programs and program modifications are properly authorized, tested, and approved, and that access to and distribution of programs is carefully controlled. Without proper controls, there is a risk that security features could be inadvertently or deliberately omitted or "turned off" or that processing irregularities or malicious code could be introduced.

Our testing of internal controls identified weaknesses related to the information protection in FEC's information systems environment. These include FEC's midrange computer systems (e.g. servers) and applications. Weaknesses noted include the following:

- The PeopleSoft application is currently running on an Oracle Release 8i Relational Database Management System that is no longer supported by the vendor.
- Audit trail parameters for the Oracle database that supports the PeopleSoft application have not been set to ensure appropriate segregation of incompatible security responsibility and to provide necessary management oversight. Although

'auditing' is activated, the audit and archive logs are written to database tables and operating system logs respectively to which the database administrators (DBAs) have full access. This implies that the DBAs have the capability to purge these logs and remove possible evidence of database activity.

- FEC does not maintain documentation supporting timely approval and testing of patches and software upgrades prior to being moved into production.
- The PeopleSoft application does not have built-in functionality to enforce FEC's password policies. Furthermore, the mitigating controls implemented by FEC do not address the following PeopleSoft weaknesses:
  - PeopleSoft does not have an account lockout policy.
  - PeopleSoft does not prevent users from using previous passwords.
  - PeopleSoft does not have the ability to enforce strong password requirements.
- FEC does not properly monitor access to its networks, systems and physical facility:
  - Six out of 10 separated employees still have active network accounts.
  - Three out of 10 LAN accounts have not logged on for more than 90 days.
  - One out of 10 LAN accounts has not changed its password in 180 days.
  - Two out of 10 LAN accounts have not logged on for more than 90 days and have not changed their passwords in 180 days.
  - Access documentation is not maintained for system administrators and database administrators. Additionally, administrator privileges are not periodically reviewed for appropriateness. FEC's current policy is to grant employees access based on their positions. Only employees hired to perform administrative functions are granted administrative access.

Recommendations:

15. Transfer processing to a service provider or update existing platform to vendor-supported versions/releases.

Management Response:

FEC has evaluated four approved agencies for a Line of Business (LOB) solution and selected the General Services Administration (GSA) as its service provider. FEC has finalized its decision regarding moving its financial, human resources, travel services and procurement activities to GSA's LOB by signing an Interagency Agreement. GSA's LOB solution will replace the FEC PeopleSoft application thus eliminating the discrepancies described in this finding.

16. Write audit trails related to DBA activity to Operating Systems logs and limit DBA's access to these logs.

Management Response:

Although the FEC has a process in place to trace any and all (attempted and successful) transactions which may occurs in its Oracle databases, it concurs that implementing additional separation of duty controls will assist in eliminating the possibility that a *database administrator could purge auditing logs to hide inappropriate actions. To this end, the FEC recently implemented a process whereby database administrators have been restricted to read only access to Oracle audit log files.*

17. Maintain documentation to support the testing and approval of system software changes.

Management Response:

Although FEC believes its recently issued patch management standard is sufficient, the process of maintaining supporting documentation to support the standard can be improved. In an effort to improve this process, the FEC will issue patch management standard reminders to its technical personnel. In addition, the FEC will add reviewing patch management supporting documentation to its Security Review Policy to ensure that supporting documentation is properly maintained.

18. Develop additional mitigating controls to ensure that PeopleSoft passwords are in agreement with FEC policy or ensure that if PeopleSoft processing is outsourced, the third party maintains password controls that comply with FEC password policies.

Management Response:

Although FEC has developed compensating controls to reduce the risk associated with this finding, it concurs that the PeopleSoft application does not meet the requirements specified in FEC's Password Policy. With this in mind and understanding the limitations of the current version of PeopleSoft utilized at FEC, the Password Policy is being amended to allow an exemption for the PeopleSoft application.

In addition, the FEC selection of GSA's LOB financial solution will replace the FEC PeopleSoft application thus eliminating the discrepancies described in this finding.

19. Promptly terminate access to FEC resources for separated employees. Procedures should be documented and implemented to coordinate separations between Human Resources and IT management to ensure user accounts are immediately disabled upon termination.

20. Utilize access request forms that identify the user's access level to document user access rights to all FEC systems and facilities. Additionally, FEC should periodically review and recertify user access to ensure current access is commensurate with job responsibilities.

Management Response:

Although the FEC has a documented process in place to terminate FEC resources for separated employees, it concurs that this process can be improved. To this end, the FEC recently awarded a contract to develop and implement an automated HR New Personnel Workflow Process.

The New Personnel Workflow Process will include full time employees, interns, and contractors and eliminate the discrepancies described in this finding. The new process will track staff from the start of their employment at FEC to exit and allow managers to request and document any changes in network and application access. This new process will enable a higher degree of coordination between HR and ITD to ensure that user accounts are disabled upon exiting per FEC policy. The new process will retain all historical information regarding account creation, changes to access rights, system resources, and termination information regarding a particular account.

OTHER MATTER

OMB Bulletin No. 07-04 requires that the auditor's report on internal control "identify those material weaknesses disclosed by the audit that were not reported in the reporting entity's Federal Managers' Financial Integrity Act (FMFIA) report." The FEC's schedule of material weaknesses and non-conformances included in the Performance and Accountability Report did not identify the material weakness noted in this report. We do not believe, however, that failure to report the material weaknesses in FMFIA constitutes a separate reportable condition or a material weakness because different criteria are used by management and the auditors in determining material weaknesses.

STATUS OF PRIOR YEAR CONDITIONS

We have reviewed the status of the FEC's corrective actions with respect to the findings and recommendations from the prior year's report on internal controls. We have attached Appendix A to our report that presents the status of prior year findings and recommendations.

****

FEC's response to the material weakness and significant deficiency identified in our audit is presented within the body of our report. We did not audit the FEC's response and, accordingly, we express no opinion on it.

In addition to the material weakness and significant deficiency described above, we noted certain matters involving internal control and its operation that we reported to the management of the FEC in a separate letter dated November 13, 2007.

This report is intended solely for the information and use of the management of the FEC, the FEC Office of Inspector General, Government Accountability Office, the OMB, and the U.S. Congress, and is not intended to be and should not be used by anyone other than these specified parties.

Clifton Gunderson LLP

Calverton, Maryland
November 13, 2007

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APPENDIX A
FEDERAL ELECTION COMMISSION
STATUS OF PRIOR YEAR FINDINGS AND RECOMMENDATIONS
September 30, 2007

PY Rec. No.	Condition/Audit Area	Recommendation	Current Status[1]
		Material Weaknesses	
I. Program Cost Allocation			
1	Cost Allocation Methodology	Revise the account lockout threshold in TRS to five invalid attempts.	Closed
2	Cost Allocation Methodology	Establish written policies and procedures to ensure that employees enter their time in the cost system timely and properly and the results are supported by source data which is reviewed and approved by management	Closed
3	Cost Allocation Methodology	Ensure correct and consistent application of the cost allocation process in accordance with the cost system user manual and conceptual design document.	Closed
4	Cost Allocation Methodology	Ensure errors in TRS causing the system to allocate hours for the Information Division to the wrong program are resolved.	Closed
II. General Property and Equipment			
5	Property, Plant and Equipment	Improve analytical and quality control review of subsidiary schedules, journal vouchers and property reconciliation to ensure material errors and differences are identified and resolved timely.	Closed
6	Property, Plant and Equipment	Use correct USSGL.	Closed
7	Property, Plant and Equipment	Develop a mechanism for reconciling individual property items in the property system to the bulk purchases recorded in the general ledger to ensure completeness of the property system records. Also, ensure that the property management system has complete information, such as bar code identification, serial number and location of the asset.	Closed
8	Property, Plant and Equipment	Clearly document physical inventory procedures, results of the physical inventory, and the reconciliation performed. Maintain the documentation for audit trail and management review purposes.	Updated – reported in current year management letter

[1] Updated recommendation can be considered closed since a new recommendation has been proposed in current year's Auditor's Report on Internal Control or management letter.

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FEDERAL ELECTION COMMISSION
STATUS OF PRIOR YEAR FINDINGS AND RECOMMENDATIONS
September 30, 2007

PY Rec. No.	Condition/Audit Area	Recommendation	Current Status[1]
9	Property, Plant and Equipment	Establish a standard process, mechanism or policies to ensure [offices and divisions] notify the Finance Office of the acquisition and disposition of property assets.	Updated – reported in current year management letter.
10	Property, Plant and Equipment	Perform a monthly analysis of property as part of the monthly analysis of financial activities.	Closed
		Reportable Conditions	
III. Information Technology			
11	Entity-Wide Security	Complete the documentation approval and implementation of an entity-wide security program plan.	Open – reported in current year significant deficiency
12	Entity-Wide Security	Finalize and implement FEC's information classification policy and certification and accreditation policy along with any accompanying standards.	Open – reported in current year significant deficiency
13	Entity-Wide Security	Perform risk assessments, as part of FEC's overall strategy to mitigate risks associated with its IT environment.	Open – reported in current year significant deficiency
14	Entity-Wide Security	Incorporate the results of the risk assessments into FEC's security plans.	Open – reported in current year significant deficiency
15	Entity-Wide Security	Classify information resources in accordance with the risk assessments.	Open – reported in current year significant deficiency
16	Entity-Wide Security	Utilize corrective action plans for all reviews of security controls whether performed internally or by a third party.	Closed

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STATUS OF PRIOR YEAR FINDINGS AND RECOMMENDATIONS
September 30, 2007

PY Rec. No.	Condition/Audit Area	Recommendation	Current Status[1]
17	Entity-Wide Security	Ensure that corrective action plans identify the task to be completed in addition to identifying the resources required to accomplish the elements of the plan, any milestones in meeting the tasks, and scheduled completion dates for the milestones.	Closed
18	Entity-Wide Security	Certify and accredit all major applications and mission critical general support systems.	Open – reported in current year significant deficiency
19	Contingency Planning	Perform a BIA to formally identify and prioritize all critical data and operations on FEC's networks and the resources needed to recover them if there is a major interruption or disaster.	Open – reported in current year significant deficiency
20	Contingency Planning	Ensure that emergency processing priorities are established to assist in managing disaster situations more effectively for the network and include business owners in the discussion to determine how much backup data is needed on-hand to minimize the impact of a disaster.	Open – reported in current year significant deficiency
21	Contingency Planning	Establish an alternative processing site for FEC's operations in the event of a disaster and ensure that an operational mechanism exists to update the disclosure database in the event that FEC's database is unavailable to replicate the disclosure database resident at the off-site location.	Open – reported in current year significant deficiency
22	Contingency Planning	Develop and document a comprehensive COOP of FEC's data centers, networks, and telecommunication facilities.	Open – reported in current year significant deficiency
23	Contingency Planning	Develop a COOP to support the continuation of FEC's core mission in the event of a disaster that renders FEC's facilities unusable.	Open – reported in current year significant deficiency

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FEDERAL ELECTION COMMISSION
STATUS OF PRIOR YEAR FINDINGS AND RECOMMENDATIONS
September 30, 2007

PY Rec. No.	Condition/Audit Area	Recommendation	Current Status[1]
24	Controls to Protect Information	Finalize and implement FEC's process to manually review logs of users using budgetary overrides where the reviewer is an individual who does not have access to utilize the overrides.	Closed
25	Controls to Protect Information	Develop mitigating controls to ensure that PeopleSoft passwords are in agreement with FEC's policy or ensure that when PeopleSoft processing is outsourced, the third-party maintains password controls that comply with FEC's password policies.	Open – reported in current year significant deficiency
26	Controls to Protect Information	Use access request forms that identify the user's access level to document user access rights to all FEC's systems. Additionally, FEC should periodically review the appropriateness of access granted and recertify user access rights.	Closed
27	Controls to Protect Information	Investigate to determine a baseline level of auditing that can be performed without causing a detrimental impact to the performance of the Oracle databases and the applications that they support.	Closed
28	Controls to Protect Information	Periodically review data center access and remove unnecessary access rights.	Closed
29	Software Development and Change Controls	Implement formal policies and procedures for managing system software changes.	Closed
30	Software Development and Change Controls	Maintain documentation to support the testing and approval of system software changes.	Open – reported in current year significant deficiency
31	Software Development and Change Controls	Complete the migration of financial processing to a third-party service provider and verify that the service provider is utilizing vendor supported system software version.	Open – FEC has plans to migrate to a third party service provider in FY 2008.

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FEDERAL ELECTION COMMISSION
STATUS OF PRIOR YEAR FINDINGS AND RECOMMENDATIONS
September 30, 2007

PY Rec. No.	Condition/Audit Area	Recommendation	Current Status[1]
IV. Integrated Financial Management System			
32	Integrated Financial Management System	Evaluate the extent of systems integration needed for existing systems when considering the outsourcing of the FEC's accounting services to a shared service provider.	Updated – reported in current year material weakness
V. Administrative Fines, Civil Penalties and Miscellaneous Receipts			
33	Administrative Fines, Civil Penalties and Miscellaneous Receipts	Implement policies and procedures for reviewing the accounts receivable schedules for reasonableness and accuracy prior to recording related account transactions in the general ledger.	Closed
34	Administrative Fines, Civil Penalties and Miscellaneous Receipts	Formalize policies and procedures for performing accounts receivable reconciliations. While developing these procedures, the FEC should consider establishing a timeline for when the reconciliations should be finalized by the program offices and forwarded to the Finance Office.	Updated – reported in current year material weakness
35	Administrative Fines, Civil Penalties and Miscellaneous Receipts	Document all the methodologies applied in calculating allowances for uncollectible accounts. Periodically review the methodologies against actual procedures performed and revise them as necessary.	Updated – reported in current year management letter
VI. Controls Over Procurement and Disbursement Transactions			
36	Procurement and Disbursement	Issue formal guidance for performing corrective action when negative obligation balances occur. Procedures should describe the conditions when corrective action is needed, corrective actions to perform and the individuals responsible for resolving the error. The timely response and clear communication on corrective action should also be included in the procedures.	Closed
37	Procurement and Disbursement	Ensure documentation related to procurement and disbursement actions are properly approved and supported. Procurement policies and procedures should be enhanced to document, completely and clearly, operating procedures for the procurement cycle and should include procedures for documenting justification when exceptions are made to established procedures.	Updated – Reported in current year management letter

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STATUS OF PRIOR YEAR FINDINGS AND RECOMMENDATIONS
September 30, 2007

PY Rec. No.	Condition/Audit Area	Recommendation	Current Status[1]
38	Procurement and Disbursement	Ensure reconciliations are consistently performed, reviewed and approved in a timely manner.	Closed
39	Audit Follow-up	Formalized the remediation process related to audit findings and recommendations that is consistent with OMB Circular A-50 guidelines.	Updated – reported in current year management letter

BALANCE SHEET
As of September 30, 2007 and 2006 (in Dollars)

Assets (Note 2)	2007	2006
Intragovernmental:		
Fund balance with Treasury (Note 3)	$ 10,250,297	$ 10,068,481
Total Intragovernmental Assets	10,250,297	10,068,481
Accounts receivable, net (Notes 2 & 4)	817,309	520,471
General property and equipment, net (Note 5)	7,745,134	8,757,157
Advances to others	6,927	–
Total assets	**$ 18,819,667**	**$ 19,346,109**
Liabilities (Note 6)		
Intragovernmental:		
Accounts payable	$ –	$ 50,000
Employer contribution and payroll taxes payable	297,573	290,119
Custodial liability	807,032	976,525
Payable to Treasury	10,277	–
Total Intragovernmental	1,114,882	1,316,644
With the public:		
Accounts payable	901,977	864,387
Accrued payroll and benefits	1,143,513	1,105,617
Unfunded leave	1,964,478	1,931,980
Other	663	30,312
Total liabilities	**5,125,513**	**5,248,940**
Net Position		
Unexpended appropriations - Other Funds	7,912,472	7,289,060
Cumulative results of operations - Other Funds	5,781,682	6,808,109
Total net position	**13,694,154**	**14,097,169**
Total liabilities and net position	**$ 18,819,667**	**$ 19,346,109**

The accompanying notes are an integral part of these statements.

STATEMENT OF NET COST

For the Years Ended September 30, 2007 and 2006 (in Dollars)

Program costs:	**2007**	**2006**
Administering and enforcing the *FECA*	$ 56,599,698	$ 55,906,556
Less: Earned revenue	(222,137)	–
Net cost of operations (Note 9)	**$ 56,377,561**	**$ 55,906,556**

The accompanying notes are an integral part of these statements.

STATEMENT OF CHANGES IN NET POSITION

For the Years Ended September 30, 2007 and 2006 (in Dollars)

	2007 Consolidated Total	2006 Consolidated Total
Cumulative Results of Operations:		
Beginning balances	$ 6,808,109	$ 8,064,275
Beginning balances, as adjusted	6,808,109	8,064,275
Budgetary Financing Sources		
Appropriations used	53,029,611	52,297,571
Transfers in-out without reimbursement	(10,277)	–
Other Financing Sources (Non-Exchange):		
Imputed financing from costs absorbed by others	2,331,800	2,352,819
Total Financing Sources	55,351,134	54,650,390
Net Cost of Operations	(56,377,561)	(55,906,556)
Net Change	(1,026,427)	(1,256,166)
Cumulative Results of Operations	**$ 5,781,682**	**$ 6,808,109**
Unexpended Appropriations:		
Beginning Balances	7,289,060	5,821,556
Beginning Balances, as adjusted	7,289,060	5,821,556
Budgetary Financing Sources:		
Appropriations received	54,527,516	54,700,000
Other adjustments	(874,493)	(934,925)
Appropriations used	(53,029,611)	(52,297,571)
Total Budgetary Financing Sources	623,412	1,467,504
Total Unexpended Appropriations	**7,912,472**	**7,289,060**
Net Position	**$ 13,694,154**	**$ 14,097,169**

The accompanying notes are an integral part of these statements.

STATEMENT OF BUDGETARY RESOURCES
For the Years Ended September 30, 2007 and 2006 (in Dollars)

	2007	2006
Budgetary Resources (Note 10)		
Unobligated balance, brought forward, October 1	$ 2,078,695	$ 1,794,495
Recoveries of prior year obligations	1,352,281	967,661
Budget authority:		
Appropriations received	54,527,516	54,700,000
Spending authority from offsetting collections: Earned		
Collected	211,860	–
Accounts receivable	10,277	–
Transfer in/out without reimbursement	(10,277)	–
Permanently not available:	(874,493)	(934,925)
Total Budgetary Resources	**$ 57,295,859**	**$ 56,527,231**
Status of Budgetary Resources		
Obligations Incurred		
Direct	$ 54,255,141	$ 54,448,901
Reimbursable	211,860	–
Total Obligations Incurred	**54,467,001**	**54,448,901**
Unobligated balance		
Apportioned	220,350	108,327
Total Unobligated Balance	220,350	108,327
Unobligated balance not available	2,608,508	1,970,003
Total Status of Budgetary Resources	**$ 57,295,859**	**$ 56,527,231**
Change in Obligated Balance:		
Obligated balance, net		
Unpaid obligations, brought forward, October 1	$ 7,521,417	$ 6,520,709
Obligations incurred net	54,467,001	54,448,901
Less: Gross outlays	(53,215,541)	(52,480,532)
Less: Recoveries of prior year unpaid obligations, actual	(1,352,281)	(967,661)
Obligated balance, net, end of period		
Unpaid obligations	7,420,596	7,521,417
Total, unpaid obligated balance, net, end of period	7,420,596	7,521,417
Net Outlays		
Gross outlays	53,215,541	52,480,532
Less: Offset collections	(222,137)	–
Less: Distributed offsetting receipts	(215,677)	–
Net outlays	**$ 52,777,727**	**$ 52,480,532**

The accompanying notes are an integral part of these statements.

STATEMENT OF CUSTODIAL ACTIVITY

For the Years Ended September 30, 2007 and 2006 (in Dollars)

	2007	2006
Revenue Activity:		
Sources of Cash Collections:		
Miscellaneous Receipts	$ 215,677	$ 373,669
Civil Penalties	4,135,632	5,960,484
Administrative Fees	393,669	174,924
Total Cash Collections	4,744,978	6,509,077
Accrual Adjustments	286,560	93,321
Total Custodial Revenue (Note 11)	**$ 5,031,538**	**$ 6,602,398**
Disposition of Collections:		
Transferred to Treasury	$ 4,744,978	$ 6,303,190
Amount Yet to be Transferred	286,560	299,208
Total Disposition of Collections	**$ 5,031,538**	**$ 6,602,398**
Retained by FEC	**$ –**	**$ –**
Net Custodial Activity	**$ –**	**$ –**

The accompanying notes are an integral part of these statements.

NOTES TO THE FINANCIAL STATEMENTS

Note 1 – Summary of Significant Accounting Policies

Reporting Entity

The Federal Election Commission (FEC or Commission) was created in 1975 as an independent regulatory agency with exclusive responsibility for administering, enforcing, defending and interpreting the *Federal Election Campaign Act* (*FECA*) *of 1971*, 2 U.S.C. 431 et seq., as amended by the *Bipartisan Campaign Reform Act* of 2002 (*BCRA*), Pub. L. 107–155, 116 Stat. 81 (2002) ("the Act"). The Commission is also responsible for administering the public funding programs (26 U.S.C.) for presidential campaigns and conventions, which includes certification and audits of all participating candidates and committees, and enforcement of public funding legislation.

The financial activity presented relates primarily to the execution of the FEC congressionally approved budget. Consistent with Federal Accounting Standards Advisory Boards' (FASAB) Statement of Federal Financial Accounting Concept No. 2, "Entity and Display," the Presidential Election Campaign Fund ("the fund") is not a reporting entity of the FEC. Financial activity of the funds is budgeted, apportioned, recorded, reported and paid by the Department of Treasury, and therefore, the accounts of the Presidential Election Campaign Fund are not included in the FEC's financial statements.

Basis of Accounting and Presentation

As required by the Accountability of Tax Dollars Act of 2002, the accompanying financial statements present the financial position, net cost of operations, changes in net position, budgetary resources, and custodial activity of the FEC. While these financial statements have been prepared from the books and records of the FEC in accordance with U.S. generally accepted accounting principles (GAAP) and in accordance with the form and content for entity financial statements specified by the Office of Management and Budget (OMB) in Circular A-136, as revised, Financial Reporting Requirements, as well as the accounting policies of the FEC, the statements may differ from other financial reports submitted pursuant to OMB directives for the purpose of monitoring and controlling the use of the FEC's budgetary resources. Generally Accepted Accounting Principles for federal entities are the standards prescribed by the Federal Accounting Standards Advisory Board (FASAB), which is the official body for setting the accounting standards of the federal government.

These financial statements reflect both accrual and budgetary accounting transactions. Under the accrual method of accounting, revenues are recognized when earned and expenses are recognized when a liability is incurred, without regard to receipt or payment of cash. Budgetary accounting is designed to recognize the obligation of funds according to legal requirements. Budgetary accounting is essential for compliance with legal constraints and controls over the use of federal funds.

Throughout these financial statements, assets, liabilities, revenues, and costs have been classified according to the type of entity with which the transactions are associated. Intra-governmental assets and liabilities are those from or to other federal entities. Intra-governmental earned revenues are collections or accruals of revenue from other federal entities and intra-governmental costs are payments or accruals to other federal entities. These statements should be read with the understanding that they are for a component of the U.S. Government, a sovereign entity.

Reclassifications

Certain prior year balances were reclassified to conform to current year presentation. The FEC updated its strategic plan, which now reflects one strategic goal and three objectives. Accordingly, and consistent with OMB Circular A-136, as revised, and OMB Circular A-11, Preparation, Submission and Execution of the Budget, the Statement of Net Cost (SNC) was revised to reflect management's definition of its operations. To be consistent with the FY 2007 presentation, the three responsibility segments reflected in the FY 2006 SNC were consolidated and reclassified as one program. Except for the SNC, this reclassification had no impact on the financial statements, and there was no net effect on the total net costs for FY 2006.

The FEC revised its methodology in determining the intragovernmental costs. Accordingly, Note 9 – Statement of Net Cost for FY 2006 was reclassified to be consistent with the new methodology applied for FY 2007.

The presentation of the Statement of Financing (SOF) has been revised, effective this fiscal year, to comply with OMB Circular A-136, revised, which provided for the SOF to no longer be considered a basic statement. Instead, the SOF is required to be displayed in the notes and referred to as "Reconciliation of Net Cost of Operations to Budget" rather than the SOF. Accordingly, certain reclassifications were made to the previously issued FY 2006 SOF to conform to the new format.

Assets

Assets that an entity is authorized to use in its operations are termed entity assets, while assets that are held by an entity and are not available for the entity's use are termed non-entity assets. Most of the FEC's assets are entity assets and are available to carry out the mission of the FEC. The FEC also has non-entity assets, which primarily consist of receipts from fines. These funds are not available to use in its operations and must be transferred to the U.S. Treasury.

Fund Balance with Treasury

The FEC does not maintain cash in commercial bank accounts. The U.S. Treasury processes cash receipts and disbursements. Funds with the U.S. Treasury consist of appropriated, deposited funds, and custodial collections. With the exception of the custodial collections, these funds are available to pay current liabilities and finance authorized purchase commitments. Custodial collections, which are not available to finance FEC activities, are classified as non-entity assets.

Accounts Receivable

The FEC's accounts receivable represent amounts due from the public or the U.S. Treasury for fines and penalties assessed by the FEC and referred to Treasury for collection. The FEC establishes an allowance for the loss on accounts receivable from the public that are deemed uncollectible accounts, which is included in Accounts Receivable on the balance sheet. The allowance is a percentage of the overall receivable balance and the collection rate of past balances.

General Property and Equipment

General Property and Equipment (P&E) is reported at acquisition cost. The capitalization threshold is established at $25,000 and a useful life of 2 or more years. For bulk purchases, items are capitalized when the individual useful lives are at least two years and have an aggregate value of $250,000 or more. The bulk purchase capitalization threshold is a new policy that was implemented in FY 2007. Acquisitions of P&E that do not meet the capitalization criteria are recorded as operating expenses. General P&E consists of items that are used by FEC to support its mission. Depreciation on these assets is calculated using the straight-line method with no salvage value. Depreciation begins the month after the asset is placed in service. Maintenance, repairs and minor renovations are expensed as incurred. Expenditures that materially increase values, change capacities or extend useful lives are capitalized.

The headquarters building in which the FEC operates is leased through the General Services Administration (GSA) under an occupancy agreement, which manages the lease agreement between the federal government and the commercial entity. FEC is billed by GSA for the leased space based upon estimated lease payments made by GSA plus an administrative fee. The cost of the headquarters building is not capitalized. The costs of any leasehold improvements, which are managed through GSA, are financed with FEC appropriated funds. Construction costs of $25,000 or more are accumulated as Construction in Progress until completion and then are transferred and capitalized as a Leasehold Improvement over 7 years or the remainder of the lease, whichever is less.

Internal use software development and acquisition costs of $25,000 are capitalized as software development in progress until the development stage is completed and the software successfully tested. At acceptance, software development-in-progress costs are reclassified as internal use software costs and amortized using the straight-line method over an estimated useful life of 5 years. Purchased commercial software that does not meet the capitalization criteria is expensed. Enhancements which do not add significant new capability or functionality are expensed.

Liabilities

Liabilities represent amounts that are likely to be paid by the FEC as the result of transactions or events that have already occurred; however, no liabilities are paid by the FEC without an appropriation. Intragovernmental liabilities arise from transactions with other federal entities. Liabilities classified as not covered by budgetary resources are liabilities for which appropriations have not been enacted (e.g., annual leave benefits and actuarial liability under the Federal Employees Compensation Act), and liabilities resulting from the agency's custodial activities. FEC also has an intragovernmental liability to the U.S.Treasury for fines and miscellaneous receipts collected from the public but not yet transferred. These funds may not be used to fund FEC operations.

Accounts Payable

Accounts payable consist of liabilities to commercial vendors and contractors for amounts owed for goods, services, and other expenses received but not yet paid at the end of the fiscal year. Accounts payable also consist of disbursements in transit that have been recorded by the FEC but not paid by the U.S. Treasury.

Accrued Payroll and Benefits

Accrued payroll and benefits represents salaries, wages and benefits earned by employees, but not disbursed as of September 30, 2007. Accrued payroll and benefits are payable to employees and are therefore not classified as intragovernmental.

Liabilities Not Covered by Budgetary Resources

Liabilities represent the amount of monies or other resources that are likely to be paid by the FEC as a result of a transaction or event that has already occurred. Liabilities for which an appropriation has not been enacted are classified as Liabilities Not Covered by Budgetary Resources.

Annual, Sick and Other Leave

Annual leave is recorded as a liability when it is earned; the liability is reduced as leave is taken. Each quarter, the balance in the accrued leave account is adjusted to reflect current leave balances and pay rates. Accrued annual leave is paid from future funding sources and accordingly is reflected as a liability not covered by budgetary resources. Sick leave and other types of non-vested leave are expensed as taken.

Federal Employee Benefits

A liability is recorded for estimated and actual future payments to be made for workers' compensation pursuant to the *Federal Employees Compensation Act* (*FECA*). The liability consists of the net present value of estimated future payments calculated by the Department of Labor (DOL) and the actual unreimbursed cost paid by DOL for compensation paid to recipients under this *FECA*. The future workers' compensation estimate was generated by DOL from an application of actuarial procedures developed to estimate the liability for *FECA*, which includes the expected liability for death, disability, medical, and miscellaneous costs for approved compensation cases. The liability is calculated using historical benefit payment patterns related to a specific incurred period to predict the ultimate payments related to that period. These projected annual benefits payments were discounted to present value.

Employee Retirement Plans

FEC employees participate in either the Civil Service Retirement System (CSRS) or the Federal Employees Retirement System (FERS), which became effective on January 1, 1987. Most FEC employees hired after December 31, 1983, are automatically covered by FERS and Social Security. For employees covered by CSRS, the FEC withheld 7.0 percent of base pay earnings. The FEC matches this withholding, and the sum of the withholding and the matching funds is transferred to the Civil Service Retirement System.

For each fiscal year, the Office of Personnel Management (OPM) calculates the U.S. Government service cost for covered employees, which is an estimate of the amount of funds that, if accumulated annually and invested over an employee's career, would be enough to pay that employee's future benefits. Since the U.S. Government's estimated service cost exceeds contributions made by employer agencies and covered employees this plan is not fully funded by the FEC and its employees. For 2007 and 2006, FEC recognized approximately $2.3 million and $2.4 million, respectively, as of September 30, as an imputed cost and as an imputed financing source for the difference between the estimated service cost and the contributions made by FEC and its employees.

FERS contributions made by employer agencies and covered employees exceed the U.S. Government's estimated service costs. For FERS covered employees the FEC made contributions of 10.7 percent of basic pay. Employees participating in FERS are covered under the Federal Insurance Contribution Act (FICA) for which the FEC contributes a matching amount to the Social Security Administration.

Thrift Savings Plan (TSP)

The Thrift Savings Plan (TSP) is a retirement savings and investment plan for employees covered by either CSRS or FERS. The TSP is administered by the Federal Retirement Thrift Investment Board on behalf of federal agencies. For employees belonging to FERS, the FEC automatically contributes one percent of base pay to their account and matches contributions up to an additional four percent. For employees belonging to CSRS, there is no governmental matching contribution.

The FEC does not report on its financial statements CSRS and FERS assets, accumulated plan benefits, or unfunded liabilities, if any, which may be applicable to FEC employees. Reporting such amounts is the responsibility of the Office of Personnel Management. The portion of the current and estimated future outlays for CSRS not paid by the FEC is, in accordance with Statement of Federal Financial Accounting Standards (SFFAS) No. 5, Accounting for Liabilities of the Federal Government, included in the FEC's financial statements as an imputed financing source.

Commitments and Contingencies

Commitments are contractual agreements involving financial obligations. The FEC is committed for goods and services that have been ordered, but have not yet been received.

A contingency is an existing condition, situation, or set of circumstances involving uncertainty as to possible gain or loss. The uncertainty will ultimately be resolved when one or more future events occur or fail to occur. A contingent liability is recognized when a past event or exchange transaction has occurred, and future outflow or other sacrifice of resources is measurable and probable. A contingency is not disclosed when any of the conditions for liability recognition are met but the chance of the future event or events' occurring is remote. A contingency is disclosed when any of the conditions for liability recognition are not met and the chance of the future confirming event or events occurring is more than remote but less than probable.

Revenues and Other Financing Sources

Annual Appropriation

The FEC received the majority of its funding through an annual appropriation as provided by Congress. Also, the FEC, in FY 2007, received authority from Congress to collect registration fees for FEC hosted conferences and apply these funds to its account, which are available to the FEC without further appropriation for the costs of carrying out it conferences.

Imputed Financing Sources

In accordance with OMB Circular A-136, all expenses should be reported by agencies whether or not these expenses would be paid by the agency that incurs the expense. The amounts for certain expenses of the FEC, which will be paid by other federal agencies, are recorded in the SNC. A corresponding amount is recognized in the "Statement of Changes in Net Position" as an "Imputed Financing Source." These imputed financing sources primarily represent unfunded pension costs of FEC employees, as described above.

Statement of Net Cost

The SNC presents one program, which is based on the FEC's mission and strategic goal as outlined in the revised strategic plan. The major program that reflects this strategic goal is summarized as: Administer and enforce the *FECA* efficiently and effectively.

Earned Revenue

Earned revenues include fees for seminars and conferences held during the year.

Net Position

Net position is the residual difference between assets and liabilities and is comprised of unexpended appropriations and cumulative results of operations. Unexpended appropriations represent appropriated spending authority that is unobligated and has not been withdrawn by the U.S. Treasury, and obligations that have not been paid. Unobligated balances associated with appropriations that expire at the end of the fiscal year remain available for obligation adjustments, but not for new obligations, until that account is closed, five years after the appropriations expire. Cumulative results of operations represent the excess of financing sources over expenses since inception.

Statement of Custodial Activity

The Statement of Custodial Activity summarizes collections transferred or transferable to the U.S. Treasury or other parties for miscellaneous receipts, fines and penalties. These amounts are reported as custodial revenue and are not available for FEC operations.

Use of Estimates

The preparation of accompanying financial statements in accordance with generally accepted accounting principles requires management to make certain estimates and assumptions that directly affect the reported assets, liabilities, revenues, and expenses. Actual results could differ from these estimates.

Note 2 – Non-Entity Assets

Non–entity assets, which primarily represent receipts resulting from the FEC imposing civil penalties on those that violated the requirements of the *Federal Election Campaign Act*, consist of the following at September 30:

	2007	2006
Intragovernmental:		
Fund Balance with Treasury (Custodial)	$ –	$ 456,054
With the Public:		
Accounts Receivable – Custodial	807,032	520,471
Accounts Receivable – Conference Fees	10,277	–
Total non-entity assets	817,309	976,525
Total entity assets	18,002,358	18,369,584
Total Assets	$ 18,819,667	$ 19,346,109

Note 3 – Fund Balance with Treasury

Fund balances with Treasury consisted of the following at September 30:

	2007	2006
Fund Balance with Treasury:		
Appropriated Funds	$ 10,250,297	$ 9,612,427
Custodial	–	456,054
Total Fund Balance with Treasury	$ 10,250,297	$ 10,068,481

Status of Fund Balance with Treasury	2007	2006
Unobligated Balance		
Available	$ 220,350	$ 108,327
Unavailable	2,608,508	1,970,003
Obligated Balance not yet disbursed	7,421,439	7,534,097
Non-Budgetary Fund Balance with Treasury		
Custodial Funds not yet transferred to Treasury	–	456,054
Total Status of Fund Balance with Treasury	$ 10,250,297	$ 10,068,481

Available unobligated balances represent amounts that are apportioned for obligation in the current fiscal year. Unavailable unobligated balances represent amounts that are not apportioned for obligation during the current fiscal year and expired appropriations that are no longer available to incur new obligations. Obligated balances not yet disbursed include undelivered orders unpaid and expended authority unpaid.

Note 4 –
Accounts Receivable, net

All accounts receivable are with the public and consist of the following at September 30:

	2007		
	Gross Accounts Receivable	Allowance	Net Accounts Receivable
With the Public			
Penalties and Miscellaneous Receipts	$ 1,443,300	$ 636,268	$ 807,032
Conference Fees	10,277	–	10,277
Total Non-Entity	$ 1,453,577	$ 636,268	$ 817,309

	2006		
	Gross Accounts Receivable	Allowance	Net Accounts Receivable
With the Public			
Penalties and Miscellaneous Receipts	$ $1,074,698	$ $ 554,227	$ $ 520,471
Total Non-Entity	$ $1,074,698	$ $ 554,227	$ $ 520,471

Non-Entity receivables consist of civil penalties assessed by FEC through its enforcement processes or conciliation agreements reached with parties. FEC has three offices that administer the penalties: the Office of General Counsel (OGC); the Office of Administrative Review (OAR); and the Office of Alternative Dispute Resolution (ADR). Each office has a distinct role in the enforcement and collection process. The allowance is based on the historical rate of collection and an overall assessment of the debtors' willingness and ability to pay. Furthermore, debts administered by OAR are referred to the U.S. Treasury for collection when delinquent. Debts administered by the OGC and ADR are not considered delinquent, under the definition of the Debt Collection Improvement Act of 1996, and are therefore not referred to the U.S. Treasury. The terms of the agreement between the FEC and the parties establish the conditions for collection.

In FY 2007, the FEC received authorization to collect fees for its conferences. Accordingly, a receivable pertaining to the fees associated with these conferences as of September 30, 2007 was $10,277. There were no conferences held in FY 2006.

Note 5 –
General Property and Equipment, Net

The general components of capitalized property and equipment, net of accumulated depreciation, consisted of the following as of September 30, 2007 and 2006:

2007

Asset Class	Service Life (years)	Acquisition Value	Accumulated Depreciation	Net Book Value
Software	5	$ 14,315,296	$ 9,112,519	$ 5,202,777
Computers and peripherals	3 to 5	4,139,404	3,280,787	858,617
Leasehold Improvements	7 or less	5,116,757	5,116,757	–
Furniture	7	852,754	594,480	258,274
Software-in-Development	n/a	1,425,466	–	1,425,466
Total		$ 25,849,677	$ 18,104,543	$ 7,745,134

2006

Asset Class	Service Life (years)	Acquisition Value	Accumulated Depreciation	Net Book Value
Software	5	$ 12,582,805	6,971,393	$ 5,611,412
Computers and peripherals	3 to 5	3,553,620	2,810,613	743,007
Leasehold Improvements	7 or less	4,912,211	3,566,376	1,345,835
Furniture	7	852,754	450,409	402,345
Software-in-Development	n/a	654,558	–	654,558
Total		$ 22,555,948	$ 13,798,791	$ 8,757,157

Depreciation expense was $4,305,752 and $3,990,233 for the periods ending September 30, 2007 and September 30, 2006, respectively.

Note 6 – Liabilities Not Covered By Budgetary Resources

Liabilities Not Covered by Budgetary Resources result from the receipt of goods and services, or the occurrence of events, for which appropriations, revenues, or other financing sources necessary to pay the liabilities have not yet been made available through Congressional appropriation. Liabilities Not Covered by Budgetary Resources consisted of the following as of September 30, 2007 and 2006:

Liabilities Not Covered by Budgetary Resources	**2007**	**2006**
Intragovernmental	$ 807,032	$ 976,525
Custodial		
With the Public:		
Unfunded Annual Leave	1,964,478	1,931,980
FECA Liability	663	17,631
Total Liabilities Not Covered by Budgetary Resources	2,772,173	2,926,136
Total Liabilities Covered by Budgetary Resources	2,353,340	2,322,804
Total Liabilities	$ 5,125,513	$ 5,248,940

The FEC accrues a liability related to the Federal Employee's Compensation Act (*FECA*) at September 30 each year. This amount is included under "Other" liabilities.

Note 7 – Commitments and Contingencies

In the opinion of FEC management and legal counsel, FEC is not a party to any legal actions which are likely to result in a material liability. Accordingly, no provision for loss is included in the financial statements.

Note 8 – Leases

FEC has no capital leases. The FEC has a commitment under an operating lease for its headquarters office space. The lease for this space expired September 30, 2007. FEC renewed its lease agreement with GSA for another ten years. Future payments due under the new lease, approved December 2006, with an effective date of October 1, 2007 through September 30, 2018 are:

Future Operating Lease Payments

Fiscal Year	**Lease Payment**
2008	$ 4,787,089
2009	5,705,136
2010	5,755,351
2011	5,818,278
2012	5,883,092
2013 and thereafter	30,457,819
Total Future Lease Payments	$ 58,406,765

Note 9 – Statement of Net Cost

FEC's costs are consolidated into one program, "Administering and enforcing the *FECA*," as noted below:

	FY 2007	FY 2006
Intragovernmental gross costs	$ 6,810,914	$ 7,391,510
Intragovernmental net costs	6,810,914	7,391,510
Gross costs with the public	49,788,784	48,515,046
Less: Earned revenues from the public	(222,137)	–
Net costs with the public	49,566,647	48,515,046
Net Cost of Operations	$ 56,377,561	$ 55,906,556

In accordance with OMB Circular A-136, costs incurred for goods and services provided by other federal entities are reported in the full costs of FEC's program and are identified as "intragovernmental." All other costs are identified as "with the public."

Note 10 – Statement of Budgetary Resources

The Statement of Budgetary Resources (SBR) compares budgetary resources with the status of those resources. As of September 30, 2007, budgetary resources were $57,295,859 and net outlays were $52, 777, 727. As of September 30, 2006, budgetary resources were $56,527,231 and net outlays were $52,480,532.

Apportionment Categories of Obligations Incurred

FEC receives apportionments of its resources from OMB. Category A apportionments are those for resources that can be obligated without restriction on the purpose of the obligation, other than to be in compliance with legislation underlying programs for which the resources were made available. Prior to FY 2006 Category B apportionments were to be used for Information Technology enhancements only. Beginning in FY 2006 the B fund designation was eliminated.

In FY 2007 and FY 2006, direct obligations incurred amounted to $54,255,141 and $54,448,901, respectively; and reimbursable obligations incurred amounted to $211,860 and $0, respectively.

Comparison to the Budget of the United States Government

SFFAS No. 7, Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting, requires an explanation of material differences between budgetary resources available, the status of those resources and outlays as presented in the Statement of Budgetary Resources to the related actual balances published in the Budget of the United States Government (Budget). The Budget that will include FY 2007 actual budgetary execution information is scheduled for publication in February 2008, which will be available through OMB's website at http://www.whitehouse.gov/omb. Accordingly, information required for such disclosure is not available at the time of publication of these financial statements.

Balances reported in the FY 2006 SBR and the related President's Budget reflected the following:

FY 2006	Budgetary Resources	Obligations Incurred	Distributed Offsetting Receipts	Net Outlays
Statement of Budgetary Resources	$ 53,765,075	$ 54,448,901	–	$ 52,480,532
Budget of the U.S. Government	54,000,000	54,000,000	–	52,000,000
Difference	$ (234,925)	$ 448,901	$ –	$ 480,532

The differences between the Combined Statement of Budgetary Resources and the Budget of the U.S. Government are due to rounding. The Budget of the U.S. Government reflects amounts in millions while the Statement of Budgetary Resources is in dollars.

In FY 2007 FEC's Total Resources on the Statement of Budgetary Resources differed from the SF-133 by $213,191. This difference is primarily due to the timing of when the SF-133 was submitted and the Statement of Budgetary Resources was finalized, incorporating adjustments for upward and downward spending in the reports. The Total Status of Resources line differs by a corresponding amount.

In FY 2007, the U.S. Treasury reflected $456,054 on the *2007 Treasury Combined Statement, Part 4*. However, these funds are not considered offsetting receipts. These funds represent amounts initially recorded by the FEC in the budget clearing account that were then transferred to the civil penalties account. Accordingly, these amounts are recorded on the Statement of Custodial Activity and not reported on the Statement of Budgetary Resources.

Note 11 – Custodial Revenues and Liability

FEC uses the accrual basis of accounting for the collections of fines, penalties and miscellaneous receipts. Collectibility by FEC of the fines and penalties is based on the responsible parties' willingness and ability to pay:

Custodial Revenue	2007	2006
Fines, Penalties, and Other Miscellaneous Revenue	$ 5,031,538	$ 6,602,398
Custodial Liability		
Receivable for Fines, Penalties and Other Miscellaneous Receipts	1,443,300	1,074,698
Less: Allowance for Doubtful Accounts	636,268	554,227
Total Custodial Liability	$ 807,032	$ 520,471

Note 12 – Undelivered Orders at the End of the Period

Undelivered orders at September 30, 2007 and 2006 totaled $5,077,159 and $5,211,294 respectively.

Note 13 – Reconciliation of Net Cost of Operations to Budget

The presentation of the Statement of Financing (SOF) was revised, effective this fiscal year, to reflect a new format required pursuant to OMB Circular A-136, revised, which provided for the SOF to be displayed in the notes and referred to as "Reconciliation of Net Cost of Operations to Budget" rather than the SOF. The objective of this information is to provide an explanation of the differences between budgetary and financial (proprietary) accounting. This is accomplished by means of a reconciliation of budgetary obligations and non-budgetary resources available to the reporting entity with its net cost of operations.

	2007	2006
Resources Used to Finance Activities:		
Budgetary Resources Obligated		
Obligations incurred	$ 54,467,001	$54,448,901
Less: Recoveries of prior year obligations	(1,352,281)	(967,661)
Obligations net of recoveries of prior year obligations	53,114,720	53,481,240
Less: Offsetting collections	(222,137)	–
Net Obligations	52,892,583	53,481,240
Other Resources		
Transfer in/out without reimbursement	(10,277)	–
Imputed financing from costs absorbed by others	2,331,800	2,352,819
Total resources used to finance activities	$ 55,214,106	$ 55,834,059
Resources Used to Finance Items not Part of the Net Cost of Operations		
Change in budgetary resources obligated for good, services, and benefits order but not yet provided	(127,207)	1,184,233
Resources that fund expenses recognized in prior periods cost of operations	16,968	50,406
Resources that finance the acquisition of assets	$ 3,295,311	$ 2,160,662
Total resources used to finance items not part of the Net Cost of Operations	3,185,072	3,395,301
Total resources used to finance the net cost of operations	$ 52,029,034	$ 52,438,758
Components of the Net Cost of Operations that will not require or Generate Resources in the Current Period		
Components Requiring or Generating Resources in Future Periods		
Increase in annual leave	32,498	–
Increase in exchange revenue receivable from the public	10,277	–
Total Components of the Net Cost of Operations that will require or Generate Resources in Future Periods	42,775	–
Components not Requiring or Generating Resources		
Depreciation and amortization	4,305,752	3,990,233
Revaluation of assets or liabilities	–	(522,435)
Total Components of the Net Cost of Operations that will not require or Generate Resources in the Current Period	4,348,527	3,467,798
Net Cost of Operations	$ 56,377,561	$ 55,906,556

SECTION IV
Other Accompanying Information

From the Inspector General

FEDERAL ELECTION COMMISSION
Washington, DC 20463

Office of Inspector General

MEMORANDUM

TO: The Commission

FROM: Inspector General

SUBJECT: Inspector General Statement on the Federal Election Commission's Management and Performance Challenges

DATE: October 15, 2007

Each year, the Inspector General is required to provide a summary and assessment of the most serious management and performance challenges facing the Federal Election Commission. The requirement is contained in the Reports Consolidation Act of 2000 (Public Law 106-531), an amendment to the Chief Financial Officers (CFO) Act of 1990. The attached document responds to the requirement, and provides the annual statement on Commission challenges to be included in the *Federal Election Commission Performance and Accountability Report (PAR) Fiscal Year (FY) 2007*.

The Inspector General has identified three areas for inclusion in the FEC's FY 2007 PAR:

Human Capital Management
Information Technology Security
Financial Reporting

The Inspector General identified these same three challenges in the 2005 and 2006 PARs and continues to believe the issues remain challenges for the FEC. This year, human capital management is again highlighted, due in part to the significant staff turnover in the Office of Human Resources. Overall, the FEC has devoted significant efforts to address the challenges and progress is being made on these important areas.

The Inspector General's assessment is based on information derived from a combination of several sources; including Office of Inspector General audit and inspection work, Commission reports, and a general knowledge of the Commission's programs and activities.

The Reports Consolidation Act of 2000 permits agency comment on the Inspector General's statements. Agency comments, if applicable, are to be included in the final version of the PAR that is due on November 15, 2007.

Lynne A. McFarland
Inspector General

Attachment

Cc: Patrina M. Clark, Staff Director
Erin D. Singshinsuk, Chief Financial Officer
Alec Palmer, Chief Information Officer
John W. Sigmon, Deputy Staff Director
Management & Administration
James J. Wilson, Director Office of Human Resources

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Inspector General's Assessment of FY 2007
Management and Performance Challenges
Facing the Federal Election Commission

HUMAN CAPITAL MANAGEMENT

According to the Government Accountability Office (GAO), it first added strategic human capital management as a governmentwide high-risk area in 2001 because federal agencies lacked a strategic approach to human capital management that integrates human capital efforts with agency mission and program goals. GAO asserts the area remains high-risk "because the federal government now faces one of the most significant transformations to the civil service in half a century, as momentum grows toward making governmentwide changes to agency pay, classification, and performance management systems."

While GAO recognizes that progress has been made in addressing federal human capital challenges, it notes "significant opportunities remain to respond to current and emerging 21st century challenges." Further, GAO advises that "before implementing any future human capital reforms, agencies should demonstrate they have met certain conditions; including that they have developed an institutional infrastructure that can support reform. This infrastructure should include, among other things, (1) a modern, credible performance management system that provides clear linkage between institutional, unit, and individual performance oriented outcomes; and (2) adequate safeguards to ensure fair, effective, credible and nondiscriminatory implementation of the system." The FEC has performed the first step in the process by developing a new organization-wide strategic plan covering 2007 - 2012. Although currently in draft, the new plan is due to be updated and finalized in late 2007 and expected to cover the period 2008 - 2013.

The second key step, a "modern, credible performance management system," is also underway. The FEC recently transitioned to a new performance management system which includes quarterly reviews of progress towards stated objectives and objective setting done in consultation with staff. While the new system remains paper-based, there is the potential to move to a more automated system in the future. Notwithstanding the change, a recent human capital survey participant noted, "While people may want to fix the performance appraisal system, what really needs to change is the culture." Management and staff throughout the FEC must be willing to participate fully and openly in creating and assessing timely, achievable, measurable performance objectives. Without the necessary monitoring that appraisals are created and assessed in a frequent and timely manner, there is the potential the benefits will not be realized.

The FEC Office of Human Resources (OHR) has undergone significant change recently, experiencing an 86 percent staff turnover in the last 18 months, with a 57 percent change in the last four months alone. In order to address the identified challenges, the FEC sought to assemble a highly skilled and multi-faceted human resources team. The FEC hired a new HR Director with the opportunity to recruit the best staff. Recognizing the old HR system did not contain written plans for recruitment, retention or training, the new HR team has begun creating a strategic plan to address the universal risk of an aging workforce as well as ongoing business needs of retention, recruitment and training.

Forming the core of the revamped HR strategy is the HR staff themselves. The FEC OHR will move from an HR specialist to an HR generalist model. While newly recruited staff was selected for their experience and specialist skills, each will be tested using the Office of Personnel Management Federal Competency Assessment Tool for Human Resources (FCAT-HR). Based on the results, the HR staff will each create training plans aimed at securing, at a minimum, basic competency in all generalist skills as well as setting goals for achieving advanced and expert skill sets in more technical areas. This new model involves cross-training and enabling HR staff to transition from performing specialist activities to become generalists by acquiring knowledge and expertise in a broad range of human capital areas, with emphasis on strong interpersonal and communication skills. According to the HR Director, OHR will implement an organizational model similar to that of a professional services firm. Further, in this model, OHR is strategic, transparent and customer-focused.

Further enabling the new HR generalist model is a move to an HR line of business (LOB). The FEC plans to outsource some administrative HR activities and automate others using the U.S. General Services Administration (GSA) Comprehensive Human Resources Integrated System (CHRIS). The planned LOB conversion includes: an automated workflow process for personnel actions; automated time and attendance; reminders of when performance evaluations are due with an eventual move to an on-line performance evaluation system; training history; and conversion to a new travel system. Much like the Office of Personnel Management's *Employee Express*, the CHRIS system will allow FEC employees to review changes in employment information and manage their personnel activities on-line. Timing for implementation has not yet been agreed and it is likely that a phased approach will be used. According to the FEC, the over-all effect will be to minimize the day-to-day administrative processing of HR activities and address the evolving needs and growing demands for consultative, advisory and analytical services. The LOB efforts are in the early stages of planning and implementation, therefore the OIG has not received a detailed business plan for the LOB efforts such as a cost-benefit analysis or other detailed plan.

Prior to recruitment and placement of the current HR team, the previous two years has been a period of relative instability within the FEC OHR area. As such, programs that sought to address the HR challenges of employee and leadership development and work-life balance have not progressed as planned. For example, the mentoring and development program that included detailing employees to other federal agencies is neither well known nor widely exercised. The IG notes only one instance of use in the last several years and is not aware of a system to notify FEC employees of access to or benefits of the program. The planned FEC Employee Handbook is still in the conceptual stage and the senior management development program identified and budgeted in 2005 has not progressed to date. According to the FEC, due to budget shortages, the use of interns was eliminated entirely in the Audit division for the last two years but is expected

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to resume in 2008 with a plan to hire clerks to perform matching funds review, if required, relating to Presidential audits. The 2005 legislative recommendation to move FEC senior management to senior executive service (SES) status was not approved and further approval requests are on hold with no plan for a similar request in 2008. The SES approval was sought to allow the FEC to financially compete for management talent both within government and the private sector. The flexiplace (telecommute) pilot program has been extended a number of times and is currently under negotiation between management and the National Treasury Employees Union. The revised program, covering bargaining unit employees, is expected to be finalized in late 2007 or early 2008.

The IG notes the positive and continuing effort to address HR challenges through improved communication within the Commission. Two staff-level town hall meetings held in April and September 2007 have elicited a great deal of employee feedback to management and serve as both a sounding board and a means for collective communication from management to staff. The use of separate monthly management meetings should continue with greater emphasis on consistent timing and communicating whether the objectives of the various management initiatives are being met. The OHR should review past programs that may have been in various stages of implementation and determine whether the programs should be further developed or terminated. The increased planning through rigorous development of strategic and business plans at the unit level, as well as individual performance plans, should be monitored to ensure the plans are complete, consistent, and fully aligned to the FEC objectives.

INFORMATION TECHNOLOGY SECURITY

Information technology (IT) security, while improving each year at the FEC, continues to be a challenge for the agency. The challenge the FEC faces in IT security is shared by other departments and agencies in the Federal government. Over the last several years, identity theft and the need to protect personal information has received heightened national attention. Recent incidents of data theft and loss at federal agencies expose Americans to increased risk of identity theft and raise concern about how well the Federal government is securing its computer systems; protecting sensitive information from unauthorized use, disclosure, and modifications; and notifying the public when data breaches occur. The Government Accountability Office (GAO) has continued to list IT security on their list of high-risk areas since 1997.

Some of the weaknesses GAO has cited at other Federal departments and agencies are also continuing weaknesses at the FEC. Risk assessments are to be conducted every three years as part of an overall strategy to mitigate risks associated with its IT environment. The FEC has not conducted these necessary risk assessments. In addition, the FEC’s disaster recovery plan needs improvement to include a comprehensive contingency plan of its data centers, networks and telecommunication facilities. The disaster recovery plan should also include a prioritization and timeframe for recovering resources in the event of a disaster.

The FEC has awarded contracts to address these issues. In the upcoming fiscal year, an entity-wide security program plan is to be developed and implemented, risk assessments, as part of the FEC's overall strategy to mitigate risks associated with its information technology environment are to be performed, and the results of the assessments are to be incorporated into the FEC's security plans. A Business Impact Analysis is also to be performed to formally identify and prioritize all critical data and operations of the FEC's networks and the resources needed to recover them if there is a major interruption or disaster. The Inspector General is pleased to observe the steps the FEC is taking to correct the existing weaknesses. These are important steps to enhance IT security and should resolve many of the related outstanding issues.

In the past year, continued commitment of the Information Technology Division staff has resulted in success in addressing some of the security challenges. The FEC has continued to improve the physical security controls over the data center by adding the Datacenter access list to the agency's Security Review Policy. A comprehensive set of policies and procedures for managing system software changes has also been fully implemented by the Commission. Account lockout thresholds have been revised on some systems and ITD has developed a corrective action plan that specifically addresses IT security.

While the commitment of the FEC staff to improve IT security is vital, the IG continues to believe the adherence to government-wide IT security standards is an important part of an effective security program. GAO has cited the enactment of the Federal Information Security Management Act of 2002 (FISMA) as important legislation requiring the development, documentation, and implementation of an agency-wide information security program. The FEC is one of a handful of Federal agencies that are exempt from FISMA. While the IG and management have come to an informal understanding that the FEC should be expected to adhere to IT security "best practices", which in the Federal government would include adherence to IT security standards published by the National Institute of Standards and Technology (NIST), the IG feels that the FEC should formally adopt adherence in principle to FISA and the NIST standards. The IG understands that part of the hurdle to this is the necessary resources and time.

FINANCIAL REPORTING

Since fiscal year 2004, the FEC has been required to prepare and submit annual audited financial statements as a result of the Accountability of Tax Dollars (ATD) Act of 2002. The submission of audited financial statements to Congress and the Office of Management and Budget is an important component to effective financial management. The requirement to prepare and submit audited financial statements has been a continuing challenge for the FEC.

A major factor contributing to the FEC challenge of improving financial management has been a lack of continuity in the Chief Financial Officer position. In the past four years, five different individuals have held the CFO positions. The FEC has been fortunate that the Accounting Officer and his immediate staff have been able to provide continuity during the past several fiscal years and in the past, experienced FEC employees were acting CFOs during transition periods. In January 2007, the FEC hired a permanent CFO who has experience in financial management and the production of audited financial statements. The CFO's knowledge should assist the FEC in continuing to establish the appropriate policies and procedures related to the sound financial management of the agency's resources. The duties, responsibilities and reporting structure for the CFO have also been significantly revised during her tenure.

One of the changes that occurred was the reassignment of the management and administrative functions that originally resided in the CFO's office. Those duties have been transferred to a senior level manager who reports directly to the Staff Director. In addition, the procurement function that was located in the Administrative Office was reassigned to the CFO. The most significant revision transpired when a reorganization in reporting structure occurred that now has the CFO reporting directly to the Commission. This shift in reporting has elevated the importance of sound financial management and internal controls. The IG believes the above changes should have a positive impact on the operations of the OCFO and in turn the production of audited financial statements.

The FEC also updated its strategic plan in FY 2007. The FEC has developed a draft strategic plan that management feels more clearly defines the agency's objectives and consolidates its strategic goals into one concise goal. The Statement of Net Cost (SNC) was revised to reflect the changes to the strategic plan and several outstanding issues that related to the SNC were resolved by this consolidation.

The FEC has made significant progress in the initiative started the previous year concerning transitioning the FEC to a Financial Management Line of Business (FMLoB). The FEC has chosen GSA to be its provider for financial services. Management is moving forward during fiscal year 2008 and anticipates the conversion of financial data to be completed mid-way thorough the fiscal year. The FMLoB has the potential to provide the FEC with cost saving and efficiencies in its financial management, and the IG hopes the FEC will take full advantage of the opportunity.

APPENDIX A
List of Acronyms

ADR	Alternative Dispute Resolution
AF	Administrative Fine
AICPA	American Institute of Certified Public Accountants
AO	Advisory Opinion
ATD	Accountability of Tax Dollars
BCRA	Bipartisan Campaign Reform Act
CFO	Chief Financial Officer
CFR	Code of Federal Regulations
CHRIS	Comprehensive Human Resources Integrated System
CSRS	Civil Service Retirement System
DOL	Department of Labor
E&J	Explanation and Justification
FASAB	Federal Accounting Standards Advisory Board
FBWT	Fund Balance with Treasury
FCAT-HR	Federal Competency Assessment Tool for Human Resources
FEC	Federal Election Commission
FECA	Federal Election Campaign Act
FECA	Federal Employees Compensation Act
FERS	Federal Employees' Retirement System
FFMIA	Federal Financial Management Improvement Act
FICA	Federal Insurance Contribution Act
FISMA	Federal Information Security Management Act
FMFIA	Federal Managers' Financial Integrity Act
FMLOB	Financial Management Line of Business
FOIA	Freedom of Information Act
FTE	Full-time Equivalent
FY	Fiscal Year
GAAP	Generally Accepted Accounting Principles
GAO	Government Accountability Office
GPRA	Government Performance and Results Act
GSA	General Services Administration
IG	Inspector General
IPIA	Improper Payments Information Act
IRS	Internal Revenue Service
IT	Information Technology
LOB	Line of Business
MD&A	Management's Discussion and Analysis
MUR	Matters under Review
NIST	National Institute of Standards and Technology
NPRM	Notices of Proposed Rulemaking
OAR	Office of Administrative Review
OGC	Office of General Counsel
OHR	Office of Human Resources
OIG	Office of the Inspector General

OMB	Office of Management and Budget
OPM	Office of Personnel Management
P&E	Property and Equipment
PART	Performance Assessment Rating Tool
PAC	Political Action Committee
PAR	Performance and Accountability Report
PEC	Presidential Election Campaign
PMA	President's Management Agenda
RAD	Reports and Analysis Division
RFAI	Request for Additional Information
SAS	Statement on Auditing Standards
SBR	Statement of Budgetary Resources
SFFAS	Statement of Federal Financial Accounting Standards
SNC	Statement of Net Cost
SOF	Statement of Financing
TSP	Thrift Savings Plan
USC	United States Code