FEDERAL ELECTION COMMISSION

Performance and Accountability Report
Fiscal Year 2008

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(cont.)

Message From The Chairman

November 15, 2008

The FEC's Performance and Accountability Report for Fiscal Year 2008 reflects the agency's program performance and financial activities over the past year and demonstrates our continued commitment to administering the *Federal Election Campaign Act (FECA*) of 1971, as amended. As an agency with specific jurisdiction, the FEC provides the American public confidence in the integrity of the Federal election process by disclosing the amounts, sources and uses of contributions, as well as emphasizing effective and fair enforcement of the *FECA*.

During fiscal year 2008, the Commission faced significant challenges. The most significant challenge was that the Commission was without a quorum during a six-month lapse between the expiration of prior recess appointments and Senate confirmation of the President's nominees for Commissioners. As a result of the FEC being without a quorum of Commissioners for nearly half of the year, the Commission was unable to take action on many core business matters that required a four-vote quorum.

The lack of a quorum impacted the Commission beyond the obvious inability to finalize work as statutorily authorized. It also affected the Commission's ability to retain and recruit personnel, thereby impacting the Commission's ability to effectively manage, monitor and communicate with the staff. For example, during these six months, turnover was at an all time high within the Commission, including the resignation of the Chief Financial Officer and Staff Director.

Although I have less than two months remaining in my six months term as the Chairman, I am determined to continue to improve the day-to-day operations and management of the FEC. The number one priority of the Commission is our staff. So, in addition to addressing our statutory workload, we must figure out how to resolve the many staff-related issues. Although it won't be easy, we are on our way in making improvements. For example, the retention of staff has now stabilized enabling staffing to reach close to the Commission's authorized level. Other changes made since regaining a full Commission in July 2008 continue to reap positive results as evidenced by the Commission again receiving an unqualified "clean" opinion on its FY 2008 financial statements. The financial and performance data are reliable, accurate and complete. Receiving a clean opinion provides the public the confidence that the FEC is managing taxpayers dollars in the most fiduciary manner. The FEC's financial and performance data is more fully discussed in Sections II and III.

Despite our successes, we have ongoing challenges to address. For example, our Independent Auditor's Report on Internal Control identified one material weakness relating to financial accounting and reporting and one significant deficiency relating to information technology. Looking ahead, continued oversight by the Commissioners, along with greater emphasis on financial management and internal controls, conveys the high priority of the Commission to eliminate its internal control weaknesses. Strengthening internal controls and enhancing the financial management system will also help the Commission address its management challenges. The successes and challenges of this past fiscal year will serve as a foundation for our future efforts.

Sincerely,

Donald F. McGahn II
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, 2007 through September 30, 2008.

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 2008 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 responsibilities.

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 agency's financial position, audit results and describing the FEC's compliance with key legal and regulatory requirements.

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

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 of 1971*, 2 U.S.C. 431 et seq., as amended by the *Bipartisan Campaign Reform Act of 2002* (*BCRA*), P.L. 107–155 (*FECA* or 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) enforce the provisions of the law such as the limits and prohibitions on contributions, and 3) interpret and administer the law.

The *Act* reflects a belief that democracy works best when voters can make informed decisions in the political process, decisions based in part on knowing the sources of candidates' financial support, focusing on transparency. Public confidence in the political process depends not only on laws and regulations to assure transparency and limits and prohibitions on the amounts and sources of contributions, but also on the knowledge that those who disregard campaign finance regulations will face real consequences for non-compliance, emphasizing effective and fair enforcement to maintain the integrity of campaign financing.

How the FEC is Organized

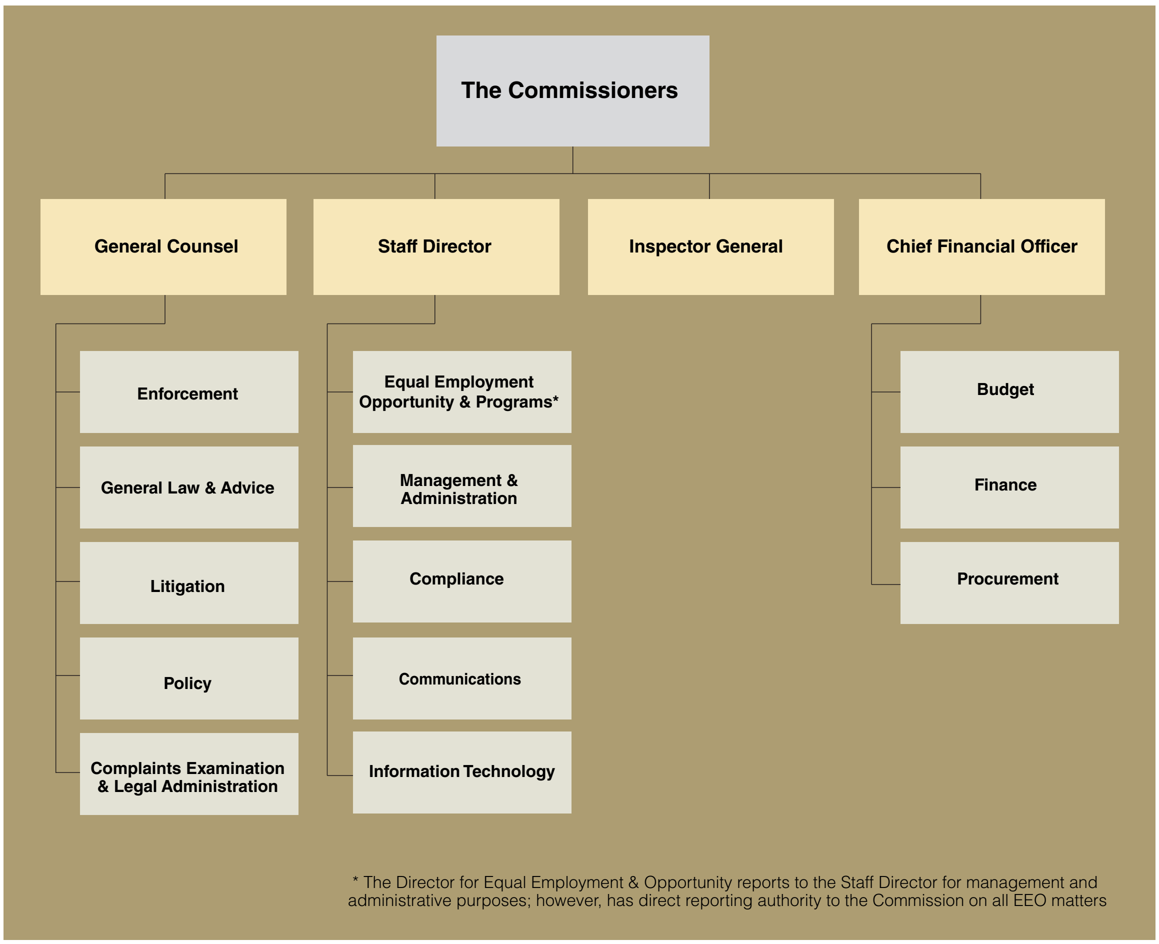
Organization

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 a quorum of at least four votes for the Commission to adopt any official action or policy.

Fiscal year 2008 presented management with a unique challenge in conducting its day-to-day operations. Specifically, the Commission was without a quorum during a six-month lapse between the expiration of prior recess appointments and Senate confirmation of the President's nominees for Commissioners. As a result of the FEC being without a quorum of Commissioners for nearly half of the year, the FEC was unable to take action on many core business matters that required four votes. This prolonged lack of a quorum impacted the agency's ability to achieve several of its performance goals and other key activities.

The FEC is headquartered in Washington, D.C. and does not have any regional offices. The FEC's authorized funding and staffing levels for fiscal year (FY) 2008 were $59.2 million and 375 full-time equivalent (FTE) positions. The FEC is funded by a single annual appropriation for salaries and expenses. The FEC is also authorized to collect fees to offset the costs of its conferences. The following chart represents the organizational structure of the agency as of September 30, 2008.

FEC Organizational Chart



The Offices of the Chief Financial Officer, General Counsel, and Staff Director support the agency in accomplishing its mission. 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 specific roles and responsibilities of each office are described in greater detail at http://www.fec.gov/about.shtml.

As illustrated by 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.

Disclosure, Compliance and Enforcement

Disclosing Campaign Finance Information

Disclosing the sources and amounts of funds used to finance federal elections is one of the most important duties of the FEC. In fact, it would be virtually impossible for the Commission to fulfill effectively any of its other responsibilities without disclosure. The public campaign finance 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.

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 identifies an apparent violation or raises questions about the information disclosed on a report, the Office of Compliance 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.

Encouraging Compliance through Education

Helping the regulated community understand its obligations under the *Act* is an essential component of voluntary compliance. The FEC, through its Office of Communications, places a significant emphasis on encouraging compliance. The Office of Communications consists of the following offices/divisions: 1) Information Division, 2) Public Disclosure Division, 3) Press Office, and 4) the Office of Congressional, Legislative and Intergovernmental Affairs.

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 encourages voluntary compliance through 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.

Enforcing 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 a Commission audit;

- Voluntary self-reporting by representatives of candidates or political committees who believe 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.

Swift resolution of enforcement matters is one of the Commission's highest priorities. The Commission's efforts to promptly resolve enforcement matters were hindered during this fiscal year because the agency lacked a quorum for six months. Without a quorum, the Commission was unable to vote on pending enforcement matters from January through June 2008, thereby impacting the number of OGC's enforcement matters closed by the FEC in fiscal year 2008. Once the Commission regained a quorum, immediate focus was placed on resolving those pending matters.

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 OGC's Enforcement Division:

- 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.

If a conciliation agreement cannot be reached and the Commission votes to initiate civil litigation, it will file and prosecute a civil action in Federal district court to address the alleged violation of the *Act*. Depending on the size and complexity of the lawsuit, such cases may be resolved quickly or may require a significant amount of resources for several years.

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 that permitted by the traditional enforcement process. The AF program was set to expire at the end of calendar year 2008, but was extended by Congress through 2013. This program, which is administered by the Office of Compliance's Office of Administrative Review (OAR) and RAD, assesses 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.

The Commission also enforces the *Act* through audits of candidates and political committees. The Commission conducts mandatory audits, under Title 26, as discussed in the section on Public Funding below. In addition, the Commission performs "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*. The Commission's audit presence not only contributes to its enforcement efforts, but also encourages voluntary compliance within the regulated community.

Interpreting and Developing 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.

To further its outreach and responsiveness to the public and regulated community, the Commission responds to questions from the regulated community about how the *Act* applies to specific situations by issuing advisory opinions (AOs). The Commission recently instituted an expedited process for handling certain time-sensitive requests in even shorter timeframes than the *Act* allows, generally 60 days. It should be noted that for AO requests from candidates in the two months leading up to an election, the response time for the Commission is reduced to 20 days.

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 Chapters 95 and 96 of 26 U.S.C. The program is funded by taxpayers who voluntarily check off the $3 designation for the Presidential Election Campaign on their income tax returns. Through the public funding program, the Federal government provides (1) matching funds to candidates seeking their party's Presidential nomination, (2) grants to 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.

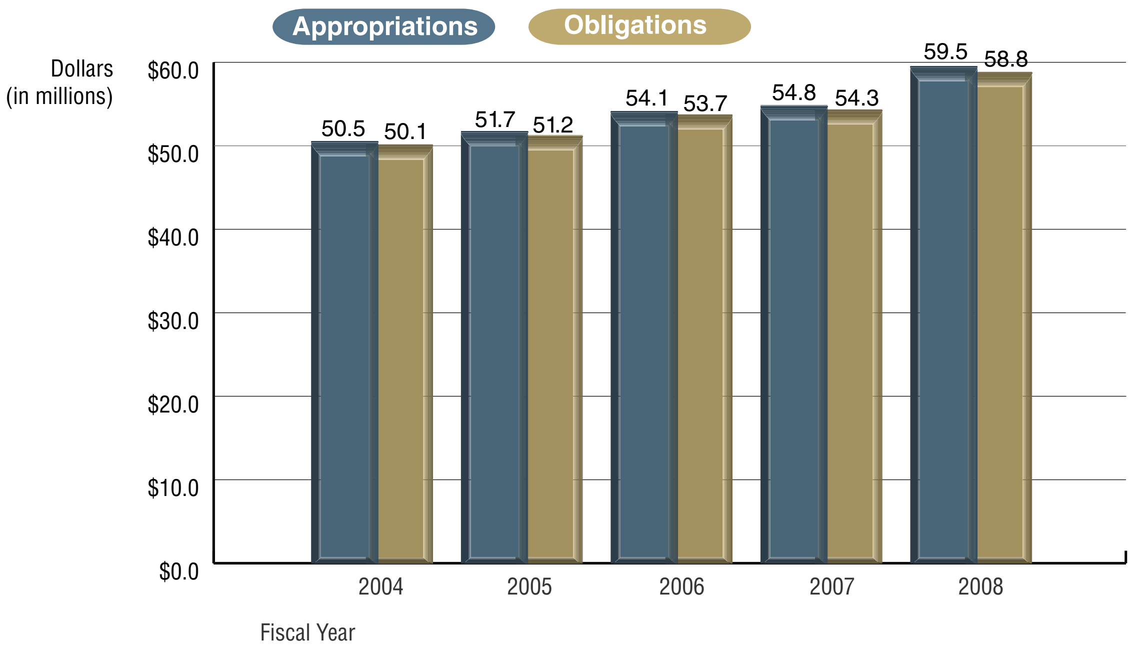
Section 1.B: FEC Performance Goals, Objectives, and Results

Sources of Funds

The FEC receives an annual appropriation for Salaries and Expenses. In addition, the FEC has authority to collect registration fees for the costs of carrying out FEC-hosted conferences. In FY 2008, the FEC's authorized funding level included an appropriation of $59.2 million and estimated registration fees of $300,000.

The FEC's total budget authority level in FY 2008 was $59.5 million. Figure 1 shows the agency's funding and obligations from FY 2004 to 2008.

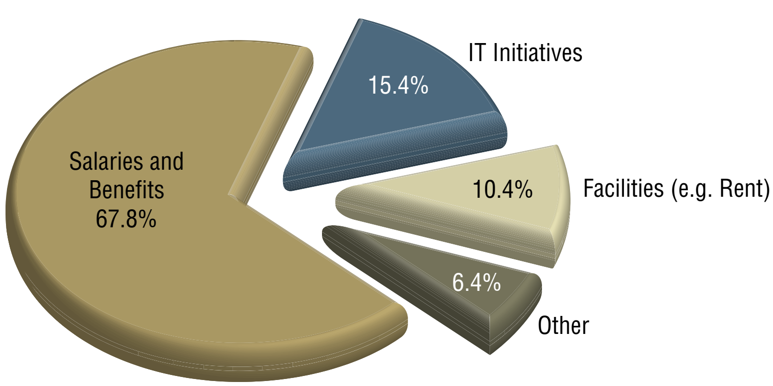
Figure 1 – Summary of Funding



Personnel vs. Non-Personnel Costs

Figure 2 represents the Commission's actual expenditures broken out between personnel and non-personnel costs for FY 2008. Personnel costs comprised 67.8 percent of the FEC's costs; the other 32.2 percent was spent primarily on information technology (IT) software and hardware and rent and related costs, such as building security.

Figure 2 – Fiscal Year 2008 by Major Catagory



Summary of Significant Performance Results

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.

The FEC's strategic plan was updated effective FY 2008. The changes to the strategic plan were primarily to reflect the FEC's current operations and to more clearly set forth the FEC's objectives. The FEC's strategic framework consists of a mission statement supported by a single, overarching strategic goal, which is: **To protect the integrity of the Federal campaign process by providing transparency, enforcing contribution restrictions, and fairly administering the *FECA* and related statutes.**

To help the Commission achieve its goal, the following three objectives were established:

- 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, Administering, and Defending the Act

The revised strategic plan also incorporated means and strategies used in achieving its overarching strategic goal: (1) operational processes; (2) the development and use of technologies; and (3) human resources. These objectives provide the framework for defining the strategic activities needed to effectively measure the Commission's success in achieving its goal. Accordingly, the FEC refined its performance measures in FY 2008 to enhance its ability in capturing the data needed to assess the effectiveness of its operations.

The following table provides a summary of the Commission's FY 2008 target and actual results of its performance measures. As previously mentioned, the lack of a quorum for six months adversely impacted the agency's ability to achieve several of its FY 2008 performance targets.

	Performance Measure	FY 2008 Target	FY 2008 Actual
	Strategic Objective A: Transparency		
1.	Process reports within 30 days of receipt as measured quarterly	95%	91%
2.	Meet the statutory requirement to make reports and statements filed on paper with the FEC available to the public within 48 hours of receipt	100%	100%
	Strategic Objective B: Compliance		
3.	Conduct educational conferences and host roundtable workshops on the campaign finance law each election cycle, achieving a mean satisfaction rating of 4.0 on a 5.0 scale	100%	100%
4.	Issue press releases summarizing completed compliance matters within two weeks of a matter being made public by the Commission	100%	22%
5.	Issue press releases containing summaries of campaign finance data quarterly	100%	100%
6.	Process enforcement cases within an average of 15 months of receipt	100%	66%
7.	Process cases assigned to Alternative Dispute Resolution within 155 days of a case being assigned	75%	64%
8.	Process reason-to-believe recommendations for the Administrative Fine Program within 60 days of the original due date of the subject untimely or unfiled report	75%	79%
9.	Process the challenges in the Administrative Fine Program within 60 days of a challenge being filed	75%	14%
10.	Conclude non-Presidential audits with findings in an average of 10 months, excluding time delays beyond the Commission's control, such as subpoenas and extension requests	100%	95%
11.	Conclude non-Presidential audits with no findings in an average of 90 days from beginning of fieldwork	100%	100%
12.	Conclude Presidential audits in an average of 24 months of the election, excluding time delays beyond the Commission's control, such as subpoenas and extension requests	100%	TBD
	Strategic Objective C: Development of the Law		
13.	Complete rulemakings within specific time frames that reflect the importance of the topics addressed, proximity to upcoming elections, and externally established deadlines	100%	100%
14.	Issue all advisory opinions within 60-day and 20-day statutory deadlines	100%	97%
15.	Issue expedited advisory opinions for time-sensitive highly significant requests within 30 days of receiving a complete request, or a shorter time when warranted	100%	60%
16.	Ensure that court filings meet all deadlines and rules imposed by the Courts	100%	100%
17.	Process public funding payments in the correct amounts and within established time frames	100%	100%

Section II of this report presents the FEC's Performance Report, which provides the annual program performance information submitted in accordance with the *Government Performance Results Act* (*GPRA*) in greater detail.

Highlights of Performance Measures

As previously mentioned, disclosing campaign finance information for Federal elections is a key responsibility of the Commission. The FEC continues to encounter an increase in the number of filings related to Congressional and Presidential elections. Despite the continued growth in the number of filings and information related to the filings, the FEC made 100 percent of these filings available to the public within 48 hours of receipt.

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. The Commission reviewed 63,380 documents out of 66,767 documents filed within FY 2008, well on its way to completing its review of 100 percent of the documents received.

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.

Over the past couple of years, the Commission has placed a significant emphasis on the review process to improve the FEC's ability to process cases more timely with more qualitative results. A key factor in helping the Commission achieve its target 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 previously have been dismissed by OGC under the statute of limitations.

In recent years, the FEC has steered resources to the most significant violations, leading to a steep increase in civil penalties for serious violators. The Commission processed 71 enforcement cases during the fiscal year, of which 47 cases (66%) were closed within 15 months. The average processing time for enforcement cases was 16.9 months.

Section 1.C: Analysis of FEC Financial Statements and Stewardship Information

The FEC's FY 2008 financial statements and notes are presented in the required format for the current year 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 in Section III of this report.

The following table summarizes the significant changes in the FEC's financial position during FY 2008.

Net Financial Condition	FY 2008	FY 2007	Increase/ (Decrease)	% Change
Assets	$18,849,424	$18,819,667	$29,757	0.2%
Liabilities	$7,218,576	$5,125,513	$2,093,063	40.8%
Net Position	$11,630,848	$13,694,154	($2,063,306)	(15.1%)
Net Cost	$62,024,007	$56,377,561	$5,646,446	10.0%
Budgetary Resources	$61,452,650	$57,295,859	$4,156,791	7.3%
Custodial Revenue	$2,305,665	$5,031,538	($2,725,873)	(54.2%)

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, nearly 100 percent of the FEC's assets consist of Fund Balance with Treasury (FBWT), Property, Plant and Equipment (PP&E), and Accounts Receivable. 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 approximately $353 thousand, or 3.4 percent from the prior year.

Accounts Receivable represent amounts due from the public for fines and penalties assessed by the FEC and referred to Treasury for collection. The accounts receivable balance decreased by approximately $287 thousand, or 35.1 percent, from FY 2007.

Statement of Net Cost

The Statement of Net Cost presents the annual cost of operating FEC programs. Gross costs less any offsetting revenue is used to arrive at the total net cost of operations. The FEC's total appropriations in FY 2008 was $59.2 million, which is approximately $4.7 million greater than FY 2007. Roughly $39.8 million, or 67.8 percent, of the budget was dedicated to personnel costs. The remaining costs related to rent, information technology initiatives, and general operating expenses. Overall, net costs increased by $5.6 million or 10.0 percent from FY 2007. The majority of the increase is attributable to: 1) a $1.7 million increase in personnel for the cost of living adjustment (COLA), 2) increase of $1.5 million in rent, and 3) approximately $1.0 million increase in IT initiatives to address the prior year audit findings. Other costs of operations, such as training, printing, and supplies, account for the remaining amount.

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. Total Net Position decreased by about $2.1 million, or 15.1 percent, primarily due to an increase in Appropriations Used, which is largely a function of payments made.

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 $4.2 million, or 7.3 percent, over FY 2007. This increase primarily is derived from an increase in appropriations received.

Statement of Custodial Activity

The Statement of Custodial Activity represents an accounting of funds collected by the FEC that are owed to the U.S. Treasury's general fund. These monies are not available for the FEC's use. Total custodial revenue decreased from the prior year in the area of fines and penalties by approximately $2.7 million, or 54.2 percent. The decrease is primarily due to the Commission's inability to vote or take action on its enforcement matters and to assess fines and penalties because of the lack of a quorum for nearly half of the fiscal year.

Section 1.D: Analysis of FEC's Systems, Controls, and Legal Compliance

1.D.i – Management Assurances

The *Federal Managers' Financial Integrity Act of 1982* (*FMFIA*) 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 its 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 2008 provide qualified assurance that FEC systems and management controls comply with the requirements of the *FMFIA*. For FY 2008, the FEC reports one material weakness under Section 2 of the *FMFIA*.

The Commission faced significant challenges pertaining to its Human Capital. For example, the Commission was without a quorum of four Commissioners from January 2008 through June 2008. As a result of the FEC being without a quorum of Commissioners for nearly half of the year, the FEC was unable to vote or take action on many core business matters that require a four-vote quorum. This prevented the agency in fulfilling its mission such as closing enforcement matters, certifying Presidential funding payments, and issuing final advisory opinions, rulemakings, or audit reports.

The lack of a quorum directly impacted retention of leadership and key management positions, causing retention of employees to remain a factor for the Commission and its ability to operate effectively and efficiently. As also noted by the Inspector General, the previous three years has been a period of relative instability within key management positions. Programs to address the HR challenges and leadership development have not progressed as planned. For example, the 2005 legislative recommendation to move FEC senior management to senior executive service (SES) status was not approved and further approval requests were on hold through this fiscal year. The SES approval was sought to allow the FEC to financially compete for management talent both within government and the private sector.

Another factor increasing the HR risk factor is the FEC does not have a succession plan in place for key positions. The impact of these Human Capital challenges facing the Commission has been reflected in its inability to recruit or retain qualified individuals.

The Commission continues to make efforts to address its ability to recruit and retain individuals. Furthermore, the Commission continues to emphasize the need for a succession plan. The Office of Human Resources has developed a draft HR strategic plan, including a timeline in addressing the weaknesses identified by management and the Office of the Inspector General.

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, 2008 in accordance with the *FMFIA* and OMB Circular No. A-127, *Financial Management Systems*, as applicable. The results of management reviews provide qualified assurance under Section 4 of the *FMFIA* that the FEC's financial systems controls generally conform to the principles and standards required.

The Commission also considers its financial management system to be a non-conformance with Section 4 of *FMFIA*, as it is not fully integrated as defined by OMB Circular A-127. The financial statements auditors also identified the lack of an integrated financial management system as a material weakness in the prior year's audit report. As a result of the lack of an integrated financial management system, the FEC staff expends a significant amount of resources preparing the necessary management reports, and reconciling data from the disparate system, thus increasing the risk of error.

The Commission has taken steps to address this weakness. First, in February 2008, the FEC converted its accounting system from in-house to an OMB-certified Line of Business (LOB) provider to process its accounting transactions. Second, the FEC upgraded its procurement system to a web-based system, eliminating the need for procurement requests via paper. Third, the FEC has begun to convert its time and attendance reporting from a paper process to a web-based system. The Commission recognizes that additional integration efforts are needed for this weakness to be fully eliminated.

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. Until this fiscal year, no material weaknesses were identified under the *FMFIA* by the FEC.

The following table summarizes the results of this year's *FMFIA* assessment:

Effectiveness of Internal Control over Operations (FMFIA § 2)						
Statement of Assurance	Qualified					
Material Weakness	Beginning Balance	New	Resolved	Consolidated	Reassessed	Ending Balance
Human Capital	0	1				1
Total Material Weaknesses	0	1				1

Conformance with financial management systems requirements (FMFIA § 4)						
Statement of Assurance	Systems do not fully conform to financial management system requirements					
Non-Conformance	Beginning Balance	New	Resolved	Consolidated	Reassessed	Ending Balance
Integrated Financial Management System	0	1				1
Total Non-Conformances	0	1				1

In addition to the two matters identified above, additional areas for improvement were noted during the internal control review. 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, qualified assurance is provided that management controls are in place and the Commission's financial management systems conform to government standards articulated in OMB Circulars A-123 and A-136, as revised.

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 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 fiscal year 2008 evaluation, the Commission identified one material weakness in its internal control over the effectiveness and efficiency of operations and compliance with applicable laws and regulations and one instance of non-conformance of financial systems requirements, as of September 30, 2008.

The Commission faced challenges pertaining to its Human Capital throughout fiscal year 2008. The most significant challenge pertained to the fact that the Commission was without a quorum of four Commissioners beginning January 1, 2008, for six months of the calendar year. The lack of a quorum prevented the agency from fulfilling its mission such as addressing enforcement matters, performing audits, and issuing advisory opinions or rulemakings. Furthermore, retention of leadership and key management positions has remained a factor in the Commission's ability to operate effectively and efficiently, as previously noted by the Inspector General.

The impact from this challenge is reflected in the results of the Commission's performance measures, which highlight many areas where the Commission did not achieve its target. Although the Commission continued to perform its statutorily authorized work, particular matters requiring the approval of a minimum of four

Commissioners could not go forward for approximately six months, until the agency regained a quorum. The Commission will address this weakness by conducting an overall organizational assessment.

The Commission also considers the lack of an integrated financial management system to be a non-conformance with Section 4 of *FMFIA*. Without an integrated financial management system, the Commission cannot easily produce accurate and timely management reports. The independent auditors have identified financial accounting and reporting controls as a material weakness. To address this weakness, the Commission will hire new staff and provide additional training. The Commission also recognizes that additional system integration efforts are needed for this weakness to be fully eliminated.

Except for these two matters discussed above, which are discussed in greater detail throughout this report, the Commission is able to provide a qualified statement of assurance that the internal control and financial management systems meet the objectives of the *FMFIA*.

Donald F. McGahn II
Chairman
October 24, 2008

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
Financial Accounting and Reporting Controls (Modified Repeat Finding)	1	0	0	0	1
Total Material Weaknesses	1	0	0	0	1

In addition to the one material weakness, Clifton Gunderson also observed one significant deficiency, as defined by the American Institute of Certified Public Accountants (AICPA), Statement on Auditing Standards (SAS) 112: Communicating Internal Control Related Matters Identified in an Audit. The FEC has developed 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 2008 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 payments made in its operations.

The FEC reviewed all of its programs and activities to identify those susceptible to significant erroneous payments. Approximately 68 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 also reviewed all of its FY 2008 procurements for non-personnel costs to verify their accuracy and completeness. Accordingly, the FEC is unaware of any improper payments. The FEC continues to monitor its payment process to ensure that the risk of improper payments remains low.

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

The Inspector General's report in Section IV identified four areas specific to management and performance challenges, which include: 1) Governance, 2) Human Capital Management, 3) Information Technology Security, and 4) Financial Reporting. The matter pertaining to Governance is new this fiscal year, while the other three areas had been identified in prior years.

Governance

The Commission agrees with the Inspector General that the agency has encountered challenges in retaining several key senior leadership and other vital management positions. The Commission has begun to take steps to address this concern. It has updated the agency-wide Strategic Plan, as well as implemented a new annual performance planning system. The Commission's next step in its efforts to complete the overarching framework, is to conduct an agency-wide organizational assessment to address the concerns raised by the Inspector General.

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 observed 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.

Information Technology Security

As the Inspector General points out, computerized systems enable the FEC to carry out its mandate to ensure that the campaign finance 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.

At the start of the fiscal year, the FEC placed significant emphasis on its procurement efforts. This included upgrading its procurement system to a web-based version, updating its procurement policies and procedures, and providing targeted training to FEC staff. These efforts have enhanced the FEC's ability to process procurement actions more timely. For example, in the past, a request was submitted via paper. Under the new system, all requests are submitted electronically, which not only eliminates the risk of losing the paper request, but it also provides a tracking for each stage of the procurement action. The risk of possible delays, duplication, or not recording an obligation in the accounting system has significantly decreased as a result of the FEC's efforts in procurement.

Beginning February 1, 2008, the FEC transferred its accounting services to the General Services Administration (GSA), an OMB-certified line of business service provider for financial management. To demonstrate that GSA has adequate controls and safeguards in place, GSA undergoes an annual audit of its control objectives and control activities, including those controls over information technology and related processes. The audit is performed in accordance with the Statement on Auditing Standards (SAS) No. 70, Service Organizations, which is an auditing standard developed by the American Institute of Certified Public Accountants (AICPA) indicating that a service organization has been through an in-depth audit, by an independent auditing firm.

The most recent examination of GSA's controls included procedures to obtain reasonable assurance about whether (1) the accompanying description presents fairly, in all material respects, the aspects of GSA's and Pegasys' controls that may be relevant to a user organization's internal control as it relates to an audit of financial statements; (2) the controls included in the description were suitably designed to achieve the control objectives specified in the description, if those controls were complied with satisfactorily and user organizations applied the controls contemplated in the design of GSA's controls; and (3) such controls had been placed in operation as of June 30,

2008. The results of the SAS 70 audit of GSA's operations stated that the "aforementioned controls presents fairly in all material respects, the relevant aspects of GSA's and Pegasys' controls that had been placed in operation as of June 30, 2008."

The FEC continues to make improvements in its financial management but some challenges remain. Management continues to work with the Inspector General to improve internal control and eliminate the weaknesses identified as part of the annual audit.

1.D.iii – FEC Integrated Internal Control Framework and Legal Compliance

The Commission is subject to numerous legislative and regulatory requirements that promote and support effective internal control. Such 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 1.E: Possible Future Effects of Existing Events and Conditions

There are several existing events and conditions that may affect the FEC in the future. The new Administration coming into office in January 2009 could propose changes to the FECA. Any amendments to the *FECA* might significantly impact the Commission, and could require changes in internal processes or procedures and require that implementing regulations be adopted.

The solvency of the *Presidential Election Campaign Fund* ("*Fund*") could impact the FEC. This past fiscal year, for the first time in the history of the Fund, which dates to the 1976 elections, the shortfall was so great that the primary candidates did not receive any public funds on the first date that they would ordinarily have been paid. After the Department of Treasury set aside the amount for the general election and convention financing, it could not pay primary election candidates when the matching payment period began at the start of the calendar year. Had the Treasury deposited money in the primary matching account based on anticipated receipts, rather than actual receipts, there would have been funds sufficient to pay timely primary candidates who participated in the program while still reserving all necessary funds for the national party conventions and the general election grants. The Department of the Treasury has not interpreted the *Fund Act* and the *Presidential Primary Matching Payment Account Act* as permitting it to proceed in this fashion, and legislation may be necessary to effect such a change.

Only one of the two major party nominees for the presidency opted to take general election public funding in 2008. As a result, the Fund will begin the 2009-2012 presidential election cycle with more funds than previously anticipated. However, long-term stability of the availability of funds and viability of the program remain a concern of the FEC.

Section 1.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 has built 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 is 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 also presents 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. The FEC's 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.

Enhancements to the Presidential Map

The FEC has released a major enhancement to the Presidential Map improving functionality and performance. The presidential map now includes detailed information on each candidate's campaign expenditures. The upgraded presidential map is an easy-to-use online tool for obtaining detailed information about the Presidential campaigns and how they spend their money, including the payee name, purpose, date and amount of each campaign expenditure. Improvements include easier search capabilities, quick access to summary and expenditure information, one-click downloading, better graphics, and a new and very useful "compare" feature.

The Federal election campaign finance map applications have received wide press coverage. Due to the popularity of both Federal election campaign finance map applications, web hits on fec.gov web site increased almost tenfold. About 20 percent of total web hits on fec.gov are generated from the Presidential and House and Senate Map. This is an obvious testament to the Federal election campaign finance map applications, popularity, and the sound architecture of the Federal election campaign finance map applications reliably to handle the large number of web hits.

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 Commission partially launched its Intranet this past year. Once all portals are completed, the Intranet will feature a rich suite of products and deliver productivity and efficiency gains throughout the agency. 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;
- RSS newsfeeds;
- Employee quick polls; and
- Non-technical staff's ability to publish and contribute content to the Intranet site.

Electronic Vote Database

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 were completed in FY 2008 in the Office of the Commission Secretary: (1) 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.

Email Automation and Notification Tool

The Federal Election Commission launched a new system on its website (www.fec.gov) offering automated email updates for a variety of campaign finance information. The new service allows users to sign-up to receive notification whenever information important to them is added or changed on the Commission's site.

System Certification and Accreditation Program

The FEC formally began working on implementing its Certification and Accreditation program. The first phase of the program consisted of conducting a third party risk assessment of its mission critical information systems. This unbiased third party review identified the risks posed against its core applications, determined the potential impact of risk exploitation, and identified current and planned security controls. This phase also evaluated the impact of implementing new security controls to mitigate any newly discovered risks. This phase of the project provides senior management with the necessary knowledge to address risks to its mission critical information systems in an effective and cost efficient manner.

Section 1.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

Performance Purposes, Objectives, and Results

This section of the report 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 2008

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 A: TRANSPARENCY – Receiving Accurate and Complete Campaign Finance Disclosure Reports and Making Them Available to the Public

OBJECTIVE B: COMPLIANCE – Education and Enforcement

OBJECTIVE C: DEVELOPMENT OF THE LAW – Interpreting, Administering, and Defending 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.

The Commission recently reviewed the performance measures and refined them, thereby enhancing the FEC's ability to capture and report data in a more meaningful manner. For example, where a performance measure was broad in nature, the FEC made it more specific. Furthermore, many performance measures were combined as it was determined that the data being reported was duplicative. The following provides a detailed discussion on the FEC's performance measures, as outlined in its updated Strategic Plan.

Results by Objective

Objective A: 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.

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.

Performance Measures

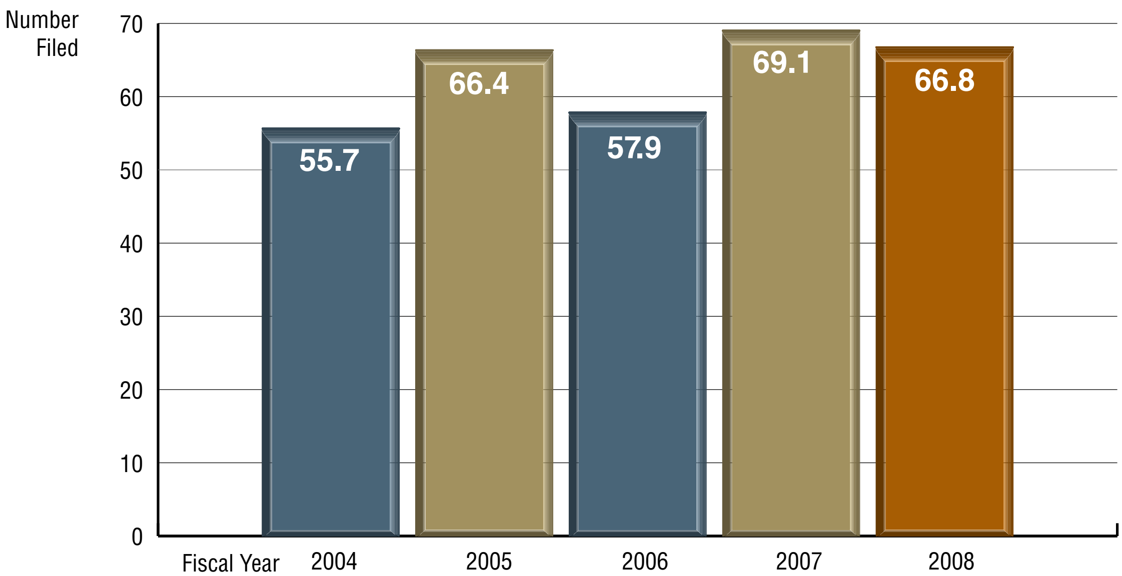
- Process reports within 30 days of receipt as measured quarterly; and
- Meet the statutory requirement to make reports and statements filed on paper with the FEC available to the public within 48 hours of receipt.

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, to 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 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 Disclosure Division ensures that a copy is available for public inspection within 48 hours or receipt, both electronically on the website and at the FEC's headquarters, located at 999 E Street, N.W., Washington, D.C.

Figure 3 shows the total number of campaign finance reports and statements filed with the FEC each fiscal year since 2004. As illustrated, election years (the odd fiscal years), show a spike in the number of filings received by the FEC. The public can access the campaign finance reports and data at http://www.fec.gov/disclosure.shtml.

Figure 3 – Reports and Statements Filed (in thousands)

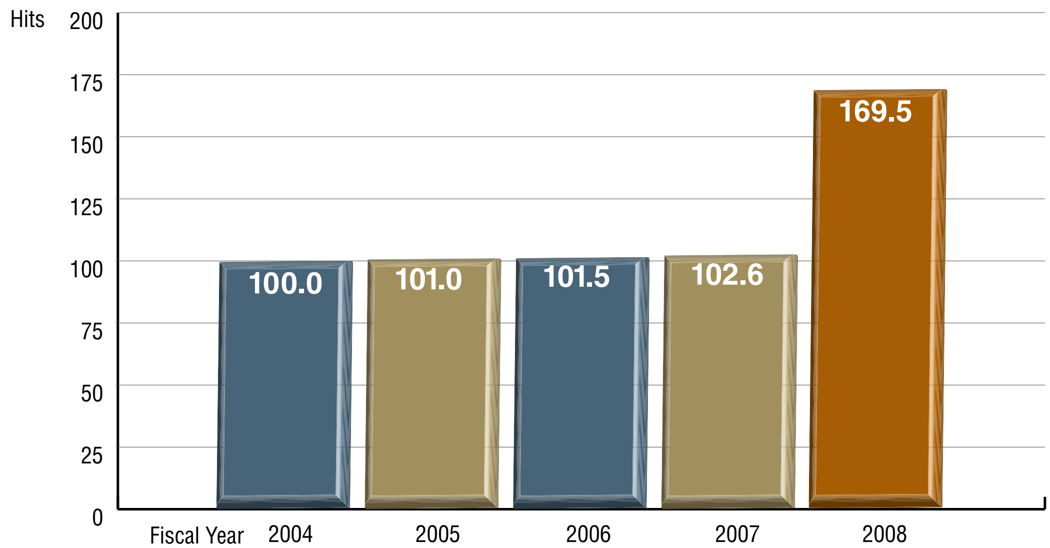


The FEC achieved a success rate of 100 percent in making the financial disclosure reports and statements available to the public within 48 hours of receipt. This fiscal year has been phenomenal in the number of contributors, which has led to a significant increase in the volume of data associated with filings. For example, to-date, the data equivalent to the number of pages for filings received has been approximately 6.0 billion pages, while in fiscal year 2007, the number of pages received was approximately 4.0 billion. This represents a 50 percent increase from last year. Although the FEC has not increased its staffing from last year, it still has been able to successfully achieve its mandate.

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 complete disclosure of campaign finance information. The agency's goal is to code and enter 95 percent of the reports within 30 days of receipt. For FY 2008, the FEC was able to process 91 percent of the reports within 30 days of receipt.

The FEC's website (www.fec.gov) represents the major source of Federal campaign finance information. The FEC website provides access to the campaign finance data that has 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. During FY 2008, the website received approximately 169.5 million hits.

Figure 4 – Total Website Hits (in millions)

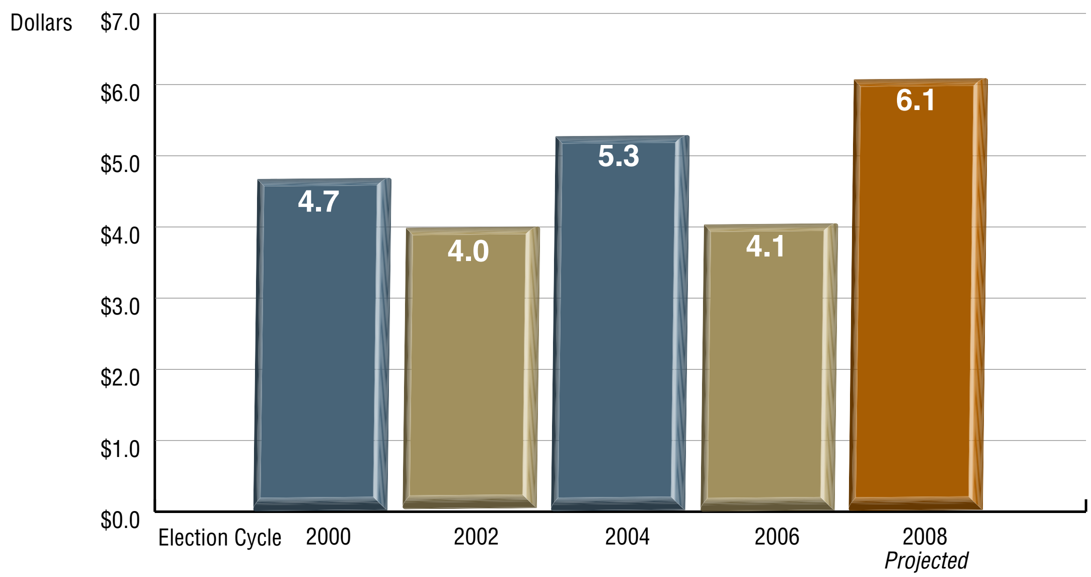


To make campaign finance data more accessible to the public, the FEC launched an interactive map providing users immediate access to contribution information for the 2008 Presidential, House and Senate elections. Users can access the amount of funds raised on a state-by-state basis, contributions, cash-on-hand, and the distribution of contributions by amount with a simple click at www.fec.gov/DisclosureSearch/mapApp.do. 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.

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 5 illustrates that expenditures related to Federal elections are on the rise, especially as they relate to a Presidential election year. Total receipts collected as of September 30, 2008 were slightly over $5.0 billion, while disbursements were approximately $4.2 billion. As the election cycle crosses fiscal years, the FEC is projecting disbursements for the 2008 Presidential election to near $6.1 billion.

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, increasing the potential for misappropriation of funds.

Figure 5 – Expenditures in Federal Elections (in billions)



Objective B: 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 campaign finance violations. Instances of non-compliance may lead to an 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. By law, all these matters must remain confidential until they are closed. Violations involving the late submission of FEC reports or failure to file reports are subject to the Administrative Fine program.

Performance Measures

- Conduct educational conferences and host roundtable workshops on the campaign finance law each election cycle, achieving a mean satisfaction rating of 4.0 on a 5.0 scale 100% of the time
- Issue press releases summarizing completed compliance matters within two weeks of a matter being made public by the Commission
- Issue quarterly press releases containing summaries of campaign finance data
- Process 100% of enforcement cases within an average of 15 months of receipt
- Process 75% of the cases assigned to Alternative Dispute Resolution within 155 days of a case being assigned

- Process 75% of reason-to-believe recommendations for the Administrative Fine Program within 60 days of the original due date of the subject untimely or unfiled report
- Process 75% of the challenges in the Administrative Fine Program within 60 days of a challenge being filed
- Conclude non-Presidential audits with findings in an average of 10 months, excluding time delays beyond the Commission's control, such as subpoenas and extension requests
- Conclude non-Presidential audits with no findings in an average of 90 days from beginning of fieldwork
- Conclude Presidential audits in an average of 24 months of the election, excluding time delays beyond the Commission's control, such as subpoenas and extension requests

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 to respond to inquiries regarding campaign finance data.

One way the Commission encourages voluntary compliance is by hosting conferences across the country, where Commissioners and staff explain how the *Act* applies to candidates, parties and political action committees. These conferences address recent changes in campaign finance laws and focus on fundraising and reporting regulations. The FEC held five conferences in FY 2008, three in the District of Columbia, one in St. Louis, Missouri, and one in Orlando, Florida. The FEC also held a roundtable workshop on pre-election communications and a seminar for nonconnected committees during FY 2008. The success of these efforts is evidenced by the evaluation scores and comments received. The overall rating for each event exceeded a 4.0 out of a possible 5.0.

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 by representatives of candidates or political committees who believe 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.

Closed enforcement matters are available online through the Commission's Enforcement Query System at http://eqs.sdrdc.com/eqs/searcheqs.

Office of General Counsel

Enforcement matters are handled by the OGC 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. The Commission processed 71 enforcement cases during the fiscal year, which were processed in an average of 16.9 months. The Commission was able to close 47 cases (66%) within 15 months. The goal of processing 100 percent of enforcement cases within an average of 15 months of receipt was not met due to the absence of a quorum of Commissioners. The absence of a quorum extended the average closure time by preventing the agency from closing enforcement cases. Accordingly, we expect that these processing numbers will improve over the next fiscal year as matters recommended to the Commission for closure will be processed through the ordinary course.

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.

Generally, a case is considered processed when it is closed. A case is closed when the Commission votes on the recommendation made by ADR as to what final action should be taken. The number of cases processed through ADR is much lower than usual, which was directly attributable to the lack of a quorum of Commissioners for six months. During FY 2008, ADR processed 12 cases to closure. Of the12 cases closed, nine were closed within 155 days, thus meeting the benchmark of 75 percent.

In addition, the ADR processed 45 cases to the point of sending them to the Commission with a recommendation for concluding the matter. As of September 30, 2008, these cases were still pending a vote of the Commission. Accordingly, these cases are expected to be closed in FY 2009.

When both categories of cases are considered together, 57 in total, the 155-day benchmark period was achieved 64 percent of the time.

Administrative Fine Program

In response to a legislative mandate, an Administrative Fine (AF) Program was implemented in July 2000 to address untimely filing or non-filing of disclosure reports in a more efficient and effective manner. This program is administered by the Office of Administrative Review and RAD, which are within the Office of Compliance.

Since the Program's inception, the Commission has closed 1,641 cases and assessed fines of almost $3.2 million.

As previously noted, the lack of a quorum had an impact on the number of cases opened and closed as well as the number of challenges received. Through the first three quarters of fiscal year 2008, only five cases were opened, seven challenges were received, and 16 cases were closed. By the close of this fiscal year, an additional 112 cases were opened and 12 cases were closed, with total fines assessed for the fiscal year at $34,861. Approximately 79.2 percent of the reason to believe (RTB) recommendations were processed within 60 days of the reports' due dates, while only approximately 14 percent of challenges were processed within 60 days of the challenges' receipt dates.

On-going extensive legal analysis required for earlier challenges meant these cases were processed outside the 60-day target. The more recently received challenges were processed within this target, an indication that, had a full Commission been in place for the entire fiscal year and new challenges been received in response to RTB findings, it is expected that the challenge review performance measure would have been achieved.

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 26 U.S.C., the FEC audits all recipients of public funds. In addition, pursuant to 2 U.S.C. §438(b), the Commission audits non-Presidential committees that, according to FEC determinations, have not complied with the law. The FEC publishes its findings in audit reports, which can be found at http://www.fec.gov/audits/audit_reports.shtml.

The FEC's goals with respect to conducting audits in a timely and efficient manner are to:

- Conclude non-Presidential (for cause) audits with findings in an average of 10 months, excluding time delays beyond the Commission's control, such as subpoenas and requests for extensions of time to respond to audit reports;
- Conclude non-Presidential audits with no findings in an average of 90 days from the beginning of field work; and
- Conclude Presidential Audits in an average of 24 months of the general election, excluding time delays beyond the Commission's control, such as subpoenas and requests for extensions of time to respond to audit reports.

Generally, an audit concludes with the public issuance of an audit report following the Commission's approval. However, due to the lack of a Commission quorum in FY 2008, some audit reports were not approved. Additionally, no new audits were conducted above those previously approved before the Commission lost its quorum. The Audit Division notes that under the circumstances of the lack of a Commission quorum, for the purpose of measuring performance, forwarding audits reports for Commission approval concluded the audit.

In FY 2008, the Audit Division issued to the public or forwarded for Commission approval 31 audit reports resulting from audits "for cause." Findings were reported in 23 out of the 31 audits. The average time to conclude 95 percent of these audits was 10 months. The remaining eight audits resulted in no findings, and were concluded in an average of 2.94 months.

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. In FY 2008, the Commission approved the eligibility of seven candidates to receive Presidential Primary Matching Funds. This is in addition to one candidate approved eligible in FY 2007 for a total of eight candidates for the 2008 election cycle. One candidate subsequently withdrew from the program. Audits of the remaining seven candidates began in fiscal year 2008, as Commission approval was not necessary to conduct Title 26 audits. The Commission is on track to accomplish its goal of completing these Presidential audits within 24 months after the 2008 Presidential election. After the 2008 general election, the FEC will audit the publicly funded national convention committees, their host committees and one recipient of General Election public funding.

Objective C: 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

- Complete rulemakings within specific time frames that reflect the importance of the topics addressed, proximity to upcoming elections, and externally established deadlines 100% of the time
- Issue all advisory opinions within 60-day and 20-day statutory deadlines 100% of the time
- Issue expedited advisory opinions for time-sensitive highly significant requests within 30 days of receiving a complete request, or a shorter time when warranted, 100% of the time
- Ensure that court filings meet all deadlines and rules imposed by the Courts 100% of the time
- Process public funding payments in the correct amounts and within established time frames 100% of the time

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

Regulations

The FEC publishes its regulations, which are codified in Title 11 of the *Code of Federal Regulations* (*CFR*). 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 to either write new Commission regulations or revise existing regulations.

The Policy Division of OGC drafts Notices of Proposed Rulemaking (NPRMs) which, once adopted by the Commission, are published in the *Federal Register*. NPRMs are also made available on the FEC's website at http://www.regulations.gov/. NPRMs provide an opportunity for members of the public and the regulated community to review proposed regulations, submit written comments to the Commission and testify at public hearings, which are conducted at the FEC when appropriate. The Commission considers the comments and testimony and deliberates publicly regarding the adoption of the final regulations. The text of final regulations and the corresponding Explanations and Justifications, once adopted by the Commission, are published in the *Federal Register*.

The Commission worked on four rulemaking projects during FY 2008. The first rulemaking, which the Commission completed during Quarter 1, implements the Supreme Court's decision in *Wisconsin Right to Life* regarding electioneering communications. The *WRTL* rulemaking affected five existing regulations, and was completed in 121 days.

Two rulemakings required constructions of new statutory provisions in the *Honest Leadership and Open Government Act (HLOGA*), which changed the Commission's existing candidate travel rules and created a new reporting regime for lobbying entities that bundle contributions for candidates. By the end of the fiscal year, the Commission had voted on draft final rules implementing the *HLOGA*'s Travel Rules, and had held a public hearing on the Notice of Proposed Rulemaking for the Bundling Rules.

The final rulemaking that the Commission worked on during FY 2008 was the Millionaires' Amendment repeal, which implements the Supreme Court's decision in *Davis*.

Advisory Opinions

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.

The number of AO requests that the Commission receives is subject to cycles and is somewhat higher during election years. During FY 2008, the Commission completed 97 percent of AOs within the 60-day statutory deadline. The Commission did not receive any 20-day requests. Furthermore, the Commission issued five expedited advisory opinions during FY 2008, for which more than 50 percent were issued within 30 days of receiving a complete request. The average number of days from receipt of the complete AO request to issuance of the AO was 31 days. A summary of AOs can be reviewed at http://saos.nictusa.com/saos/searchao.

Defending Challenges to the *Act*

The Commission is the exclusive representative of the FEC before the Federal district and circuit courts, and the Supreme Court with respect to cases involving publicly financed presidential candidates. It also has primary responsibility for defending the *Act* and Commission regulations against court challenges. The Commission's court filings met all deadlines and rules imposed by the courts 100% of the time.

In a case decided last year by the Supreme Court, *FEC v. Wisconsin Right to Life*, the Commission defended against an "as applied" challenge to the electioneering communication provision of BCRA. In the aftermath of that decision, the Commission is defending its regulation implementing the *Wisconsin Right to Life* decision as well as a related challenge (*Citizens United v. FEC*) to disclosure provisions as applied to certain electioneering communications. The Commission prevailed before a three-judge district court in *Citizens United*, and the plaintiff has appealed to the Supreme Court.

In other ongoing litigation, the Commission is defending a lawsuit brought by SpeechNow.org, which alleges that the *Act's* limits on contributions to political committees is unconstitutional as applied to groups that receive contributions only from individuals and who make only independent expenditures with their funds. The Commission is also defending against claims that some of its regulations are unconstitutional and that it has unlawfully delayed its consideration of certain administrative complaints.

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. 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.

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;
- Pay any civil penalties assessed by the FEC; and
- Document that Primary candidates have met the "threshold requirement" for eligibility by raising in excess of $5,000 in each of 20 states.

The Commission processed seven threshold submissions (submissions to determine whether the candidates' met the eligibility requirements) and 30 non-threshold submissions. These submissions were processed in the correct amounts and within established time frames 100% of the time. The Commission certified a total of $27.2 million in federal matching funds in the 2008 campaign thus far.

The Commission approved payment of $84.1 million in federal funds for the general election campaign of Senator John McCain and Governor Sarah Palin. Presidential candidates accepting the federal payment are subject to a spending limit of $84.1 million, the amount of the payment, plus a combined personal spending limit of $50,000 from their personal funds. (All expenditures made by or on behalf of a Vice-Presidential candidate are considered to be made on behalf of the Presidential candidate.)

Legislative Recommendations

The Commission is empowered to recommend to the President and to Congress suggested improvements to the federal campaign finance law. In 2008, due to vacancies on the Commission, the Commission did not issue formal legislative recommendations. Nonetheless, the serving Commissioners requested that Congress extend the legislative authority for the Administrative Fine Program (AFP). H.R. 6296, which extends the AF program authority through 2013, passed the House of Representatives on July 15, 2008, and the Senate on October 2, 2008. The President signed it into law on October 16, 2008.

Previously in 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.

SECTION III

Auditor's Report and Financial Statements

Message From The Chief Financial Officer

November 15, 2008

The PAR summarizes the agency's annual accomplishments, in addition to providing financial and performance information. I am pleased that the FEC sustained an unqualified audit opinion on the financial statements this year. This performance benchmark validates our efforts to ensure that the financial statements of the agency, and of the funds for which we are stewards, are fairly presented. This achievement is also a testament to the hard work and dedication of the FEC's staff. This accomplishment has even greater significance this year, since the Commission was without a full quorum for six months of the fiscal year, as the Chairman mentioned.

The FEC is committed to effective and efficient management of its resources. In addition to the improvements mentioned by the Chairman, the agency also undertook the following efforts during FY 2008:

- Converted the processing of accounting transactions to an OMB certified financial management line of business (FMLOB) provider.
- Upgraded the procurement system to a web-based version. As part of this upgrade, the Commission also undertook a comprehensive review of its procurement efforts, which resulted in the issuance of updated procurement policies and procedures.
- Began implementation of a web-based Time and Attendance (T&A) system.
- Implemented the requirements of HSPD-12 with respect to ID badges.

These efforts help address the prior year's material weakness in internal control regarding a lack of an integrated financial management system. Still, additional steps are needed to fully eliminate the internal control deficiency. Until then, the Commission will continue to face challenges in financial reporting, as noted by the material weakness identified by the auditors again this year. Accordingly, the FEC will develop a corrective action plan in the first quarter of FY 2009 to remedy the control design deficiencies; continue to evaluate and strengthen controls; and develop a plan to achieve greater integration of performance and financial management systems. These efforts will lead to better performance management and decision making.

I look forward to another productive year in FY 2009 with a continuation of the same high level of financial management that resulted in our past successes.

Sincerely,

Brian J. Duffy
Acting Chief Financial Officer

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 2008 Financial Statements

DATE: November 12, 2008

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 (CG-LLP) for the fiscal year ending September 30, 2008. The audit was performed under a contract with and monitored by the Office of Inspector General (OIG) 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 (OMB) Bulletin No. 07-04, *Audit Requirements for Federal Financial Statements*, as amended.

Opinion on the Financial Statements

The consolidated balance sheets of the Federal Election Commission (FEC) as of September 30, 2008 and 2007 and the related statements of net cost, changes in net cost, changes in net position, and combined statement of budgetary resources for the years then ended (hereinafter collectively referred to as the "financial statements") were audited. 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 Independent Auditor's Report concluded that the FEC's financial statements present fairly, in all material respects, the financial position of the FEC as of September 30, 2008 and 2007, 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.

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, as amended, but not for the purpose of expressing an opinion on the effectiveness of FEC's internal control over financial reporting. The auditors 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. 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 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 affects 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 a 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 controls. 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:

- Financial Accounting and Reporting Controls

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 FEC's financial statements are free of material misstatements, CG-LLP performed tests of compliance with certain provisions of laws and regulations, non-compliance 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 No. 07-04, as amended. Tests of compliance were limited to these provisions and CG-LLP did not test compliance with all laws and regulations applicable to FEC.

The results of CG-LLP's tests of compliance with laws and regulations described in the audit report disclosed an instance of reportable noncompliance that is required to be reported under U.S. generally accepted government auditing standards or OMB guidance.

CG-LLP identified a reportable noncompliance in the area of:

- The Federal Managers' Financial Integrity Act (FMFIA)

<u>Audit Follow-up</u>

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 Follow-up*, 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.

<u>OIG Evaluation of Clifton Gunderson LLP's Audit Performance</u>

We reviewed CG-LLP's reports and related documentation and made necessary inquiries of its representatives. Our review was not intended to enable the OIG to express, and we do not express, an opinion on the FEC's financial statements, provide conclusions about the effectiveness of internal control or conclusions on FEC's compliance with laws and regulations. However, the OIG review disclosed no instances where CG-LLP did not comply, in all material respects, with *Government Auditing Standards.*

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
Inspector General

Attachments

Cc: Acting Staff Director
General Counsel
Acting Chief Financial Officer
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, 2008 and 2007, 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 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 Office of Management and Budget (OMB) Bulletin No. 07-04, *Audit Requirements for Federal Financial Statements,* as amended. 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 FEC as of September 30, 2008 and 2007, 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 accordance with *Government Auditing Standards*, we have also issued our reports dated November 7, 2008 on our consideration of FEC's internal control over financial reporting, and on our tests of 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 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's Discussion and Analysis section is not a required part of the financial statements, but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods

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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 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 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 7, 2008

Clifton Gunderson LLP
Certified Public Accountants & Consultants

Independent Auditor's Report on Internal Control Over Financial Reporting

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, 2008 and have issued our report thereon dated November 7, 2008. 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,* as amended.

The management of FEC is responsible for establishing and maintaining internal control to achieve the objectives of effective and efficient operations, and reliable financial reporting. 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, as amended, 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 a material weakness and a significant deficiency.

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. We consider the deficiency in Information Technology described below to be significant deficiency in internal control over reporting.

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 Financial Accounting and Reporting Controls described below is a material weakness.

****

MATERIAL WEAKNESS

I. Financial Accounting and Reporting Controls (Repeat Modified Finding)

The Accountability of Tax Dollars Act of 2002 (ATDA) extends to FEC a requirement to submit to the Congress and the Director of the Office of Management and Budget (OMB) audited financial statements. OMB Circular A-136, *Financial Reporting Requirements*, defines the form and content of financial statements to be prepared by the agency. To accomplish the objective of complying with the ATDA, the agency is required to develop a system to prepare a complete set of financial statements on a timely basis in accordance with generally accepted accounting principles. The statements are to result from an accounting system that is an integral part of an integrated financial management system containing sufficient structure, effective internal control and reliable data. Financial reporting also consists of policies and procedures related to the processing and summarizing of accounting entries, and the preparation of financial statements.

Below are descriptions of the control deficiencies within FEC's financial reporting environment:

A. Insufficient Resources and Personnel with Appropriate Federal Accounting and Reporting Skill Sets (New Finding)

FEC did not have adequate resources and employees with appropriate skills sets to handle financial management accounting and reporting. There was turnover in key financial positions during the year and adequate resources were not always available to fill the vacancies. For example, the staff accountant position has been vacant since March 2008. This position is responsible for performing monthly reconciliations and calculating accrual and property, plant and equipment amounts reported on the financial statements. FEC has not developed a program to cross train other Office of Chief Financial Officer (OCFO) personnel in performing these tasks and contractors hired to perform some of these duties were done so intermittently throughout the year. As a result, the Accounting Officer had to take on some of these responsibilities leaving FEC with insufficient resources to effectively administer quality assurance procedures within their financial reporting environment.

This deficiency was aggravated by the migration of the agency's accounting and financial reporting operations to a service provider during FY 2008. FEC's understanding of key processes, controls and reports utilized by the service provider is on-going and was not obtained timely enough to adequately assess associated control risks and develop or redesign internal controls to mitigate those risks. These deficiencies are key factors in many of the weaknesses in financial reporting as described further in this report.

GAO Standards for Internal Control in the Federal Government states "People are what make internal control work. The responsibility for good internal controls rests with all managers. Management sets the objectives, puts the control mechanisms and activities in place, and monitors and evaluates the control. However, all personnel in the organization play important roles in making it happen". Moreover, "All personnel need to possess and maintain a level of competence that allows them to accomplish their assigned duties, as well as understand the importance of developing and implementing good internal control. Management needs to identify appropriate knowledge and skills needed for various jobs and provide needed training, as well as candid and constructive counseling, and performance appraisals."

The need for employees with analytical and federal accounting and reporting competencies will only increase as FEC further integrates its financial management system. Without the adequate staffing levels and the proper skill sets, the FEC will continue to encounter challenges in the financial reporting process including preparing financial reports in a timely manner, and consistent with applicable laws and regulations.

Recommendations:

1. Fill vacant positions within the OCFO as soon as possible. Ensure that the individuals possess analytical, Federal accounting and financial reporting knowledge and experience to enhance the FEC's ability to comply with accounting and financial reporting standards.

2. Evaluate the resources and appropriate skills needed throughout the agency to meet FEC's financial management and reporting responsibilities and implement a plan on achieving the results and recommendations of the evaluation.

3. Ensure that appropriate and on-going training is provided to FEC employees on federal accounting and reporting and the accounting service provider's financial system. Also, ensure OCFO personnel are properly cross-trained in department activities.

Management Response:

Management generally concurs with the finding and recommendations. FEC management is committed to improving its internal control and accordingly, will develop a corrective action plan to address the issues identified.

B. Inadequate Financial Statement Preparation and Reporting (Modified Repeat Finding)

OMB Circular A-136, *Financial Reporting Requirements,* "preparation of the annual financial statements is the responsibility of the agency's management. In carrying out this responsibility, each agency chief financial officer should prepare a policy bulletin or guidance memorandum that guides the agency's fiscal and management personnel in the preparation of the annual financial statements." The existence of written procedures will provide structure and accountability for the financial statements preparation and review processes. They also help ensure activities are carried out in accordance with management directives.

Our audit disclosed the following control deficiencies in FEC's financial statement preparation and reporting process. Many of these deficiencies were identified during the prior year audit. FEC's audit follow-up process was ineffective in resolving these deficiencies in a timely manner.

- FEC did not have a comprehensive policy bulletin or guidance memorandum as required by OMB Circular A-136. The lack of formalized policies and procedures is a contributing factor for the additional control deficiencies described below.

- Accounting entries recorded in the accounting system or posted to the financial statements as "on-top" adjustments were not reviewed timely by FEC or the review was not independently performed by someone other than the preparer. Other controls in place such as management's review of the financial statements were ineffective in detecting incorrect accounting entries made by the service provider. Further, an audit trail supporting the entry was not properly maintained. Lack or inadequate internal control increases the risk of financial statement misstatements. Our audit identified accounting posting errors related to the following transactions:

    - The June 30, 2008 financial statements improperly included:
        - $1.5 million in accrued payroll costs;
        - $769,314 in advanced payments to GSA;
        - $41,530,546 in budget authority temporarily unavailable during the continuing resolution period; and
        - Accrued employer contributions and payroll taxes costs.

    - The Draft September 30, 2008 financial statements provided included:
        - Approximately $2.6 million of collections from custodial activity in Fund Balance with Treasury and the Custodial Liability line items on the Balance Sheet improperly; and
        - Adjustments made by the service provider to the trial balance, after conversion, which impacted the Statement of Budgetary Resources for Expired Allotments were not sufficiently documented.

- FEC has not established a formalized timeline for completing key processes and controls related to the financial statement process. For example, we noted that the Finance Office Checklist detailing month end closing and financial statement preparation procedures was not prepared throughout the year. Furthermore, control activities, such as fluctuation analysis and relationship testing, were not finalized until after the financial statements were issued to the auditors for audit.

- A mechanism for tracking manual accounting entries sent to the service provider was not developed, which prevented FEC from being able to verify accounting entries were posted as intended or properly.

As a result of the control deficiencies noted above, the financial statements provided for audit contained many inconsistencies, errors and typos throughout the document. We also noted that the financial statements provided were inconsistent with the guidance issued by OMB Circular A-136. Although the FEC has corrected all the items identified through the audit process, adequate controls were not in place to sufficiently detect such mistakes in a timely manner.

Recommendations:

4. Formalize and periodically update policies and procedures to a) ensure segregation of duties, b) provide guidance to management and staff in recording both recurring and unique transactions, including budgetary accounts, and c) provide guidance to management and staff in executing the financial statement preparation process in a manner that enhances the timeliness of financial statement preparation and minimizes the risk of preparing inaccurate financials.

5. Implement control activities to help ensure accounting transactions are recorded correctly, timely and are properly reviewed and adequate support documentation is maintained. Some of these control activities should include, but not be limited to:

   - Improving analytical and quality control review of journal vouchers, reconciliations and the financial statements, including interim financial statements. Procedures should include independent supervisory review of controls performed by someone other than the preparer.
   - Developing management's expectations for fluctuation analysis, which includes setting the criteria for variances considered significant. Each expectation that is not met should be researched and results collaborated by data. Analytical tools that could be used are ratio analysis and trend analysis, as well as predictive techniques such as calculation of an expected balance. Results should be documented and maintained for management review and audit purposes.
   - Implementing proper and timely cut-off controls from processing transactions and in preparing the financial statements to allow for management's timely analysis of financial data and for audit purposes.
   - Researching the accounting treatment of unique and non-reoccurring transactions and seeking specific guidance from accounting standard-setters from the beginning to ensure the recording of such events are properly included in the financial statement account balances and to ensure accuracy and transparency of financial accountable events.

6. Establish formalized policies and procedures for performing continuous assessment of risk factors associated with financial reporting, evaluating relevant controls and developing or redesigning controls to mitigate risks. These policies should include a well-defined documentation process that contains an audit trail, verifiable results, and specify retention periods so that someone not connected with the procedures can understand the assessment process.

7. Enforce the use of the Finance Office Check List throughout the entire fiscal year.

8. Establish a mechanism for tracking manual journal entries sent to the service provider and maintaining associated support documents.

9. Develop or redesign controls that strengthen the accountability structure related to the process for resolving audit findings

Management Response:

Management generally concurs with the finding and recommendations. FEC management is committed to improving its internal control and accordingly, will develop a corrective action plan to address the issues identified.

C. Integrate Financial Management System (Modified Repeat Finding)

FEC utilizes the general ledger and core financial management system (general ledger system) of its accounting service provider. The general ledger system is not capable of generating most user reports for data analysis on a real time basis. Users have to request from the accounting service provider some basic reports, which are generated by another software application.

Other financial management systems used at FEC include excel spreadsheets, database applications, and PeopleSoft (PS). These systems are used to accumulate and summarize data for the following financial transactions, all of which are material to FEC's financial statements:

- Collections, Accounts Receivable, and Custodial Liability specific to Fines and Penalties;
- Property and equipment, accumulated depreciation, and depreciation expense;
- Obligations; and
- Payroll and time attendance reporting.

None of these FEC financial management systems are interfaced with the general ledger system. OMB Circular No. A-127, *Financial Management Systems,* requires that each agency establish and maintain a single integrated financial management system. Without a single integrated financial management system to ensure timely and accurate financial data, poor policy decisions may occur due to inaccurate or untimely information. Managers are less likely to be able to report accurately to the President, Congress, and the public on Government operations in a timely manner. And, scarce resources are more likely to be directed toward the collection of information rather than to delivery of the intended programs.

As a result of these systems not being integrated, significant time is required to compile the information. In addition to gathering the data from the offices, the OCFO manually incorporates the information into each stand alone system in order to generate the necessary documentation to support the balances reported on the financial statements. For example, the OCFO must request accounts receivable information from three divisions since there is no mechanism in place to automatically notify the OCFO that a fine or penalty was assessed. After the OCFO obtains the relevant information, which may not always be received in a timely manner, the data is keystroked into a database. A journal entry is prepared for submission to the service provider to record the details into the accounting system. Given the number of times the information is separately recorded into different systems, there is an increased risk for input error. A monthly reconciliation is performed of the accounts receivable, however, without the staff accountant, as mentioned above, the recording of transactions may not always occur timely or accurately.

Another example where the lack of an integrated financial system impacts efficiency pertains to the recording of obligations. The FEC has improved its procurement operations from the prior year by converting to a web-based procurement system that requires all purchase requests to be processed electronically, which alleviates the duplication of entry in preparing the obligating document. However, the procurement system is not integrated to the financial management system. Therefore, several areas for error still exist. Specifically, the obligating document is provided via e-mail to the Finance Office for review and submission to the service provider. Should the Procurement Office forget to send the obligating document to the Finance Office, there is an increased risk that the obligation does not get recorded in a timely manner or at all. Once the Finance Office receives the obligating document, they then print the document to submit the hard copy document to the service provider. At this time, the FEC does not send the document to the service provider electronically. Therefore, this process further increases the risk that the obligation may not be recorded timely or at all. Finally, once the service provider receives the obligating document, they keystroke in the relevant financial information into the accounting system, providing for the opportunity for an input error.

Having a single, integrated financial management system does not necessarily mean having only one software application within each agency covering all financial management system needs. Also, it does not mean that all information is physically located in the same database. Rather, 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 system support. Integration means that the user is able to have one view into systems such that, at whatever level the individual is using the system, he or she can obtain needed information efficiently and effectively through electronic means. Interfaces are acceptable as long as the supporting detail is 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 reconciliations between systems, where interface linkages are appropriate, must be maintained to ensure data accuracy.

Without these systems being integrated, controls surrounding the processing, recording and review of financial transactions become much more critical and require greater resources to ensure completeness and accuracy. FEC management continues to place its emphasis on the compilation of the financial and performance data, but due to the lack of resources it is not capable of sufficiently performing the reviews needed to alleviate the control risk associated with the lack of an integrated financial management system.

Recommendation:

10. Re-evaluate if interfacing its standalone financial management systems with the service provider's system is feasible and/or cost effective. If not feasible and/or cost effective, consider the subsystems used by the service provider's financial management systems.

Management Response:

Management generally concurs with the finding and recommendations. As of February 2008, the FEC transitioned the processing of its accounting transactions to an OMB-certified line of business provider. FEC management will evaluate its stand-alone financial management systems and develop a corrective action plan to address the issues identified.

These deficiencies in internal control may adversely affect any decision by management that is based, in whole or in part, on information that is inaccurate because of these deficiencies. Unaudited financial information reported by FEC, including budget information, also may contain misstatements not prevented or detected because of these deficiencies.

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SIGNIFICANT DEFICIENCY

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

A. Commission-Wide Security Administration Needs To Be Enhanced (Repeat Finding)

An entity-wide security management program should be in place to establish a framework and continuing cycle of activity to manage security risks, develop security policies, assign responsibilities, and monitor the adequacy of computer security related controls. It should also represent the foundation for an entity's security control structure and a reflection of senior management's commitment to addressing security risks.

During our Fiscal Year 2008 review of FEC's security program, we noted that FEC made progress in addressing prior years' findings, notably a contract was awarded on September 16, 2008 to certify and accredit its major applications and general support systems. Also, FEC had developed its Disaster Recovery Plan. However, continued efforts are required especially in the areas of security administration and oversight. Specifically, we noted that FEC had not fully implemented all security procedures and standards; had not finalized and implemented an information classification policy; had not finalized and implemented its certification and accreditation policy. Furthermore, FEC is currently in the process of developing a security plan for its Local Area Network (LAN) that incorporates the results of the LAN Risk Assessment

Office of Management and Budget (OMB) Circular No. A-130, Appendix III *Security of Federal Automated Information Resources*, requires agencies to implement and maintain a program to assure that adequate security is provided for all agency information collected, processed, transmitted, stored, or disseminated in general support systems and major applications.

Without an effective entity-wide security program plan, FEC has an increased risk that security controls are inadequate and inconsistently applied. Such conditions may lead to insufficient protection of sensitive data and high expenditures for controls over low risk resources.

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:

- 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 is currently in the process of developing a security plan for its LAN that incorporates the results of the LAN Risk Assessment. However, the security plan is still in the development phase and has not been finalized and approved. **(Repeat Finding)**
- There are weaknesses in FEC's program for the continuous monitoring and evaluation of the computer security policy and control effectiveness. FEC does not utilize corrective action plans for all internal reviews of security controls. **(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).**
- There is currently no process in place to ensure that contractors undergo background investigations before obtaining access to FEC systems or data. **(Repeat Finding)**
- The PeopleSoft application is currently running on an Oracle Release 8i Relational Database Management System that is no longer supported by the vendor. **(Repeat Finding)**

Recommendations:

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

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

13. Utilize corrective action plans for all reviews of security controls whether performed internally or by a third-party.

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

15. Implement a process to ensure that background investigations are performed on all contractors prior to granting them access to FEC system resources.

16. FEC should move all of its PeopleSoft financial processing capabilities to GSA or update its existing platform to vendor-supported versions/releases.

Management Response:

FEC agrees with the majority of elements within this finding. The FEC awarded a contract to certify and accredit its major applications and general support systems on September 16, 2008. On September 23, 2008 a formal Kick-Off meeting was held to formally begin work on the contract. Since that time the vendor has provided the Contracting Officer Technical Representative (COTR) with an updated project plan that describes how and when certification and accreditation objectives are to be achieved. The vendor is currently updating system characterizations and performing a system classification for each major application and general support system. The Certification and Accreditation contract specifies line items to address the following issues identified within this finding:

- *Finalizing and implementing a modified certification and accreditation and information classification policies.*
- *Updating current security plans by incorporating the results of the recently completed risk assessment.*
- *Developing a Program of Actions and Milestones to monitor and evaluate the internal review of security controls.*
- *Certify and Accredit FEC major applications and general support systems.*

On September 29, 2008 the Director of Human Resources addressed the issue of contractor background investigations by issuing the following policy "that all contracting personnel from this date forward (September 29, 2008) must obtain a background investigation prior to obtaining access to FEC systems."

With respect to Oracle 8i, due to legacy issues associated with some FEC applications the current version of Oracle 8i is required. Although the vendor no longer provides support for this version of Oracle it does provide limited support which includes assisting customers with work-arounds to issues that may arise. In addition the FEC has built a considerable amount of experience and internal expertise over the years this product has been in its inventory. In addition to its considerable experience, the FEC has tested and maintains Oracle 8i application and data backups allowing it to restore any databases to a usable state in the event of any mishap.

The FEC recognizes the risk associated with maintaining a product with limited support. Accordingly the FEC is relying upon its considerable internal expertise, restricted access to only a few persons, backup and restoral capabilities and Oracle's limited support as compensating factors until the application can be removed from its inventory.

B. Disaster Recovery and Continuity of Operations Plan Need to be Developed (Repeat Finding)

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 that FEC has not developed a Continuity of Operations Plan (COOP) to support the continuation of its core mission in the event of a disaster or other interruption that renders the FEC's facilities unusable. **(Repeat Finding)**

Recommendation:

17. Develop and implement a Disaster Recovery Continuity of Operations Plan (COOP).

Management Response:

Management agrees with the issue presented in this finding, and in fiscal year 2008 implemented a multiple year three phase project plan to develop and implement a FEC-Wide Continuity of Operations Plan (COOP). Phase One consisted of developing an Office of Information Technology (OIT) Disaster Recovery Plan (DRP), Phase Two (Kick Off Meeting September 29, 2008) consists of preparing for the migration of the OIT DRP into a COOP, and Phase Three consists of implementing a Commission wide COOP. Bear in mind that, Phase Three is contingent upon receiving adequate funding and senior management support.

C. Logical Access Control Needs to be Strengthened (Modified Repeat Finding)

Achieving an adequate level of information protection is highly dependent upon consistently maintaining 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. 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 a weakness 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:

We noted the following control weaknesses over monitoring access to FEC's networks, systems and physical facility:

- 4 out of 10 separated employees still have active network accounts; and
- There is currently no exit clearance process in place for contractors to ensure that all FEC property is returned and all access permissions are removed.

Recommendations:

18. FEC should 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.

19. Implement an exit clearance process to track separated FEC contractors and ensure that their access permissions are removed and all FEC property has been returned.

Management Response:

Although the FEC has a documented process in place to terminate FEC resources and collect property from separated employees and contractors, it concurs that this process can be improved. To this end, the FEC has established a working group to implement more stringent procedures to ensure that network access is appropriately curtailed. In addition OIT will soon be implementing an automated information system to better deal with the issues identified in this finding. The New FEC Access System (FAS) includes processes for full time employees, interns, and contractors and will eliminate the discrepancies described in this finding. FAS will track staff and contractors from the start of their employment or contract at the Commission to exit and allow managers to request and document changes in network and application access. FAS will enable a higher degree of coordination among offices to ensure that user accounts are disabled and equipment is properly returned per FEC policy. FAS will retain all historical information regarding; account creation, changes to access rights, system resources, and termination information regarding a particular staff or contractor. FAS is now in the final testing stages and is tentatively scheduled for full implementation by December 1, 2008.

III. Other Matter

As required by OMB Bulletin No. 07-04, as amended, we compared the material weaknesses disclosed during the audit with those material weaknesses reported in the FEC's FMFIA report that relate to control over financial reporting. Our audit identified a material weakness related to the financial statement preparation and reporting as reported above that was not included in the FEC's FMFIA report.

IV. 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 7, 2008.

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 7, 2008

APPENDIX A
FEDERAL ELECTION COMMISSION
STATUS OF PRIOR YEAR FINDINGS AND RECOMMENDATIONS
September 30, 2008

PY Rec. No.	Condition/Audit Area	Recommendation	Current Status
Material Weakness			
I. Integrated Financial Management System			
1.	Integrated Financial Management System	Assess the extent of financial management system integration needed for existing systems while outsourcing the accounting operations to a third party service provider.	Recommendation closed.
2.	Integrated Financial Management System	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 controls 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 statements; • 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; and • Establish a timeline for timely receipt of completed accounts receivable schedules by the finance office from the program offices.	Recommendation open: reported in FY 2008 as a material weakness.
3.	Integrated Financial Management System	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	Recommendation closed.

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APPENDIX A
FEDERAL ELECTION COMMISSION
STATUS OF PRIOR YEAR FINDINGS AND RECOMMENDATIONS
September 30, 2008

PY Rec. No.	Condition/Audit Area	Recommendation	Current Status
		recording and classifying transactions.	
4.	Integrated Financial Management System	Provide employee training on procurement, appropriation law, budget execution, and financial reporting, as applicable to ensure financial reporting and fund control policies are consistently and accurately executed.	Recommendation open: reported in FY 2008 as a material weakness.
5.	Integrated Financial Management System	Ensure that FEC complies with regulatory agencies' reporting requirements.	Recommendation updated: reported in FY 2008 management letter
		Significant Deficiencies	
II. Information Technology			
6.	Security Administration	Perform risk assessments, as part of FEC's overall strategy to mitigate risks associated with its IT environment.	Recommendation closed
7.	Security Administration	Finalize and implement FEC's information classification policy and certification and accreditation policy along with any accompanying standards.	Recommendation open: reported in FY 2008 as a significant deficiency.
8.	Security Administration	Incorporate the results of risk assessments into FEC security plans.	Recommendation open: reported in FY 2008 as a significant deficiency.
9.	Security Administration	Certify and accredit all major applications and mission critical general support systems.	Recommendation open: reported in FY 2008 as a significant deficiency.
10.	Security Administration	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.	Recommendation closed. Re-opened in FY 2008 for New Contractors
11.	Disaster recovery & Continuity of Operations	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	Recommendation closed

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APPENDIX A
FEDERAL ELECTION COMMISSION
STATUS OF PRIOR YEAR FINDINGS AND RECOMMENDATIONS
September 30, 2008

PY Rec. No.	Condition/Audit Area	Recommendation	Current Status
		or disaster.	
12.	Disaster recovery & Continuity of Operations	Establish an alternate processing site and incorporate the results of the BIA into the contingency plan.	Recommendation closed
13.	Disaster recovery & Continuity of Operations	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.	Recommendation closed
14.	Disaster recovery & Continuity of Operations	Develop a COOP that addresses measures and procedures to follow in the event of a long-term interruption.	Recommendation open: reported in FY 2008 as a significant deficiency.
15.	Logical Access, System Software and Change Management Controls	Transfer processing to a service provider or update existing platform to vendor-supported versions/releases.	Recommendation open: reported in FY 2008 as a significant deficiency.
16.	Logical Access, System Software and Change Management Controls	Write audit trails related to DBA activity to Operating Systems logs and limit DBA's access to these logs.	Recommendation closed
17.	Logical Access, System Software and Change Management Controls	Maintain documentation to support the testing and approval of system software changes.	Recommendation closed
18.	Logical Access, System Software and Change Management Controls	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.	Recommendation closed
19.	Logical Access, System Software	Promptly terminate access to FEC resources for separated employees.	Recommendation open: reported in FY

APPENDIX A
FEDERAL ELECTION COMMISSION
STATUS OF PRIOR YEAR FINDINGS AND RECOMMENDATIONS
September 30, 2008

PY Rec. No.	Condition/Audit Area	Recommendation	Current Status
	and Change Management Controls	Procedures should be documented and implemented to coordinate separations between Human Resources and IT management to ensure user accounts are immediately disabled upon termination.	2008 as a significant deficiency.
20.	Logical Access, System Software and Change Management Controls	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.	Recommendation closed

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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, 2008, and have issued our report thereon dated November 7, 2008. 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 Office of Management and Budget (OMB) Bulletin 07-04, *Audit Requirements for Federal Financial Statements,* as amended.

The management of FEC is responsible for complying with laws and regulations, and government-wide policies 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, and government-wide policies, 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, as amended. 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, and government-wide policies was not an objective of our audit, and, accordingly, we do not express such an opinion.

The results of our tests of compliance with applicable laws and regulations, and government-wide polices described in the preceding paragraph disclosed an instance of reportable noncompliance that is required to be reported under U.S. generally accepted government auditing standards or OMB guidance and is described in the following paragraphs.

<u>The Federal Managers' Financial Integrity Act (FMFIA)</u>

The FMFIA requires agencies to establish management controls over their programs and financial systems as stated in the following sections of the Act:

- Section 2 seeks to assess internal controls necessary to ensure obligations and costs are in compliance with applicable law; funds, property, and other assets are safeguarded against waste, loss, unauthorized use, or misappropriation; and revenues and expenditures are properly recorded and accounted for to permit the preparation of accounts and reliable financial and statistical reports.

- Section 4 seeks to assess nonconformance with government-wide financial systems requirements.

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OMB Circular A-123, *Management's Responsibility for Internal Control,* is issued under the authority of the FMFIA (section 2). OMB Circular A-123 states that management is responsible for establishing and maintaining internal control to achieve the objectives of effective and efficient operations, reliable financial reporting, and compliance with applicable laws and regulations. Management shall consistently apply the internal control standards to meet each of the internal control objectives and to assess the internal control effectiveness.

OMB Circular A-127, *Financial Management Systems*, offers guidance in implementing FMFIA (section 4). OMB Circular A-127 requires that "Financial management systems shall be designed to provide for effective and efficient interrelationships between software, hardware, personnel, procedures, controls, and data contained within the systems".

The FEC has not fully complied with certain requirements of the FMFIA. See details in our Independent Auditor's Report on Internal Control, Sections I and II. The key items we identified include:

- Insufficient resources and personnel with appropriate Federal accounting and reporting skill sets;
- Inadequate financial statement preparation and reporting controls;
- Financial management systems not fully integrated; and
- Weaknesses in information technology.

This report is intended solely for the information and use of the management of FEC, FEC Office of Inspector General, GAO, 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 7, 2008

BALANCE SHEET

As of September 30, 2008 and 2007 (in Dollars)

Assets (Note 2)	**2008**	**2007**
Intragovernmental:		
Fund balance with Treasury (Note 3)	$ 10,603,627	$ 10,250,297
Total Intragovernmental	10,603,627	10,250,297
Accounts receivable, net (Notes 2 & 4)	530,187	817,309
General property and equipment, net (Note 5)	7,714,712	7,745,134
Advances to others	898	6,927
Total assets	**$ 18,849,424**	**$ 18,819,667**
Liabilities (Note 6)		
Intragovernmental:		
Accounts payable	$ 84,455	$ –
Employer contribution and payroll taxes payable	412,450	297,573
Custodial liability	530,187	807,032
Deferred rent	783,538	–
Payable to Treasury	–	10,277
Total Intragovernmental	1,810,630	1,114,882
With the public:		
Accounts payable	1,775,054	901,977
Accrued payroll and benefits	1,468,908	1,143,513
Unfunded leave	2,161,272	1,964,478
Other	2,712	663
Total liabilities	**7,218,576**	**5,125,513**
Net Position		
Unexpended appropriations	6,866,188	7,912,472
Cumulative results of operations	4,764,660	5,781,682
Total net position	**11,630,848**	**13,694,154**
Total liabilities and net position	**$ 18,849,424**	**$ 18,819,667**

The accompanying notes are an integral part of these statements.

STATEMENT OF NET COST

For the Years Ended September 30, 2008 and 2007 (in Dollars)

Program costs:	**2008**	**2007**
Administering and Enforcing the FECA:		
Gross Costs	$ 62,024,007	$ 56,599,698
Less: Earned revenue	–	(222,137)
Net cost of operations (Note 9)	**$ 62,024,007**	**$ 56,377,561**

The accompanying notes are an integral part of these statements.

STATEMENT OF CHANGES IN NET POSITION

For the Years Ended September 30, 2008 and 2007 (in Dollars)

	2008 Consolidated Total	2007 Consolidated Total
Cumulative Results of Operations:		
Beginning balance	$ 5,781,682	$ 6,808,109
Beginning balance, as adjusted	5,781,682	6,808,109
Budgetary Financing Sources:		
Appropriations used	58,873,362	53,029,611
Transfers in/out without reimbursement	–	(10,277)
Other Financing Sources (Non-Exchange):		
Imputed financing from costs absorbed by others	2,133,623	2,331,800
Total Financing Sources	61,006,985	55,351,134
Net Cost of Operations	(62,024,007)	(56,377,561)
Net Change	(1,017,022)	(1,026,427)
Cumulative Results of Operations	**4,764,660**	**5,781,682**
Unexpended Appropriations:		
Beginning balance	7,912,472	7,289,060
Beginning balance, as adjusted	7,912,472	7,289,060
Budgetary Financing Sources:		
Appropriations received	59,224,000	54,527,516
Other adjustments	(1,396,922)	(874,493)
Appropriations used	(58,873,362)	(53,029,611)
Total Budgetary Financing Sources	(1,046,284)	623,412
Total Unexpended Appropriations	**6,866,188**	**7,912,472**
Net Position	**$ 11,630,848**	**$ 13,694,154**

The accompanying notes are an integral part of these statements.

STATEMENT OF BUDGETARY RESOURCES

For the Years Ended September 30, 2008 and 2007 (in Dollars)

	2008	2007
Budgetary Resources (Note 10)		
Unobligated balance, brought forward, October 1	$ 2,828,858	$ 2,078,695
Recoveries of prior year obligations	793,729	1,352,281
Budget authority:		
Appropriations received	59,224,000	54,527,516
Earned		
Collected	2,985	211,860
Accounts receivable	–	10,277
Subtotal	59,226,985	54,749,653
Transfer in/out without reimbursement	–	(10,277)
Permanently not available	(1,396,922)	(874,493)
Total Budgetary Resources	**$ 61,452,650**	**$ 57,295,859**
Status of Budgetary Resources		
Obligations Incurred		
Direct	$ 59,491,212	$ 54,255,141
Reimbursable	–	211,860
Total Obligations Incurred	**59,491,212**	**54,467,001**
Unobligated balance		
Apportioned	426,366	220,350
Total Unobligated Balance	426,366	220,350
Unobligated balance not available	1,535,072	2,608,508
Total Status of Budgetary Resources	$ **61,452,650**	**$ 57,295,859**
Change in Obligated Balance		
Obligated balance, net		
Unpaid obligations, brought forward, October 1	$ 7,420,596	$ 7,521,417
Obligations incurred, net	59,491,212	54,467,001
Gross outlays	(57,475,890)	(53,215,541)
Recoveries of prior year unpaid obligations, actual	(793,729)	(1,352,281)
Obligated balance, net, end of period		
Unpaid obligations	8,642,189	7,420,596
Total, unpaid obligated balance, net, end of period	8,642,189	7,420,596
Net Outlays		
Gross outlays	57,475,890	53,215,541
Offsetting collections	(2,985)	(222,137)
Distributed offsetting collections	–	(215,677)
Net Outlays	**$ 57,472,905**	**$ 52,777,727**

The accompanying notes are an integral part of these statements.

STATEMENT OF CUSTODIAL ACTIVITY

For the Years Ended September 30, 2008 and 2007 (in Dollars)

	2008	2007
Revenue Activity:		
Sources of Cash Collections:		
Miscellaneous Receipts	$ 95,262	$ 215,677
Civil Penalties	2,428,750	4,135,632
Administrative Fees	58,496	393,669
Total Cash Collections	2,582,508	4,744,978
Accrual Adjustments	(276,843)	286,560
Total Custodial Revenue (Note 11)	**$ 2,305,665**	**$ 5,031,538**
Disposition of Collections:		
Transferred to Treasury	$ 2,582,508	$ 4,744,978
Increase/(decrease) in amounts to be transferred	(276,843)	286,560
Total Disposition of Collections	**2,305,665**	**5,031,538**
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 US. Government, a sovereign entity.

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, as appropriated by Congress. 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

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

FEC's accounts receivable represent amounts due from the public for fines and penalties assessed by FEC and referred to Treasury for collection. FEC establishes an allowance for the loss on accounts receivable from the public that are deemed uncollectible accounts, which is included in Accounts Receivable, net on the balance sheet. The allowance is a percentage of the overall receivable balance based on 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 other entities or persons 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 recorded by 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, 2008. Accrued payroll and benefits are payable to employees and are therefore not classified as intragovernmental.

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 leave accrued leave account is adjusted to reflect the 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 2008 and 2007, FEC recognized approximately $2,100,000 and $2,300,000, 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 are comparable to the U.S. Government's estimated service costs. For FERS covered employees, the FEC made contributions of 11.2 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 FEC is, in accordance with Statement of Federal Financial Accounting Standards (SFFAS) No. 5, Accounting for Liabilities of the Federal Government, included in FEC's financial statements as an imputed financing source.

Commitments and Contingencies

Commitments are contractual agreements involving financial obligations. 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 contingency 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

FEC received the majority of its funding through an annual appropriation as provided by Congress. Additionally, the FEC has authority 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 its 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

Net cost of operations is the difference between the FEC's expenditures and its earned revenue. The presentation of the statement is based on the FEC's strategic plan, which presents one program that is based on the FEC's mission and strategic goal. 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 fiscal year.

Net Position

Net position is the residual difference between asset and liabilities and comprises 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 assessed by the FEC. These amounts are not available for FEC operations, and accordingly, are reported as custodial revenue.

Use of Estimates

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

Note 2 – Non-Entity Assets

Non – entity assets, which primarily represent amounts due to the FEC for fines and penalties on those that violated the requirements of the *Federal Election Campaign Act*, consist of the following at September 30:

	2008	2007
With the Public:		
Accounts Receivable – Custodial	$ 530,187	$ 807,032
Accounts Receivable – Conference Fees	–	10,277
Total non-entity assets	530,187	817,309
Total entity assets	18,319,237	18,002,358
Total Assets	$ 18,849,424	$ 18,819,667

Note 3 – Fund Balance with Treasury

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

	2008	2007
Fund Balance with Treasury:		
Appropriated Funds	$ 10,603,627	$ 10,250,297
Total	$ 10,603,627	$ 10,250,297

Status of Fund Balance with Treasury	2008	2007
Unobligated Balance		
Available	$ 426,366	$ 220,350
Unavailable	1,535,072	2,608,508
Obligated Balance not yet Disbursed	8,642,189	7,421,439
Total	$ 10,603,627	$ 10,250,297

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:

2008	Gross Accounts Receivable	Allowance	Net Accounts Receivable
With the Public			
Penalties and Miscellaneous Receipts	$ 706,556	$ 176,369	$ 530,187
Total Non-Entity	$ 706,556	$ 176,369	$ 530,187

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

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 debtor's 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. A receivable pertaining to the fees associated with these conferences as of September 30, 2008 and 2007 was $0 and $10,277, respectively.

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, 2008 and 2007, respectively:

2008

Asset Class	Service Life (years)	Acquisition Value	Accumulated Depreciation	Net Book Value
Software	5	$ 15,937,663	$ 10,811,741	$ 5,125,922
Computers and peripherals	3 to 5	3,264,011	2,327,913	936,098
Furniture	7	852,754	725,573	127,181
Software-in-Development	n/a	1,525,511	–	1,525,511
Total		$ 21,579,939	$ 13,865,227	$ 7,714,712

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

Depreciation expense was $2,258,079 and $4,305,752 for the periods ending September 30, 2008 and 2007, respectively.

Note 6 – Liabilities Not Covered By Budgetary Resources

Liabilities Not Covered by Budgetary Resources consisted of the following as of September 30:

Liabilities Not Covered by Budgetary Resources	2008	2007
Intragovernmental		
Custodial Fines and Civil Penalties	$ 530,187	$ 807,032
Deferred Rent	783,538	–
Total Intragovernmental	1,313,725	807,032
With the Public:		
Unfunded Annual Leave	2,161,272	1,964,478
FECA Liability	2,712	663
Total Liabilities Not Covered by Budgetary Resources	$ 3,477,709	2,772,173
Total Liabilities Covered by Budgetary Resources	3,740,867	2,353,340
Total Liabilities	$ 7,218,576	$ 5,125,513

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 on the Balance Sheet" since the BS now classifies *FECA* liability as other.

Beginning FY 2008, the FEC entered into a new lease agreement for its headquarters that provided a rent abatement of $783,538, which covers the first two months of rent. Consistent with generally accepted accounting principles, the FEC has recorded rent abatement as deferred rent, which is amortized over the life of the lease of ten years.

Note 7 – Commitments and Contingencies

In the opinion of FEC management and legal counsel, the 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. Future payments due under the lease through September 30, 2018 are:

Future Operating Lease Payments

Fiscal Year	Lease Payment
2009	$ 5,705,136
2010	5,755,351
2011	5,818,278
2012	5,883,092
2013	5,949,852
2014 and thereafter	24,507,967
Total Future Lease Payments	$ 53,619,676

Note 9 – Statement of Net Cost

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

	FY 2008	FY 2007
Intragovernmental gross costs	$ 8,373,674	$ 6,810,914
Intragovernmental net costs	8,373,674	6,810,914
Gross costs with the public	53,650,333	49,788,784
Less: Earned revenues from the public	–	(222,137)
Net costs with the public	53,650,333	49,566,647
Net Cost of Operations	$ 62,024,007	56,377,561

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, 2008, budgetary resources were $61,452,650 and net outlays were $57,472,905. As of September 30, 2007, budgetary resources were $57,295,859 and net outlays were $52,777,727.

Apportionment Categories of Obligations Incurred

FEC receives apportionments of its resources from OMB. 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.

For FY 2008 and FY 2007, direct obligations incurred amounted to $59,491,212 and $54,255,141, respectively; and reimbursable obligations incurred amounted to $0 and $211,860, 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 2008 actual budgetary execution information is scheduled for publication in February 2009, 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 2007 SBR and the related President's Budget reflected the following:

FY 2007	Budgetary Resources	Obligations Incurred	Distributed Offsetting Receipts	Net Outlays
Statement of Budgetary Resources	$ 57,295,859	$ 54,467,001	–	$ 52,777,727
Budget of the U.S. Government	55,000,000	55,000,000	–	53,000,000
Difference	$ 2,295,859	$ 532,999	$ –	$ 222,273

The difference between the Combined Statement of Budgetary Resources and the *Budget of the U.S. Government* for budgetary resources is primarily due to expired unobligated balances. The differences for obligations incurred and net outlays are due to rounding.

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

The 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	**2008**	**2007**
Fines, Penalties, and Other Miscellaneous Revenue	$ 2,305,665	$ 5,031,538
Custodial Liability		
Receivable for Fines, Penalties and Other Miscellaneous Receipts	$ 706,556	$ 1,443,300
Less: Allowance for Doubtful Accounts	176,369	636,268
Total Custodial Liability	$ 530,187	$ 807,032

Note 12 – Undelivered Orders at the End of the Period

Undelivered orders at September 30, 2008 and 2007 totaled $4,901,323 and $5,077,159, respectively.

Note 13: Reconciliation of Net Cost of Operations to Budget

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.

	2008	2007
Resources Used to Finance Activities:		
Budgetary Resources Obligated		
Obligations incurred	$ 59,491,212	54,467,001
Less: Recoveries of prior year obligations	(793,729)	(1,352,281)
Obligations net of recoveries of prior year obligations	58,697,483	53,114,720
Less: Offsetting collections	(2,985)	(222,137)
Net Obligations	58,694,498	52,892,583
Other Resources		
Transfer in/out without reimbursement	–	(10,277)
Imputed financing from costs absorbed by others	2,133,623	2,331,800
Total resources used to finance activities	$ 60,828,121	$ 55,214,106
Resources Used to Finance Items not Part of the Net Cost of Operations		
Change in budgetary resources obligated for goods, services, and benefits ordered but not yet provided	(181,865)	(127,207)
Resources that fund expenses recognized in prior periods cost of operations	(2,424)	16,968
Resources that finance the acquisition of assets	$ 2,226,814	$ 3,295,311
Total resources used to finance items not part of the Net Cost of Operations	2,042,525	3,185,072
Total resources used to finance the net cost of operations	$ 58,785,596	$ 52,029,034
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	196,794	32,498
Increase in deferred rent	783,538	–
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	980,332	42,775
Components not Requiring or Generating Resources		
Depreciation and amortization	2,258,079	4,305,752
Total Components of the Net Cost of Operations that will not require or Generate Resources in the Current Period	3,238,411	4,348,527
Net Cost of Operations	$ 62,024,007	$ 56,377,561

SECTION IV
Other Accompanying Information

FEDERAL ELECTION COMMISSION
WASHINGTON, D.C. 20463

OFFICE OF THE INSPECTOR GENERAL

MEMORANDUM

TO: The Commission

FROM: Inspector General

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

DATE: November 7, 2008

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) 2008*.

The Inspector General has identified four areas for inclusion in the FEC's FY 2008 PAR:

Governance
Human Capital Management
Information Technology Security
Financial Reporting

The Inspector General identified three of these challenges in the 2005, 2006, and 2007 PARs and continues to believe the issues remain challenges for the FEC. This year the Inspector General has added governance to the list of challenges. Part of the reasoning for this is the turnover rate that has occurred in senior positions within the FEC.

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 November 17, 2008.

Lynne A. McFarland
Inspector General

Attachment

Cc: Joseph F. Stoltz, Acting Staff Director
Brian J. Duffy, Acting Chief Financial Officer
Alec Palmer, Chief Information Officer
James J. Wilson, Acting Deputy Staff Director
Management & Administration

Inspector General's Assessment of FY 2008
Management and Performance Challenges
Facing the Federal Election Commission

GOVERNANCE FRAMEWORK

The past three years has been a period of instability with respect to governance in the FEC. Specifically, there has been a lack of continuity in several key senior leadership positions of the agency. For example, there has been four different Staff Directors, two of which have been "acting" rather than permanently assigned. In addition, there have been four different Chief Financial Officers (CFOs), two of which were also in "acting" positions. The specially recruited[1] management team for Staff Director, Deputy Staff Director, Chief Compliance Officer and Chief Financial Officer resigned within a time period of six to twenty-four months. There has also been lack of continuity at other vital positions. For example, the head of the Administrative Division retired in 2007 and her replacement was employed at the FEC for only ten months. The current Office of Human Resources Director, in place only fifteen months, is currently detailed to the Deputy Staff Director for Management and Administration position, and therefore is currently serving in both positions. In addition, due to one vacancy and the expiration of several recess appointments in December 2007, the Commission operated with only two commissioners for six months in 2008, rather than the full six member Commission, and therefore lacked a quorum of at least four Commissioners. Further, Congress established six year term limits for Commissioners which will result in on-going, continual change in agency leadership. The lack of continuity in several key leadership positions, coupled with a progressive change in the Commissioners and their executive staff, has created an especially challenging operating environment for the agency.

As new Commissioners and senior leaders assume their roles, they may logically ask what information exists to describe the working relationships between the various business areas of the agency. An effective governance framework would be able to provide the FEC senior leadership and staff the answers to the following questions: What are the objectives of each business area? What are the key dependencies between the business areas? When/how do they monitor and report results? What are the risks that may prevent each area from contributing to the overall mission? How are those risks mitigated or controlled by management? What key controls exists to prevent fraud, waste and abuse? Where are the policies and procedures that drive day-to-day operations and how are staff informed of changes to policies? Are policies and procedures current? What Directives govern whole of organization activities? How does management know whether staff comply with FEC Directives? The governance framework would provide the above information not only to the Commission and senior leadership but to all staff and would define who, what, when, where, why and how of their daily work activities.

1 The FEC contracted with a firm that specializes in executive recruitment to assist in the recruitment, evaluation and selection of the senior leadership team described.

A revised agency-wide strategic plan was approved in early 2008. Prior to that, in July 2007, the Office of Human Resources implemented a new annual performance planning system, where staff performance plans would be linked to business area and organizational objectives. Both are core components of a governance framework, but they are not a complete framework. Currently, the agency lacks detailed business plans for the various offices. Instead, FEC offices rely on performance measures defined in the FEC strategic plan, with some offices having few, if any, specific goals defined in the strategic plan.

Business plans are the logical link between a strategic plan and employee performance plans in a governance framework. Business plans typically define, in detail, the objectives and goals of the business area and are clearly linked to the organizational strategic plan. In addition, business plans document risks and key dependencies that may prevent the office or program from reaching its goals; the resources required to meet objectives; stakeholders and relationships; service standards (both internal and external) and guidelines for operations; key performance indicators; and reporting methods. Progress reporting is typically done quarterly with the plan reviewed and updated at least annually. Both managers and staff then base their annual performance objectives on the business plan objectives and performance measures to ensure their work efforts contribute to the business area objectives. The performance plans also help ensure transparency and consistency in rating staff performance. Through OIG interviews with management of various business areas, however, it is noted that not all staff participate in the performance planning process. For some business areas, the implementation of the performance planning system, with mandatory semiannual and annual assessment, is limited to managers and supervisors. Also, while various business areas report statistical data such as information requests received, cases or audits in progress and completed, etc., the data is primarily a compilation of statistical volume rather than an assessment of the quality and effectiveness of service provided by each area.

If the FEC had a strong governance framework, the incremental whole of government compliance requirements routinely introduced by the Office of Management and Budget (OMB) and other federal agencies would not be a burden to the agency. Instead, the legal and regulatory requirements would largely be addressed through regular business planning or addressed through the governance framework. Currently, the FEC business processes are not adequately designed to withstand the planned and unplanned continual changes facing the agency. The OIG raised this concern with management after the OIG's 2007 Privacy Audit. During the mandatory privacy audit, the OIG recognized that the findings identified during the audit were actually symptoms of a larger issue facing the agency, a lack of a comprehensive governance framework. The OIG facilitated a presentation in early 2008 by the contract auditor to the then, two Commissioners of the FEC, where components of a governance framework and the steps necessary to implement such a framework at the FEC were explained. To date, the FEC has not taken the necessary steps to address improvements to the governance framework.

Continued regulation and reporting requirements imposed on federal agencies is not likely to decline or cease. The FEC needs to take action to address significant weaknesses in the governance framework within the agency. The OIG recommends a systematic approach to improving the governance framework of the agency through the creation of business plans for each FEC office that clearly links to the FEC strategic plan, but also includes the detail necessary to effectively manage and report business level activities. Business plans for all areas should be made available to all FEC staff to further illustrate the internal systems, processes and goals of the agency. The OIG further recommends the performance management system be fully implemented for all FEC staff and that each employee have a performance plan linked to their respective office's business plan. The implementation of these recommendations would provide the framework necessary to address the continuous evolution of the agency and the inevitable change in leadership caused by Commissioners' term expirations, separations and retirement of senior leaders.

HUMAN CAPTIAL MANAGEMENT

Like most federal agencies, the FEC continues to address the on-going challenge of effectively managing human capital in order to fulfill its mission. As noted in the previous management challenge on governance framework, recent and potential recurring high turn-over in senior leadership and a lack of framework to deal effectively with such turnover could directly impact the FEC's ability to achieve its goals. As such, the OIG retains human capital management as a challenge facing the FEC.

Over the last year, the FEC Office of Human Resources (OHR) developed a strategic plan to align human capital strategies with the agency mission, goals and objectives. While not yet finalized, the five year plan, originally intended to begin in 2008, is expected to be finalized within three months. Within the last year, OHR has made progress implementing several programs designed to address human capital management challenges facing the FEC. In order to recruit high-performing staff, OHR has implemented the Presidential Management Fellows (PMF) program and placed two members at the FEC. While the PMF program typically places staff with exceptional management potential at agencies for only a two-year rotation, the goal is to retain those individuals at the FEC by converting the PMFs to permanent FEC employees. In addition, OHR has implemented an employee recognition and awards program that is separate from the annual performance rating system. The program resulted in 31 awards presented to staff at the initial award ceremony held in September 2008 and 151 "on the spot" or other informal type awards presented to staff throughout the year. Another OHR initiative is the flexiplace (telecommuting) program, formerly in pilot since 2005, was formally approved for bargaining unit employees in June, 2008. The voluntary program allows staff to work from home or an alternate duty location in order to improve job satisfaction and productivity, employee family life and work-life balance, as well as allows the FEC to use resources more efficiently and effectively without decreasing the quality of service to the public, Congress or other entities that do business with the FEC. In order to achieve the full potential of the flexiplace program, inclusion of eligible non-bargaining unit employees is desirable. OHR intends to conduct an assessment in 2009 to determine whether the flexiplace program has achieved the intended results. In 2007, the OHR instituted a new employee performance management system for non-bargaining unit employees to link employee performance objectives to specific agency or business area goals. Now entering its second year, OHR should analyze and report on whether the program has been successfully implemented, needs refinement, or whether FEC staff require additional assistance in defining performance goals and assessing performance results for individuals.

In order to effectively address the human capital management challenges facing the FEC, it is vital that the OHR not only have a detailed plan to address those challenges, but that it executes the plan well. OHR and FEC management should not plan to assess the impact of programs as viewed through the Federal Human Capital Survey (FHCS) results or informal feedback mechanism. Rather, they must define and implement appropriate service delivery standards, quality assurance processes, monitoring, and reporting mechanisms as programs are planned and implemented. Further, programs that have been initiated should not be abandoned or revised without adequate assessment. In the 2007 Management Challenges section of the Performance and Accountability Report, the OIG noted the positive aspects of the quarterly Town Hall meetings and monthly management meetings aimed at improving collective communication throughout the Commission. The OIG stressed the need to place greater emphasis by consistently scheduling, conducting and monitoring of whether the objectives of the meetings were met. Since publishing the last report, only one Commission-wide Employee Town Hall meeting and six monthly management meetings have been held. OHR and senior leadership must support efforts to address human capital challenges by leading through example and demonstrating commitment to finalizing, implementing and monitoring the results of human capital initiatives.

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. 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. While the FEC has made progress in several areas, issues remain from previous years. There are still weaknesses in contingency planning. The FEC has developed a contingency plan; however this plan is not comprehensive and has yet to include steps for recovering all of the FEC's major applications and mission critical general support systems. The FEC has still not developed a Continuity of Operations Plan (COOP) to support the continuation of its core mission in the event of a disaster.

The FEC has taken important steps to establish and implement an effective information security program; however steps still need to be taken to ensure that the FEC has a complete and robust security program. Although the FEC has implemented the majority of its information security policies, it has not fully implemented all of the related procedures and standards. The FEC has still not established an alternate processing site for its operations in the event of a disaster.

The FEC awarded contracts to address several of the above issues. These contracts were to develop and implement an entity-wide security program plan, risk assessments, as part of the FEC's overall strategy to mitigate risks associated with its information technology environment were to be performed and the results of the assessments were to be incorporated into the FEC's security plans. A Business Impact Analysis was 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. It appears that some of these tasks were completed and others still need to be accomplished.

While the commitment of the FEC staff to improve IT security is vital, the OIG 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 FISMA and the NIST standards. We continue to believe this is a necessary and an important step for the FEC to take to ensure that the FEC's vital operations are safe and secure according to government standards.

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. The FEC did transition to an approved business provider this fiscal year. It is hoped that this transition will assist the FEC and will improve financial management.

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 five years, seven different individuals have held the CFO positions. The FEC has been fortunate that that the Accounting Officer, who is now the acting CFO, and his immediate staff have been able to provide stability during the past several fiscal years and in the past, experienced FEC employees were acting CFOs during transition periods. Last year it was noted that the FEC hired a permanent CFO who had years of experience in financial management and the production of audited financial statements. Unfortunately, this person has resigned. Even though she has remained on staff to assist with the audit, the IG has concerns with the amount of turnover in this vital position. It is very difficult to address the recommendations that have been made over the years in the various financial statement audits with no stable CFO to direct and oversee the changes that need to be made. The IG also believes that part of the reason the audit of financial statements has remained a challenge to the FEC is the lack of continuity in the CFO position. Unfortunately, the FEC is starting another fiscal year with an acting CFO. Still, without a permanent CFO to guide and direct the necessary changes, the FEC is liable to find it difficult to make the progress that is needed to address the recommendations raised over the course of the past five financial statement audits.

APPENDIX A
List of Acronyms

ADR	Alternative Dispute Resolution
AF	Administrative Fine
AICPA	American Institute of Certified Public Accountants
AO	Advisory Opinion
ATDA	Accountability of Tax Dollars Act
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

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