Federal Election Commission

Performance and Accountability Report

(Reports Consolidation Act of 2000)

Fiscal Year 2010

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CONTENTS

(cont.)

FEDERAL ELECTION COMMISSION
WASHINGTON, D.C. 20463

Message From The Chairman

November 12, 2010

I am pleased to present the Federal Election Commission's (FEC) *Performance and Accountability Report* (PAR) for Fiscal Year (FY) 2010. The PAR 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 of 1971*, as amended (the Act).

The Commission received an unqualified opinion from its independent auditors with respect to the agency's FY 2010 annual financial statements. This unqualified opinion reflects the continued commitment by the Commissioners and the FEC staff to ensure that the FEC's financial statements present fairly the agency's fiscal position.

In FY 2010, the FEC focused on ensuring that resources were in place to effectively administer and enforce the Act during the 2010 federal election cycle. At the same time, the FEC responded to a number of important court cases impacting the work of the FEC. In January 2010, the Supreme Court issued its opinion in *Citizens United* v. *FEC*, in which the Court struck down the Act's prohibitions on corporate funding of independent expenditures and electioneering communications as unconstitutional, while upholding the reporting requirements for these disbursements.

In addition, the U.S. Court of Appeals for the D.C. Circuit handed down two significant campaign finance decisions. In *SpeechNow.org* v. *FEC*, the court held that the Act's contribution limits could not be constitutionally applied to a group that is devoted to running independent advertisements for and against candidates and makes no direct contributions to candidates. In *EMILY's List* v. *FEC*, which was issued in the final weeks of FY 2009, the court vacated certain Commission regulations governing 1) the financing of various types of activities and public communications by non-connected committees and 2) the treatment of funds received in response to certain solicitations as contributions. The court held that these regulations both violated the First Amendment and were contrary to the Act.

The Commission also finalized a number of significant rules during FY 2010, including 1) implementation of the statutory provision in the *Honest Leadership and Open Government Act* concerning political travel; 2) final action on three rulemakings pertaining to coordinated communications, federal candidate involvement in non-federal fundraisers, and the definition of "federal election activity" to comply with the decision of the U.S. Court of Appeals for the D.C. Circuit in *Shays* v. *FEC*; 3) effectuation of the decision of the U.S. Court of Appeals for the D.C. Circuit in *EMILY's List* v. *FEC*; and 4) completion of all phases of a rulemaking to implement the *Debt Collection Improvement Act of 1996*.

In furtherance of its public disclosure responsibilities, the Commission continued to develop user-friendly online tools for searching and sorting campaign finance data. For instance, the Commission developed a database detailing campaign spending in each Congressional District. Furthermore, the Commission initiated a project that makes information regarding independent expenditures and electioneering communications available for public inspection on a virtually real-time basis. These efforts provide the electorate with valuable information to assist them in their efforts to make fully informed decisions in the political marketplace.

Finally, in FY 2010, the FEC continued to improve its information technology infrastructure by moving forward on its efforts towards virtualization, Enterprise Content Management, and data warehousing. The Commission also took steps to make audits electronically available and searchable on the FEC website, provide public access to relevant directives, and digitize the Commission's cassette tape archives.

The Commission looks forward to building on its FY 2010 achievements in order to fulfill the mission of the agency in the most efficient manner possible.

On behalf of the Commission,

Matthew S. Petersen

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, 2009, through September 30, 2010.

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 the FEC's website at http:www.fec.gov. To access this report, click on “About the FEC” and then “Budget”.

The *FY 2010 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 1) highlighting the agency’s financial position and audit results and 2) 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 federal campaign finance process under the *Federal Election Campaign Act of 1971*, as amended ("FECA" or "the Act"). The Commission is also responsible for administering the public funding program for Presidential campaigns and nominating conventions under the *Presidential Election Campaign Fund Act* and the *Presidential Primary Matching Payment Account Act*.

The Act reflects Congress's efforts to ensure that voters are fully informed about the sources of candidates' financial support. Public confidence in the political process depends not only on laws and regulations to ensure transparency, but also on the knowledge that those who disregard the campaign finance laws will face consequences.

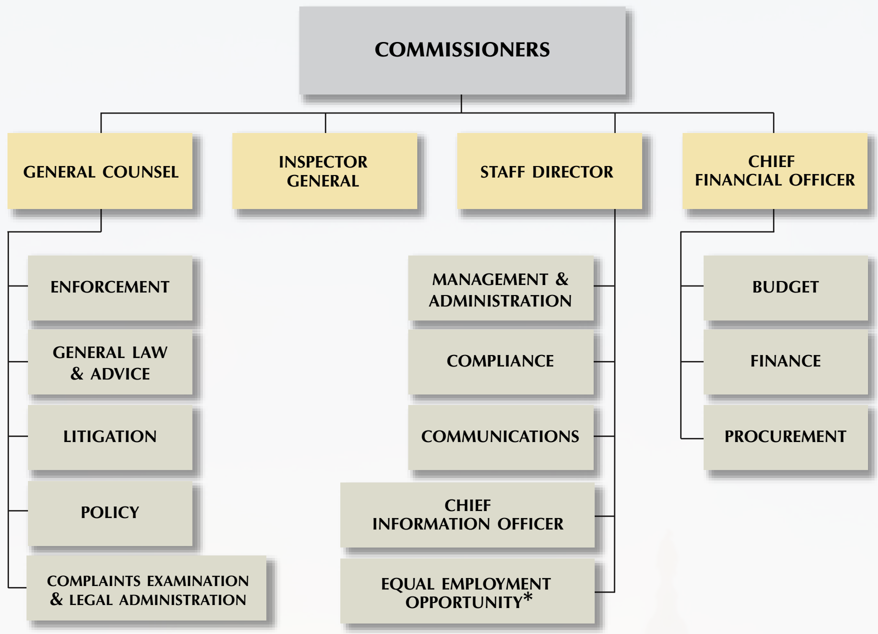
The primary objectives of the FEC are 1) to facilitate transparency through public disclosure of campaign finance activity, 2) to encourage voluntary compliance with the Act by providing information and policy guidance to the public, media, political committees and election officials on the FECA and Commission regulations and enforcing the statute through audits, investigations and civil litigation and 3) to develop the law by administering and interpreting the FECA as well as the *Presidential Election Campaign Fund Act* and the *Presidential Primary Matching Payment Account Act*.

How the FEC is Organized

Organization

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 Chair more than once during his or her term. The Commissioners meet regularly to formulate policy and to vote on significant legal and administrative matters. The Act requires at least four votes for the Commission to adopt any official action or policy, thus requiring bipartisan decision-making. The FEC has its headquarters in Washington, D.C., and does not have any regional offices.

Figure 1 – FEC Organizational Chart



* The Director for Equal Employment Opportunity reports to the Staff Director on administrative issues but has direct reporting authority to the Commission on all EEO matters.

The Offices of the Staff Director, General Counsel and Chief Financial Officer 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/offices/offices.shtml.

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. The public campaign finance reports are accessible through the FEC's website at http://www.fec.gov/disclosure.shtml. By making disclosure reports available online immediately after they are filed, the FEC provides the public with up-to-date information about the financing of federal elections and political committees' compliance with 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 Analysis Division (RAD) reviews all filed statements and financial reports to track compliance with the law and to ensure that the public record provides a full and accurate representation of campaign finance activity. Analysts provide frequent telephone assistance to committee officials who have reporting questions or compliance problems.

If RAD identifies an error, omission, need for additional clarification or possible prohibited activity, a request for additional information (RFAI) is sent 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 address the FEC's concerns sufficiently, the FEC may initiate an audit or begin an enforcement action to remedy the apparent violation.

Encouraging Compliance through Education

Helping the regulated community understand its obligations under federal campaign finance laws 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 one of the most important sources of instantly accessible information about the Act, Commission regulations and Commission proceedings. Members of the regulated community and the general public can use the website to track Commission rulemakings; search advisory opinions, completed audits and closed enforcement matters; view campaign finance data and find reporting dates. The latest additions to the educational materials available on the website include a "Recent Developments" web page that provides one-stop shopping for information about changes in campaign finance law, enhanced and expanded instructional videos available through the site's E-Learning center, and a new "Compliance Map" that provides easy access to state-by-state information detailing filing deadlines and the timeframes for certain pre-election obligations under the Act.

The Commission also encourages voluntary compliance through outreach programs. The FEC hosts instructional conferences in Washington, D.C., and in other cities across the country, where Commissioners and staff explain how to comply with the Act to candidates and political committees. These conferences specifically address recent changes in the campaign finance laws and focus on fundraising and reporting regulations. Additionally, Commission staff meets with political committees upon request and responds to telephone inquiries and written requests from those seeking information about the law and assistance in filing disclosure reports.

Enforcing the FECA

In fulfilling its statutory mission, the Commission must often perform a delicate balancing act. On the one hand, the Commission must administer, interpret and enforce the FECA, which was intended to serve a compelling governmental interest. On the other hand, the Commission must remain mindful of the constitutional freedoms of speech and association, and the practical implication of its actions.

The FEC has exclusive jurisdiction over civil enforcement of federal campaign finance laws and coordinates with the U.S. Department of Justice, as appropriate, on matters involving both civil and criminal enforcement of the Act. Commission enforcement actions, which are handled primarily by the Office of General Counsel (OGC), originate from a number of sources, including external complaints, referrals from other government agencies and internal referrals from the Audit or Reports Analysis Divisions.

To augment OGC's traditional enforcement role, the Office of Compliance manages several programs that seek to remedy alleged violations of the Act and encourage voluntary compliance. These programs include: 1) the Alternative Dispute Resolution Program, 2) the Administrative Fine Program and 3) the Audit Division. The Commission's Alternative Dispute Resolution Program is designed to resolve matters more swiftly by encouraging the settlement of less-complex enforcement matters via a streamlined process that focuses on remedial measures for candidates and political committees, such as training, internal audits, and hiring compliance staff. Violations involving the late submission of, or failure to file, disclosure reports are subject to the Administrative Fine Program. This Program is administered by the Office of Compliance's Office of Administrative Review (OAR) and RAD, which assess monetary penalties and handle challenges to the penalty assessments. Finally, the Audit Division conducts mandatory audits under the public funding statutes and performs "for cause" audits under the FECA in those cases where political committees have failed to meet the threshold requirements for demonstrating substantial compliance with the Act.

If the Commission cannot settle or conciliate a matter involving an alleged violation of the Act, the Commission may initiate civil litigation, and will file and prosecute a civil action in federal district court to address the alleged violation. 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.

Interpreting and Developing the Law

The Commission responds to questions from the regulated community about how the Act applies to specific situations by issuing advisory opinions (AOs). In addition, Commission initiatives, 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

The Commission's responsibilities also include administering the public funding of Presidential elections, as provided in the *Presidential Primary Matching Account Act* and the *Presidential Election Campaign Act*. 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 their general election campaigns.

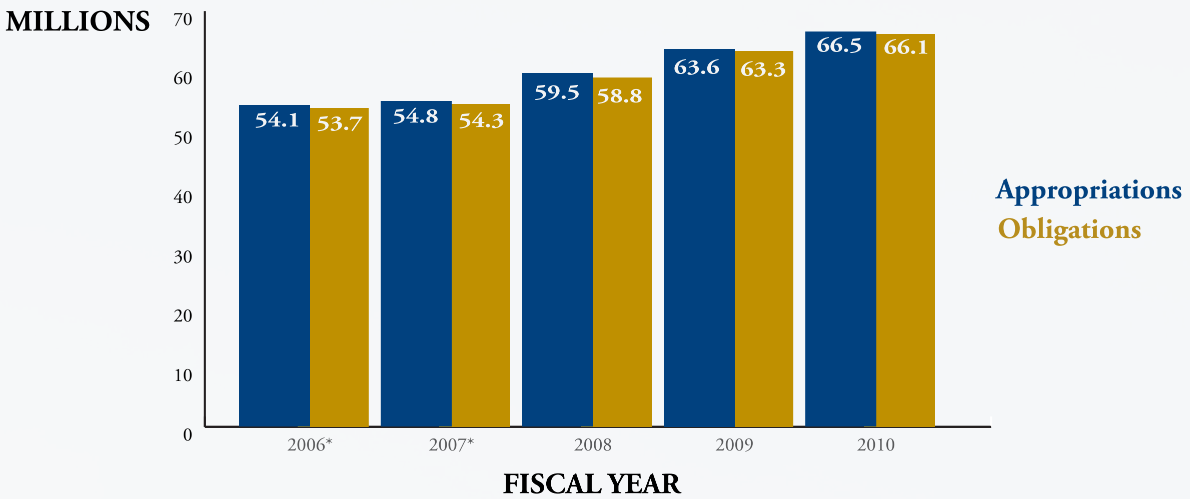
Under the Presidential public funding program, the Commission 1) determines a candidate's eligibility to participate in the program, 2) certifies the amount of public funds to which the candidate or convention committee is entitled and 3) conducts a thorough examination and audit of the qualified campaign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

Sources of Funds

The FEC receives a single, annual appropriation for Salaries and Expenses. In FY 2010, the FEC's authorized funding level included an appropriation of $66.5 million. The FEC also has the authority to collect fees from attendees of agency-sponsored educational conferences. The Commission uses those fees to defray the costs of conducting those conferences. In an effort to keep the fees as low as possible, the agency has not fully exercised that authority. Rather, the Commission sets its registration fees at a level that covers only the costs incurred by the agency's conference-management contractor, including meeting room rental and conference meals and compensation. All other conference-related expenses, such as materials and staff travel, are paid using appropriated funds. Registration fees for FY 2010 were $280,474.

Figure 2 shows the agency's appropriations and obligations from FY 2006 to 2010.

FIGURE 2 – SUMMARY OF FUNDING

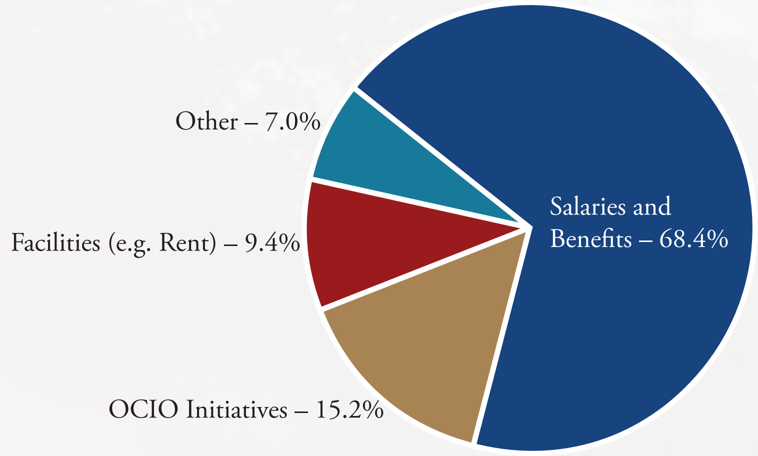


* FY 2006 and 2007 numbers include conference registration fees.

Personnel vs. Non-Personnel Costs

Figure 3 represents the Commission's FY 2010 obligations by personnel and non-personnel costs. Personnel costs comprised 68 percent of the FEC's costs; the remaining 32 percent was spent primarily on infrastructure and support, including software and hardware, office rent, building security and other related costs.

FIGURE 3 – FISCAL YEAR 2010 BY MAJOR CATEGORY



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

Summary of Significant Performance Results

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

FY 2010 represented the FEC's third year under its current strategic plan. 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, it established the following three objectives:

- **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 strategic plan also incorporates the Commission's support functions, which underpin its ability to pursue its mission. These functions strive to ensure the agency's strategic goal and objectives are met in the most efficient and effective manner.

The following table provides a summary of the Commission's actual FY 2008, FY 2009 and FY 2010 results of its performance measures, along with the targets set by the strategic plan.

	PERFORMANCE MEASURE	Target	FY 2008 Actual	FY 2009 Actual	FY 2010 Actual
	Strategic Objective A: TRANSPARENCY				
1.	Process reports within 30 days of receipt as measured quarterly	95%	91%	78%	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%	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%	100%	100%
4.	Issue press releases summarizing completed compliance matters within two weeks of a matter being made public by the Commission	100%	22%	63%	98%
5.	Issue press releases containing summaries of campaign finance data quarterly	100%	100%	75%	75%
6.	Process enforcement cases within an average of 15 months of receipt	100%	66%	76%	75%
7.	Process cases assigned to Alternative Dispute Resolution within 155 days of a case being assigned	75%	64%	26%	64%

	PERFORMANCE MEASURE	Target	FY 2008 Actual	FY 2009 Actual	FY 2010 Actual
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%	84%	100%
9.	Process the challenges in the Administrative Fine Program within 60 days of a challenge being filed	75%	14%	60%	100%
10.	Conclude non-Presidential audits with findings in an average of ten months, excluding time delays beyond the Commission's control, such as subpoenas and extension requests	100%	95%	12%	60%
11.	Conclude non-Presidential audits with no findings in an average of 90 days from beginning of fieldwork	100%	100%	0%	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%	N/A	100%	100%
	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%	50%	83%	50%
14.	Issue all advisory opinions within 60-day and 20-day statutory deadlines	100%	97%	100%	100%
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%	100%	N/A
16.	Ensure that court filings meet all deadlines and rules imposed by the Courts	100%	100%	100%	100%
17.	Process public funding payments in the correct amounts and within established time frames	100%	100%	100%	N/A

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* in greater detail.

Highlights of Performance Measures

In FY 2010, the Commission focused significant attention on ensuring that it provides the public with the most up-to-date and accessible campaign finance information, that it provides comprehensive educational outreach to the public and the regulated community and that Commission procedures are fair, efficient and transparent. The agency's commitment to providing timely guidance and accurate information has been especially important in FY 2010 in light of a series of recent court decisions. On January 21, 2010, the United States Supreme Court issued its decision in *Citizens United* v. *FEC*, which struck down the Act's prohibitions on using corporate funds to finance independent expenditures or electioneering communications. The Court reasoned that the funding restrictions could not be justified by the government's interest in preventing corruption and, therefore, were unconstitutional.

In addition, two decisions of the U.S. Court of Appeals for the D.C. Circuit have further altered the state of the law and affected the work of the Commission in FY 2010: In September 2009, the D.C. Circuit issued its decision in *EMILY's List* v. *FEC*, which concerned sources of funding for various types of activities and public communications by non-connected committees, and the treatment as contributions of funds received in response to solicitations. In March 2010, the D.C. Circuit issued its decision in *SpeechNow.org* v. *FEC*, which concerned whether certain FECA provisions were constitutional as applied to a group that runs independent advertisements for and against candidates and makes no contributions to candidates.

Although these court decisions make sweeping changes to alter the previous rules governing political committees and increase the ability of outside organizations to engage in independent political speech, *Citizens United* and *SpeechNow* also upheld the existing disclosure requirements for political spending. The agency continues to provide the public with data concerning where candidates for federal office derive their financial support. With its state-of-the-art disclosure program, the agency again succeeded in FY 2010 in making 100 percent of the reports and statements it received on paper available to the public within 48 hours of receipt by the Commission, while electronic filings were made available nearly instantaneously.

As part of its statutory mandate, the FEC strives to make its campaign finance information available to the public in more robust and interactive formats on the FEC website. Anticipating increased public interest following the *Citizens United* decision in the disclosure of spending on independent expenditures and electioneering communications, the Commission recently initiated a project to make information about independent expenditures and electioneering communications available in nearly real-time as the information is received during the 2010 election cycle. Over the course of the year, the Commission has also expanded the use of searchable, sortable and downloadable data technologies to provide information to the public through its data catalog. Now, for the first time, the agency can provide in database form detailed information about spending by Congressional campaigns.

In each of these efforts, the Commission has maintained its commitment to providing accessible and user-friendly information to the public. Agency staff is currently working to revise standard disclosure pages to make better use of plain language and simplify navigation, and the FEC has implemented a "blog" to explain the new information and receive and respond to comments, questions and suggestions from users in a format that encourages an open dialog.

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 election cycle are received at the Commission on a daily basis. The Commission reviewed 50,056 documents out of 51,103 documents filed within FY 2010, and is well on its way to complete 100 percent of the documents received.

The Commission continues to place a significant emphasis on the FEC's ability to process compliance matters in a timely manner and with more substantive resolution. A key factor in helping the Commission achieve its target relates to the Administrative Fine and ADR Programs' handling of the less-complex cases, which not only improves the timeliness of addressing such cases but also reduces incidence of noncompliance by encouraging voluntary compliance. Indeed, as detailed later in this report, the success of the Administrative Fine Program in reducing instances of late and non-filed reports allowed the agency to reallocate staff this year from that office to the Reports Analysis Division.

As with the improvements made to the disclosure program, many improvements made to the review and compliance programs center on increasing the transparency and accessibility of the process.

For example, the Commission launched a pilot program in July 2010 to allow committees to have legal questions considered by the Commission earlier in the review and audit processes, and in October 2010 the Commission launched a searchable audit database to allow users to search audit reports in the same way that they can search for advisory opinions on the Commission's website, http://www.fec.gov/audits/audit_reports.shtml.

The Commission has also taken steps in the past year to augment its educational outreach programs to provide more cost-effective training to the regulated community. For example, the Commission has launched a YouTube channel and E-Learning page to allow the public and the regulated community the convenience of participating in trainings without the costs of travel. This year the agency also initiated a program to provide live, interactive webinars to provide additional distance learning to the public.

In addition, in anticipation of the increased need for training in the coming year as new regulations take effect for the 2012 election cycle, the Commission has revised and expanded its already successful conference and seminar program. The FEC increased its conference schedule to include six conferences in FY 2010, with events held in Washington, D.C., and in cities across the country. Each conference again received an overall evaluation score exceeding 4.0 on a 5.0 scale. For FY 2011, the Commission plans to tailor its outreach to provide the most cost-effective programs for participants. In addition to hosting a regional multi-day conference, the agency will replace its usual schedule of multi-day conferences in Washington, D.C., with a series of low-cost seminars and roundtables to be held at FEC Headquarters. Each full-day seminar or half-day roundtable will focus on a specific group or legal issue, allowing participants to choose only the programs most relevant to them at a fraction of the cost of a full conference. The new program will also allow the Commission to be more responsive to the demand for outreach and provide new trainings as new rules take effect.

Section 1.C: Analysis Of FEC Financial Statements And Stewardship Information

The FEC's FY 2010 financial statements and notes are presented in the required format in accordance with OMB Circular A-136, as 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 2010:

Net Financial Condition	FY 2010	FY 2009	Increase/ (Decrease)	% Change
Assets	$17,559,053	$17,661,603	($102,550)	-0.6%
Liabilities	$7,723,040	$7,186,588	$536,452	7.5%
Net Position	$9,836,013	$10,475,015	($639,002)	-6.1%
Net Cost	$69,768,762	$66,826,731	$2,942,031	4.4%
Budgetary Resources	$68,690,110	$65,792,156	$2,897,954	4.4%
Custodial Revenue	$1,023,494	$1,383,882	($360,388)	-26.0%

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

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, all of the FEC's assets consist of Fund Balance with Treasury (FBWT), Property and Equipment (P&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 $2,011,000, or 18 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, as deemed appropriate. In compliance with the *Debt Collection Improvement Act of 1996 (*DCIA), the OCFO takes into consideration the most appropriate approach to debt management. These amounts are not available for FEC operations and are sent to the U.S. Treasury as miscellaneous receipts. The accounts receivable balance decreased by approximately $189,000, or 92 percent, from FY 2009.

In 2010, the FEC issued Final Rules to implement the DCIA.

Statement of Net Cost

The Statement of Net Cost presents the annual cost of operating the FEC program. Gross costs are used to arrive at the total net cost of operations. The FEC's total appropriation in FY 2010 was $66.5 million, approximately $2.9 million higher than in FY 2009. Roughly $45 million, or 68 percent, of the budget was dedicated to personnel costs. Overall, net costs increased by approximately $2.9 million or 4.4 percent from FY 2009. The increase of approximately $1.3 million is attributable to the personnel cost for the cost of living adjustment (COLA). The imputed costs increased by approximately $729,000 from FY 2009. The remaining increase of approximately $853,000 is attributable to other costs of operations, including OCIO contracts, training, the annual rent adjustment and costs for services provided by other federal agencies.

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 approximately $639,000 or 6 percent, which is the result of depreciation, amortization, and impairment expenses that are offset by acquisition of assets and the change in unexpended appropriations.

Statement of Budgetary Resources

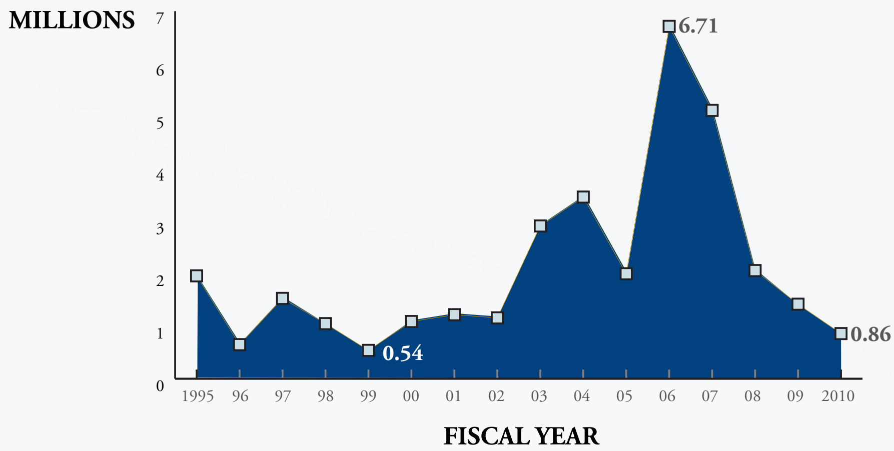
The Statement of Budgetary Resources provides information on the source and status of budgetary resources made available to the FEC during the reporting period. It presents the relationship between budget authority and budget outlays, as well as the reconciliation of obligations to total outlays. Total Budgetary Resources and Status of Budgetary Resources increased by approximately $2.9 million, or 4 percent, over FY 2009. This increase primarily is derived from an increase in appropriations received.

Statement of Custodial Activity

The Statement of Custodial Activity (SCA) represents an accounting of revenue and 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. Collection and revenue activity primarily result from enforcement actions that come before the Commission during the fiscal year. Revenue and collections on the SCA consist of collections on new assessments, prior year(s) receivables, and Miscellaneous Receipts. In FY 2010, the total custodial revenue and collections decreased by approximately $360,000 or 26 percent from FY 2009.

The chart below displays the assessment history for the past 16 years.

FIGURE 4 – FINES ASSESSED, BY FISCAL YEAR



Section 1.D: Analysis Of FEC's Systems, Controls And Legal Compliance

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

The Commission is subject to numerous legislative and regulatory requirements that promote and support effective internal controls. Such laws and regulations the FEC complies with, as applicable, include:

- Annual Appropriation Law – establishes the FEC's budget authority;
- *Inspector General Act of 1978*, as amended;
- *Government Performance and Results Act of 1993*;
- *Federal Financial Management Improvement Act of 1996*;
- *Clinger-Cohen Act of 1996*;
- *Debt Collection Improvement Act of 1996*, as amended; and
- *Chief Financial Officers 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.

1.D.ii – 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* and OMB Circular A-127, *Financial Management Systems*. The FEC management is responsible for establishing and maintaining effective internal control and financial management systems that meet the objectives of the FMFIA and for 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 their internal and administrative controls. The reviews that took place during FY 2010 provide unqualified assurance that FEC systems and management controls comply with the requirements of the FMFIA.

Section 4 of the FMFIA requires that agencies annually provide assurance on programmatic internal controls and financial management systems, and effectiveness of internal control over financial reporting. The FEC evaluated its financial management systems in accordance with the FMFIA and OMB Circular A-127, as applicable. The results of management reviews provide unqualified assurance under Section 4 of the FMFIA that the FEC's financial systems controls generally conform to the principles and standards required.

Prompt Payment Act

The *Prompt Payment Act* (PPA) 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 2010 was effectively 100 percent, with less than 0.01 percent of all invoices paid after the date required by the PPA.

Improper Payments

The *Improper Payments Information Act of 2002* (IPIA), the *Improper Payments Elimination and Recovery Act of 2010* (IPERA) and OMB guidance require agencies to identify those programs that are susceptible to significant erroneous payments, and determine an annual estimated amount of erroneous payments made in their 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 2010 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.

FEDERAL ELECTION COMMISSION
WASHINGTON, D.C. 20463

OFFICE OF THE CHAIRMAN

Annual Assurance Statement on Internal Control

The Federal Election Commission (FEC) is responsible for establishing and maintaining effective internal control and financial management systems that meet the objectives of the *Federal Managers' Financial Integrity Act of 1982 (FMFIA)*, as implemented by OMB Circular A-123, revised, *Management's Responsibility for Internal Control*. Internal control is an integral component of management to provide reasonable assurance that (1) programs operate effectively and efficiently, (2) financial reports are reliable, and (3) programs comply with applicable laws and regulations.

The FEC conducted its evaluation of internal control with applicable laws and regulations in accordance with OMB Circular A-123. Based on the results of the Fiscal Year 2010 internal control review, the FEC reports no material weaknesses under the FMFIA and is able to provide an unqualified statement of assurance that the internal control and financial management systems meet the objectives of FMFIA.

Matthew S. Petersen
Chairman
October 22, 2010

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

The Inspector General's report in Section IV identified three areas specific to management and performance challenges, which were also identified last year: 1) Governance, 2) Human Capital Management and 3) Information Technology Security.

Governance

The Commission agrees with the Inspector General that the agency has continued to face challenges in retaining key leadership and management positions this year. The Commission is committed to improving its governance framework. In FY 2010, the Commission hired a new Director of Human Resources and completed the interview process to fill the Deputy Staff Director for Management and Administration position.

Human Capital Management

The FEC is continuing to improve its working environment. The new director of Human Resources is working to fill key staff positions within the office. Recent organizational restructuring has provided more and better career paths for FEC staff. The FEC continues to support the employee awards program that recognizes employees both formally and informally. The Commission also offers alternative work schedules, compressed work schedules and the Flexiplace Program (the FEC's telework program), which allow its employees to meet their obligation to the agency while providing increased flexibility in work schedules.

The FEC continues to strive for employee engagement and satisfaction. In the 2010 Federal Employee Viewpoint Survey, the FEC attained an increase in positive employee responses to the following survey statements: 1) performance appraisals are accurate reflections of performance, 2) creativity and innovation are rewarded and 3) supervisors support employees' need to balance work and other life issues.

The establishment of a regular training calendar and the implementation of a leadership development pilot program are helping the FEC close the gaps in its leadership competencies. The FEC has also formed an Internal Coaching Alliance with other small agencies to offer certified coaching to its managers and high-potential employees.

Information Technology Security

In July 2007, the agency implemented a security review policy that contains the basic elements of a continuous monitoring program, and in FY 2010 the agency completed the expansion of its security review policy into a more comprehensive continuous monitoring program. The agency has 30 IT Security policies in effect. In FY 2010, three new policies were approved, and the remaining 27 were reviewed for compliance. The agency has also made significant progress in establishing a continuity of operations plan (COOP). The FEC chose to develop and implement a multi-phase COOP over a period of three years during which the agency can address funding issues and meet the education and training needs of the entire agency workforce on COOP activities. Over the course of the last three years, the agency has completed the first two phases of the program, and will complete the third and final phase of the COOP in November 2010. The FEC has also implemented a new agency-wide FEC System Access application (FSA) to improve access controls by automating the process of tracking staff and contractors from the beginning to the end of their FEC employment. In sum, the level of security provided by the FEC IT Security Program is within the guidance provided by applicable federal standards, including the exemption of the agency from FISMA and National Institute of Standards and Technology standards.

Section 1.E: Possible Future Effects Of Existing Events And Conditions

Several existing events and conditions may affect the FEC in the future. The 2010 federal elections already have shown a continuation of increasing levels of campaign finance activity. The Commission projects that the total amount disbursed for the 2010 election cycle will be approximately $6.5 billion, which is a 58 percent increase over 2006, the last midterm election cycle. As the agency completes its review, audit and enforcement duties with regard to this election, we expect that the level of activity reported to the FEC may necessitate a greater commitment of staff time and resources than what was needed for past election cycles.

Some of the increased levels of campaign finance activity may be due to recent court decisions, which could also significantly impact the FEC in the coming year. As detailed in Section 2.C., the decisions affect core aspects of the campaign finance law and could increase the scope and volume of campaign finance disclosure. The complete effects of the decisions may not be apparent for some time.

Section 1.F: Other Management Information, Initiatives And Issues

Website Improvement

The Commission places a high priority on ensuring the effective use of technology and internal procedures to optimize its communication with the public. The Commission has made significant progress in its ongoing effort to make the most effective use of technology in conducting its public disclosure efforts. During FY 2010, the Commission expanded the use of searchable, sortable and downloadable data technologies to provide information to the public through its data catalog. Examples include the first detailed information about spending by Congressional campaigns ever provided in database form by the FEC. The Commission also initiated a project to make comprehensive information about independent expenditures and electioneering communications available in nearly real-time as the information is received during the 2010 election cycle. The FEC also expanded its outreach and collaborative efforts by implementing a “blog” to explain the new information and receive comments, questions and suggestions from users in a format that encourages an open dialog. Other projects underway include revisions to standard disclosure pages to make better use of plain language and simplify navigation within fec.gov and also to use analytic tools to better understand user experiences which will lead to further improvements.

Enterprise Content Management System

The FEC has launched an Enterprise Content Management (ECM) system initiative to provide tools and strategies to capture, manage, store, preserve and deliver agency-wide content. Under the ECM initiative, the FEC will design a system to store, search and retrieve documents that will be available to all appropriate Commission staff. The system will encourage collaboration throughout the agency by managing and documenting changes and ensuring the security of materials as they move through various Commission offices.

Data Warehouse

In FY 2009, the FEC conducted a study to determine the best approach for housing and accessing FEC data. As a result of that study, the FEC has moved forward in implementing a comprehensive Data Warehouse System, which will provide an infrastructure to store the increasingly large volume of information the Commission receives in the most efficient way possible. This will permit the Commission to provide fast, flexible and comprehensive disclosure of campaign finance information to the public, while integrating that information with materials from FEC policy actions, including report review, advisory opinions, audits and enforcement actions. This Data Warehouse System will provide the public and the regulated community with timely and robust campaign finance information and greatly improve the public's ability to access campaign finance data. This project has been divided into five phases to be implemented over a number of years. In FY 2010, the Commission completed phases one and two of the data warehouse prototype initiative.

Audit Finding Search System

The Commission launched an Audit Finding Search System on October 1, 2010. This system allows users (both external and internal) the ability to search all approved audit reports using a two-level listing of categories, as well as by other criteria. The results list each audit containing the selected search criteria, list each finding in the selected audit reports and provide a link to the audit report on the Commission's website. This system currently contains reports for non-publicly financed committees dating back to the 1990 election cycle. Once fully implemented, all audit reports will be searchable. The Audit Finding Search System will greatly enhance the ability of both agency staff and the public to research past audit reports.

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*.

Strategic Goal And Objectives For FY 2010

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

In FY 2008 the Commission reviewed its performance measures and refined them in the agency's five-year Strategic Plan, thereby enhancing the FEC's ability to capture and report data in a more meaningful manner. The following provides a detailed discussion of the FEC's performance measures, as outlined in its 2008-2013 Strategic Plan.

17

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.

Public Disclosure

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

Performance Measures

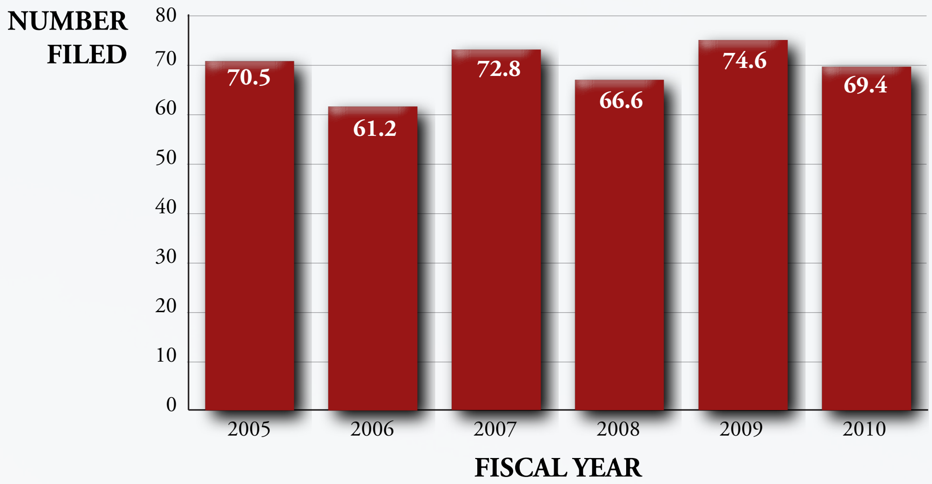
- Process reports within 30 days of receipt as measured quarterly; and
- Meet the statutory requirement to make reports and statements filed on paper with the FEC available to the public within 48 hours of receipt.

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. Under the Act, these mandatory e-filing provisions apply to any political committee or other person required to file reports, statements or designations with the FEC, except for Senate candidate committees (and other persons who support Senate candidates only).

The e-filing system acts 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 of receipt, both electronically on the website and at the FEC's offices in Washington, D.C.

Figure 5 shows the total number of campaign finance reports and statements filed with the FEC each fiscal year since 2005. Because elections occur in November, the associated spike in the number of filings received by the FEC is reflected in the odd-numbered fiscal years. The public can access the campaign finance reports and data at http://www.fec.gov/disclosure.shtml.

FIGURE 5 – REPORTS AND STATEMENTS FILED (IN THOUSANDS)



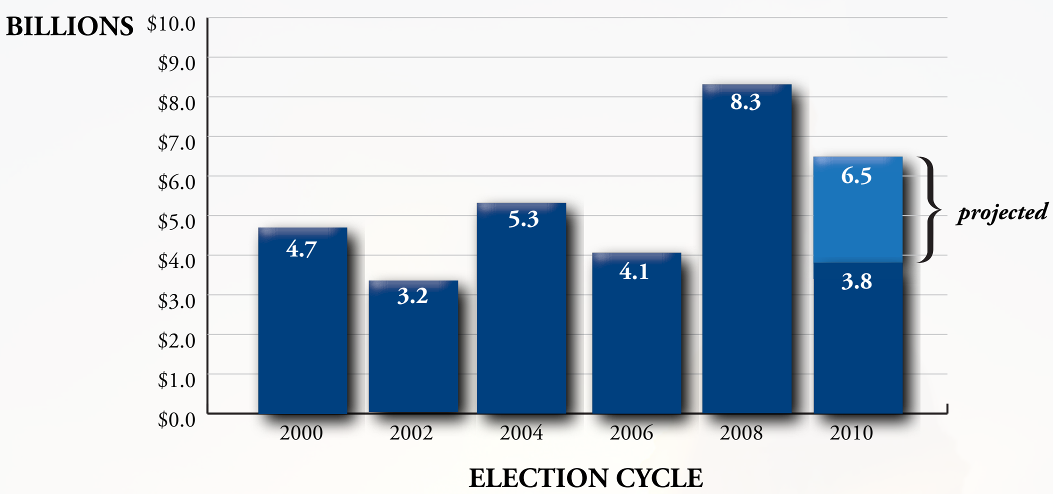
The FEC achieved a 100 percent success rate in making the financial disclosure reports and statements available to the public within 48 hours of receipt by the Commission. This fiscal year has again seen a significant increase over the last mid-term election year in the volume of data associated with filings.

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 ensure 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 2010, the FEC was able to process 91 percent of the reports within 30 days of receipt.

A mid-term election cycle at the federal level includes expenditures related to the election of: 1) all seats in the House of Representatives, 2) one-third of the Senate seats and 3) any special elections required to fill vacant seats. Figure 6 illustrates that expenditures related to federal elections are on the rise, including as they relate to mid-term election years. The data presented in Figure 6 are based on campaign finance reports, which use two calendar years as an election cycle. 2010 election cycle data are available through September 30, 2010, and spending is projected for the final quarter of calendar year 2010. All other data on the FEC's performance in this report are by fiscal year.

Although the 2010 mid-term election cycle is not yet complete, partial data for the cycle reveal that total receipts collected reached $4.3 billion by September 30, 2010, and disbursements were approximately $3.8 billion. The FEC is projecting that the total reported disbursements for the 2010 federal elections will reach $6.5 billion.

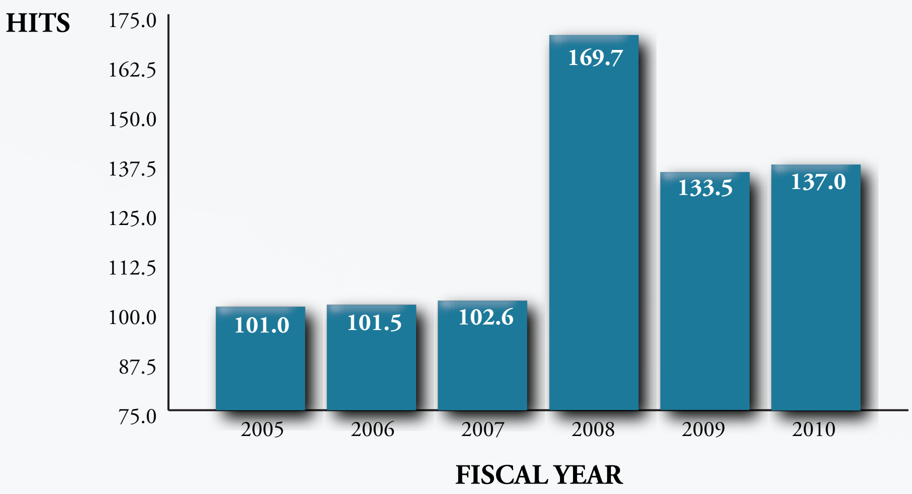
FIGURE 6 – DISBURSEMENTS IN FEDERAL ELECTIONS (IN BILLIONS)



The FEC Website

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 campaign finance information is illustrated in Figure 7, which shows a continued high number of hits on the FEC's website by users seeking campaign finance data and other information. During FY 2010, the website received approximately 137.0 million hits.

FIGURE 7 – TOTAL WEBSITE HITS (IN MILLIONS)



To make campaign finance data more accessible to the public, the FEC provides an interactive map allowing users immediate access to contribution information for the 2010 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 http://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 disclosure reports.

This year the agency also created a Compliance Map to assist members of the regulated community in their efforts to comply with campaign finance law. (http://www.fec.gov/info/ElectionDate). The Compliance Map lists all reporting dates and other significant information tied to each state's election calendar, such as the time periods when special requirements for electioneering communications and federal election activity apply. Like the interactive Disclosure Map of contribution information, the Compliance Map provides quick access to information on a state-by-state basis in an easy-to-use format.

Assuring Accurate and Complete Reports

Besides 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 Analysis Division 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 letter 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. If not, the Commission has several tools available to it, such as the Administrative Fine Program, audits, the Alternative Dispute Resolution Program and the traditional enforcement program.

Objective B: Compliance – Education and Enforcement

Helping the regulated community understand its obligations under the Act is an essential component of voluntary compliance. The FEC places a significant emphasis on encouraging compliance through its Information Division, Reports Analysis Division, Press Office and Office of Congressional, Legislative and Intergovernmental Affairs.

The Commission also encourages voluntary compliance through outreach programs. The FEC hosts instructional conferences in Washington, D.C., and in other cities across the country, where Commissioners and staff explain how to comply with the Act 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 seeking information about the law and assistance in filing disclosure reports.

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. Normally, 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 percent 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 percent of enforcement cases within an average of 15 months of receipt;
- Process 75 percent of the cases assigned to Alternative Dispute Resolution within 155 days of a case being assigned;
- Process 75 percent 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 percent 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 ten 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; and
- 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

The FEC's education and outreach programs provide the regulated community with the information it needs to comply with the campaign finance laws and provide the public with the context necessary to interpret the campaign finance data filers disclose. The FEC maintains a toll-free line to respond to inquiries regarding campaign finance data. Additionally, Campaign Finance Analysts in the Reports Analysis Division provide assistance with filing disclosure reports. The FEC also operates Press and Congressional Affairs offices.

In recent years, the Commission's website has become one of the most important sources of instantly accessible information about the Act, Commission regulations and Commission proceedings. In addition to viewing campaign finance data, anyone with Internet access can use the website to track Commission rulemakings, search advisory opinions, audits and closed enforcement matters, view campaign finance data and find reporting dates. The Commission places a high emphasis on providing educational materials about campaign finance laws and their requirements. Toward this end, the FEC has moved its focus away from the printing and manual distribution of its educational materials and instead looked for ways to leverage available technologies to create and disseminate dynamic and up-to-date educational materials through the website. While the Commission continues to make available printed copies of its educational brochures and publications, transitioning to primarily web-based media has already allowed the agency to reduce significantly its printing and mailing costs and use of resources while at the same time encouraging new and expanded ways of communicating with the public via the website.

As part of its broad effort to improve Internet communications and better serve the educational needs of the public and the regulated community, the Commission has added an E-Learning section to its Educational Outreach web page and launched its own YouTube channel, which can be found at either http://www.fec.gov/info/elearning.shtml or http://www.youtube.com/FECTube. The E-Learning page offers interactive presentations that allow users to test their knowledge of the information presented and video workshops, which are hosted on YouTube. The FEC plans to continue to expand its E-Learning program with additional content and technical improvements during the coming year.

One significant way the Commission encourages voluntary compliance is by hosting conferences across the country, where Commissioners and staff explain how to comply with the Act to candidates, parties and political action committees. The FEC held six conferences in FY 2010, three in the District of Columbia, one in Arlington, Virginia, one in San Francisco, California, and one in New Orleans, Louisiana. The FEC also hosted a series of roundtable workshops at its headquarters to explain new regulations governing the use of campaign funds for non-commercial travel and rules regarding pre-election communications and to help committees prepare their campaign finance reports. 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 Potential Violations

The FEC responds to a variety of enforcement matters through its Office of General Counsel (OGC) and, Audit, Administrative Fine, and Alternative Dispute Resolution (ADR) Programs.

Office of General Counsel

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

- The complaint process, whereby anyone may file a sworn complaint alleging violations of the Act;

- The Commission's review of a committee's reports or through a Commission audit;
- Voluntary self-reporting 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 OGC, which:

- Recommends to the Commission whether to find "reason to believe" the FECA has been violated, a finding that allows the Commission to formally initiate 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 to reach conciliation agreements with respondents; and
- Files suit in federal district court if conciliation is unsuccessful.

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

Enforcement matters are handled by OGC pursuant to the procedures set forth in 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. As a result, OGC continues to meet its obligations to the Commission and the public to handle its caseload efficiently and effectively. During Fiscal Year 2010, the Commission completed processing 135 enforcement cases, of which 101 cases (75 percent) were closed within 15 months. The average processing time for enforcement cases was 11.3 months.

Alternative Dispute Resolution

The Alternative Dispute Resolution (ADR) Program was implemented in FY 2001 to facilitate settlements outside of the traditional enforcement or litigation processes. The ADR 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 the ADR Office as to what final action should be taken. During FY 2010, the ADR Office processed 45 cases to closure and assessed $93,100 in civil penalties. The Commission met its 155-day processing benchmark in 64 percent of ADR cases, falling short of its goal of meeting this benchmark in 75 percent of cases. Total average processing time was negatively impacted by staffing issues in the ADR Office, which operated throughout much of the fiscal year with only one dispute resolution specialist instead of two. In May 2010, a second permanent ADR specialist was selected, resulting in an improvement in processing times.

Administrative Fine Program

In response to a legislative mandate, an Administrative Fine (AF) Program was implemented in July 2000 to address untimely filing and non-filing of disclosure reports in a more efficient and effective manner. The AF Program is administered by the Commission's Office of Administrative Review (OAR) and Reports Analysis Division (RAD), which are within the Office of Compliance. Since the AF Program's inception in July 2000 through July 31, 2010, the Commission has closed 2,014 cases and assessed fines of almost $3.7 million.

An administrative fine case begins when the Commission finds that a committee failed to file a required report or filed a required report late. For FY 2010, RAD exceeded its performance goal, processing 100 percent of the reason-to-believe (RTB) recommendations within 60 days of the subject report's due date. The average completion time for these recommendations was 45.4 days.

During FY 2010, OAR reviewed ten challenges submitted by committees in response to a RTB finding and/or civil money penalty. OAR reviewed 100 percent of these challenges within 60 days of receipt. The average completion time for challenges was 36.3 days. Overall, OAR has reviewed 565 challenges submitted from the Program's inception through FY 2010. The Program has successfully reduced the number of late and non-filed reports over the last several years, resulting in a dramatic reduction in the volume of work assigned to OAR. In response, the agency transferred two OAR staff members to RAD during FY 2010, leaving one staff member in OAR and better supporting RAD's workload.

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 the public funding statutes, the FEC audits all Presidential campaigns and nominating conventions that receive public funds. In addition, under FECA, the Commission audits non-Presidential committees that, according to FEC determinations, have not substantially complied with the law. The Audit Division publishes its findings in audit reports, which can be found at http://www.fec.gov/audits/audit_reports.shtml.

In FY 2009 and FY 2010, the Commission adopted procedures that provide additional opportunities for audited committees to respond to potential findings, as well as more opportunities for the Commission to review audit reports prior to approval. The most significant of the changes provides audited committees an opportunity to request a hearing before the Commission prior to final approval of the audit report. In order to maintain alignment with the agency's Strategic Plan for FY 2008 to 2013, the performance measures related to audits have not been revised to reflect the significant changes made to the audit report processing system described above. Although the data is limited at present, the Commission will continue to review the effect these procedures have on performance measures related to audits.

In FY 2010, the Commission approved eight audit reports resulting from audits "for cause." Findings were reported in five of the total eight "for cause" audit cases concluded by the Audit Division. Three of these audits (60 percent) were concluded in ten months. The average processing time for audits with findings was 512 days. The three audits with no findings were completed in an average of 66 days. The performance figures presented reflect both the added time required by the new audit report processing procedures and the time expended working out the details of that system.

Presidential committee audits demand more time and resources than FECA "for cause" audits because of their complexity. The number of audits is dependent on the number of candidates who participate in the public funding program. In the 2008 election cycle, the Commission approved the eligibility of nine candidates to receive Presidential Primary Matching Funds. One candidate subsequently withdrew from the program. The Commission also audits the publicly funded national convention committees, their host committees and General Election candidates. Of 14 Presidential audits related to the 2008 election cycle, three were completed in FY 2010 in an average of 13 months. The revisions to the audit report processing system discussed above will also affect the time needed to complete audits of publicly funded committees.

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 percent of the time;
- Issue all advisory opinions within 60-day and 20-day statutory deadlines 100 percent 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 percent of the time;
- Ensure that court filings meet all deadlines and rules imposed by the Courts 100 percent of the time; and
- Process public funding payments in the correct amounts and within established time frames 100 percent of the time.

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

Regulations

Commission initiatives, 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 regulations or revise existing regulations.

The Policy Division of OGC drafts Notices of Proposed Rulemaking (NPRMs) for Commission consideration. 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 and the corresponding Explanations and Justifications, which provide the rationale and basis for the new or revised regulations.

The Commission's strategic plan contemplates the completion of rulemakings within time frames that take into account the importance of the topics addressed, proximity to upcoming elections and externally established deadlines. There were no externally imposed deadlines for any of the nine rulemaking projects the Commission worked on during FY 2010. Hence, the Commission's time frames for the six rulemakings it completed during the fiscal year reflect the importance of the topics addressed and the proximity to the upcoming elections. Three of these six completed rulemakings were concluded within time frames that reflect these criteria.

- HLOGA travel – completed
- *Shays* coordinated communications – completed
- *Shays* voter registration and get-out-the-vote activity – completed
- *Shays* candidate appearances at State party fundraisers – completed

- *EMILY's List* repeal of invalidated provisions - completed
- *Debt Collection Improvement Act* - completed
- Standards of Conduct - in process
- *Citizens United* - in process
- *SpeechNow.org* and additional *EMILY's List* issues - in process

In early FY 2010, the Commission completed a rulemaking pursuant to the statutory provisions in HLOGA, which amended the requirements regarding candidate travel. Because the Commission lacked a quorum during part of 2008, the Commission did not meet its deadline for completing the HLOGA travel rules.

The Commission also completed three rulemakings to comply with the U.S. Court of Appeals for the District of Columbia's decision in *Shays* v. *FEC*. These rulemakings addressed coordinated communications, the definitions of "voter registration" and "get-out-the-vote activity," and fundraising by candidates and federal officeholders for state party committees and other entities. Of these three, only the candidate fundraising rulemaking was timely completed for the 2010 elections. The coordinated communications rules and the voter registration/get-out-the-vote rules were completed during the last quarter of FY 2010. Rather than putting new rules into place shortly before the 2010 general elections, which would have been confusing and disruptive for many political committees, the Commission determined that it was preferable to make these rules effective just after the 2010 elections.

The Commission also completed the repeal of certain regulations requiring nonconnected committees and separate segregated funds to allocate funds between their federal and nonfederal accounts where those funds were spent on public communications mentioning candidates, voter registration, and get-out-the-vote drives. These rules were held unconstitutional by the U.S. Court of Appeals for the District of Columbia Circuit in *EMILY's List* v. *FEC*.

Two other rulemakings focused on administrative regulations. First, the Commission issued new rules to implement the *Debt Collection Improvement Act of 1996*. Second, the Commission, together with the Office of Government Ethics, issued proposed rules on standards of conduct for FEC employees.

Lastly, the Commission began work on two rulemakings to comport with two recent court decisions. First, the Commission began a rulemaking to comply with the Supreme Court decision in *Citizens United* v. *FEC*. The Court held that the Act's prohibitions on financing independent expenditures and electioneering communications with corporate general treasury funds were unconstitutional. The second rulemaking will comply with the U.S. Court of Appeals for the District of Columbia Circuit's recent decisions in *SpeechNow.org* v. *FEC* and *EMILY's List* v. *FEC*. This second rulemaking will focus on independent groups and political committees seeking to accept unlimited funds for the sole purpose of making independent expenditures and engaging in other forms of independent spending.

Advisory Opinions

Advisory opinions (AO) are official Commission responses to questions regarding the application of federal campaign finance law to specific factual situations. The Act generally provides the Commission with 60 days to respond to an AO request. For AO requests from candidates in the two months leading up to an election, the Act provides the Commission with 20 days to respond to the request. On its own initiative, the Commission also makes available an expedited process for handling certain time-sensitive requests that are not otherwise entitled to expedited processing under the Act. The Commission has placed special emphasis on expediting its processing and consideration of these highly significant AO requests. The Commission strives to issue these advisory opinions in 30 days.

The number of AO requests that the Commission receives is subject to cycles and is somewhat higher during election years. During FY 2010, the Commission completed work on 29 AOs, all within the statutory deadlines. The Commission received one 20-day request at the end of FY 2010. The Commission did not receive any requests during FY 2010 that qualified for issuance within 30 days. The average number of days from receipt of the complete AO request to issuance of the AO was 50 days for 60-day requests that did not have extended deadlines.

Defending Challenges to the Act

The Commission is the exclusive representative of the FEC before the federal district and circuit courts, and before 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. In FY 2010, 100 percent of the Commission's court filings met all deadlines and rules imposed by the courts.

On January 21, 2010, the Supreme Court issued its opinion in *Citizens United* v. *FEC*. In ruling in large part in favor of *Citizens United*, the Supreme Court held that the Act's prohibitions on financing independent expenditures or electioneering communications with corporate general treasury funds were unconstitutional. In doing so, the Supreme Court overruled *Austin* v. *Michigan State Chamber of Commerce* that upheld a comparable state law prohibiting independent expenditures by corporations and the part of the Court's decision in *McConnell* v. *FEC* that upheld prohibitions on corporate electioneering communications. The Court reasoned that a ban on independent expenditures could not be justified by the government's interest in preventing corruption and, therefore, struck down the prohibition against corporate independent expenditures and electioneering communications. The Court, however, upheld the reporting requirements for these disbursements.

In addition, two decisions of the U.S. Court of Appeals for the D.C. Circuit have further altered the state of the law: *SpeechNow.org* v. *FEC*, which concerned whether certain FECA provisions were constitutional as applied to a group that is devoted to running independent advertisements for and against candidates and makes no direct contributions to candidates; and *EMILY's List* v. *FEC*, which concerned sources of funding for various types of activities and public communications by non-connected committees, and the treatment of funds received in response to solicitations as contributions.

In two lawsuits brought by the Republican National Committee and other plaintiffs, the Commission prevailed: the D.C. Circuit upheld the application of BCRA's soft money ban on political parties, and the Supreme Court affirmed that decision under BCRA's direct appeal procedure; and the *en banc* Fifth Circuit upheld the Act's limits on coordinated expenditures that political parties make in consultation with their candidates.

Public Funding

In addition to enforcing the FECA, the Commission is responsible for administering the public funding of Presidential elections, as specified in the public funding statutes. 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 and convention committee that receives payments under the program.

SECTION III
AUDITOR'S REPORT AND FINANCIAL STATEMENTS

Message From The Chief Financial Officer

November 12, 2010

I am pleased to present the Commission's financial statements for Fiscal Year (FY) 2010. The financial statements are an integral component of the Performance and Accountability Report. The Commission received an unqualified (clean) opinion on the Agency's financial statements from the independent auditors. This marks the second consecutive year with no material weaknesses identified. The Commission continues to improve its overall financial management by taking advantage of opportunities to modernize and upgrade business systems, facilitating training initiatives, and updating directives and policies to build toward more effective and efficient management of its resources.

In addition to this key accomplishment, the FEC:

- Provided agency-wide training on contracting officer technical representative responsibilities and managing the internal control program;
- Completed all phases of the rulemaking process to implement the *Debt Collection Improvement Act of 1996*;
- Successfully awarded 36 percent of all competed acquisitions to small businesses, of which 43 percent were Women-Owned and 16 percent were Veteran Owned – far exceeding the U.S. Small Business Administration federal government goals;
- Converted to an automated Fixed Asset Subsystem; and,
- Coordinated with the General Services Administration regarding the budget and accounting code changes necessary to support the Common Government-wide Accounting Classification (CGAC) and initiated the update of the FEC's internal systems and reports to support the new coding structure.

These efforts illustrate the organization's dedication to improved performance management in addition to strengthening financial objectives.

(cont.)

29

The Commission and FEC employees remain committed to the Agency's mission and are proud of the work we were able to accomplish in FY 2010. For FY 2011, the FEC will continue to modernize and upgrade its business systems and processes to achieve even greater levels of operational efficiency. Some of these initiatives include a payroll interface and continued efforts to convert to the CGAC structure. The Office of the Chief Financial Officer looks forward to another successful year.

Sincerely,

Mary G. Sprague

Mary G. Sprague
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 2010 Financial Statements

DATE: November 12, 2010

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 issued by Leon Snead & Company (LSC), P.C. for the fiscal year ending September 30, 2010. The audit was performed under a contract with, and monitored by, the Office of Inspector General (OIG), in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and applicable provisions of Office of Management and Budget (OMB) Bulletin No. 07-04, *Audit Requirements for Federal Financial Statements*, as amended.

Opinion on the Financial Statements

LSC audited the balance sheet of the Federal Election Commission (FEC) as of September 30, 2010, and the related statements of net cost, changes in net position, budgetary resources, and custodial activity (the financial statements) for the year then ended. The objective of the audit was to express an opinion on the fair presentation of those financial statements. In connection with the audit, LSC also considered the FEC's internal control over financial reporting and tested the FEC's compliance with certain provisions of applicable laws and regulations that could have a direct and material effect on its financial statements. The financial statements of the FEC as of September 30, 2009, were also audited by LSC whose report dated November 13, 2009, expressed an unqualified opinion on those statements.

In LSC's opinion, the financial statements present fairly, in all material respects, the financial position, net cost, changes in net position, budgetary resources, and custodial activity of the FEC as of, and for the year ending September 30, 2010, in conformity with accounting principles generally accepted in the United States of America.

Report on Internal Control

In planning and performing the audit of the financial statements of the FEC, LSC considered the FEC's internal control over financial reporting (internal control) as a basis for designing auditing procedures for the purpose of expressing their opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the FEC's internal control. Accordingly, LSC did not express an opinion on the effectiveness of the FEC's internal control.

Because of inherent limitations in internal controls, including the possibility of management override of controls; misstatements, losses, or noncompliance may nevertheless occur and not be detected. According to the American Institute of Certified Public Accountants:

- 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 affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is a more than remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control.

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

LSC's consideration of internal control was for the limited purpose described in the first paragraph in this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. LSC did not identify any deficiencies in internal control that LSC would consider to be material weaknesses, as defined above. However, LSC identified, as listed below, two deficiencies in internal controls that LSC considers to be significant deficiencies.

- Internal Controls over Financial Reporting

- Information Technology (IT) Security Control Weaknesses

Report on Compliance with Laws and Regulations

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, LSC performed tests of compliance with certain provisions of laws and regulations, noncompliance 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. LSC did not test compliance with all laws and regulations applicable to FEC.

The results of LSC's tests of compliance with laws and regulations described in the audit report disclosed no instance of noncompliance with laws and regulations that are required to be reported under U.S. generally accepted government auditing standards or OMB guidance.

Audit Follow-up

The independent auditor's report contains recommendations to address deficiencies 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.

OIG Evaluation of Leon Snead & Company's Audit Performance

We reviewed LSC's report 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; nor do we 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 LSC did not comply, in all material respects, with *Government Auditing Standards.*

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

Lynne A. McFarland

Lynne A. McFarland
Inspector General

Attachment

Cc: Alec Palmer, Acting Staff Director/Chief Information Officer
Mary G. Sprague, Chief Financial Officer
Christopher P. Hughey, Acting General Counsel

3

FEDERAL ELECTION COMMISSION

Audit of Financial Statements

As of and for the Years Ended September 30, 2010 and 2009

Submitted By

Leon Snead & Company, P.C.
Certified Public Accountants & Management Consultants

TABLE OF CONTENTS

Page

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Inspector General
The Federal Election Commission

Independent Auditor's Report

We have audited the balance sheets of the Federal Election Commission (FEC) as of September 30, 2010 and 2009, and the related statements of net cost, changes in net position, budgetary resources, and custodial activity (the financial statements) for the years then ended. The objective of our audit was to express an opinion on the fair presentation of those financial statements. In connection with our audit, we also considered the FEC's internal control over financial reporting, and tested the FEC's compliance with certain provisions of applicable laws and regulations that could have a direct and material effect on its financial statements.

SUMMARY

As stated in our opinion on the financial statements, we found that the FEC's financial statements as of and for the years ended September 30, 2010 and 2009, are presented fairly, in all material respects, in conformity with accounting principles generally accepted in the United States of America.

Our consideration of internal control would not necessarily disclose all deficiencies in internal control over financial reporting that might be material weaknesses under standards issued by the American Institute of Certified Public Accountants. However, our testing of internal control identified no material weaknesses in financial reporting. We did note one significant deficiency in internal controls over financial reporting, and one significant deficiency related to internal controls for the FEC's agency-wide Information Technology (IT) security program that are discussed later in our report.

The results of our tests of compliance with certain provisions of laws and regulations disclosed no instance of noncompliance that is required to be reported herein under *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).

The following sections discuss in more detail our opinion on the FEC's financial statements, our consideration of the FEC's internal control over financial reporting, our tests of the FEC's compliance with certain provisions of applicable laws and regulations, and management's and our responsibilities.

OPINION ON THE FINANCIAL STATEMENTS

We have audited the accompanying balance sheets of the FEC as of September 30, 2010 and 2009, and the related statements of net cost, changes in net position, budgetary resources, and custodial activity for the years then ended.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position, net cost, changes in net position, budgetary resources, and custodial activity of the FEC as of and for the years ended September 30, 2010 and 2009, in conformity with accounting principles generally accepted in the United States of America.

The information in the Management's Discussion and Analysis section is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America or OMB Circular A-136, *Financial Reporting Requirements*. We have applied certain limited procedures, which consisted principally of inquiries of FEC management regarding the methods of measurement and presentation of the supplementary information and analysis of the information for consistency with the financial statements. However, we did not audit the information and express no opinion on it. The Performance and Accountability Report, except for Management's Discussion and Analysis, is presented for the purposes of additional analysis and is not a required part of the basic financial statements. Such information has not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion on it.

INTERNAL CONTROL OVER FINANCIAL REPORTING

In planning and performing our audit of the financial statements of the FEC as of and for the years ended September 30, 2010 and 2009, in accordance with auditing standards generally accepted in the Unites States of America, we considered the FEC's internal control over financial reporting (internal control) as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the FEC's internal control. Accordingly, we do not express an opinion on the effectiveness of the FEC's internal control.

Because of inherent limitations in internal controls, including the possibility of management override of controls; misstatements, losses, or noncompliance may nevertheless occur and not be detected. 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 material weakness is a deficiency, or combination of significant deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the financial statements will not be prevented or detected and corrected on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that is less severe than a material weakness, yet important enough to merit attention by those charged with governance of the FEC.

Our consideration of internal control was for the limited purpose described in the first paragraph in this section of the report and would not necessarily identify all deficiencies in internal control that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control that we consider to be material weaknesses, as defined above. However, as discussed below, we identified certain deficiencies in internal control that we consider to be significant deficiencies.

Findings and Recommendations

1. Improvements Needed in Controls over Financial Reporting

a. <u>Accrual of Accounts Payable in Error</u>

The FEC's controls over the accrual of payables for financial statement presentation and the posting of these entries to the general ledger were not effectively implemented. Our review of September 30, 2010 financial statements, and a sample of transactions processed during Fiscal Year 2010 identified a duplicate accrual of $139,969.99 posted to the general ledger by Office of the Chief Financial Officer (OCFO) personnel. We attributed this problem to the need for more effective implementation of controls over the accounts payable accrual process.

The error we identified occurred when an accounting clerk did not follow OCFO policy to ensure that the invoice payment was not pending in Pegasys prior to recording the accrual transaction. In addition, while the OCFO's supervisory review process detected this error, actions were not taken to ensure that the error was, in fact, corrected. When discovered during the audit, OCFO personnel adjusted the financial statements to correct the error. If left uncorrected, liabilities on FEC's 2010 Balance Sheet and costs on the 2010 Statement of Net Cost (SNC) would have been overstated by approximately $140,000. Conversely, had this error not been corrected, costs on the 2011 SNC would have been understated by this same amount.

OCFO officials advised they plan to review the current accounts payable accrual process, and determine if there is a better approach to calculating the accrual estimate. They have agreed that once the OCFO ensures that the appropriate process is in place, the OCFO will train staff.

Statement of Federal Financial Accounting Standards (SFFAS) No. 1, *Accounting for Selected Assets and Liabilities*, provides that for financial reporting purposes, liabilities are recognized when goods and services are received or are recognized based on an estimate of work completed under a contract or agreement. Paragraph 77 states "When an entity accepts title to goods, whether the goods are delivered or in transit, the entity should recognize a liability for the unpaid amount of the goods. If invoices for those goods are not available when financial statements are prepared, the amounts owed should be estimated."

Recommendation

1. Provide additional training to personnel involved in accounts payable control processes, and stress to supervisors that reviews of accounts payable accruals must be more effective. Ensure when errors are noted, the reviewer follows-up to ensure corrections are made.

Agency Response

Management concurs that controls over the accounts payable accrual process should be strengthened to ensure that potential misstatements are identified and corrected in a timely manner. However, FEC management does not concur that the $140 thousand misstatement noted in the auditor's report contributes to a significant deficiency in internal control over financial reporting.

During FY 2011, management will perform the following to strengthen controls over the accounts payable accrual process:

- Perform a comprehensive review of the accounts payable accrual processes; and
- Provide additional training to ensure that agency guidelines are followed and that transactions are processed, reviewed, and reconciled consistently, completely, timely, and accurately.

Auditor Comments

We identified this error during our final testing of 2010 transactions. Our testing during FY 2009 also identified two invoices that were improperly recorded. The error in FY 2010 was identified by OCFO personnel but not corrected during supervisory review. We believe this represents a deficiency in implementation of internal controls, and does not represent "an isolated event" as stated by FEC officials since the auditors have reported problems in this area the last four years.

b. FEC Needs to Convert Manual Accounting Systems

FEC has not yet converted all manual systems and processes to automated systems that are integrated or interfaced with the core accounting system as we recommended in our prior audit. We attribute the problem in part, to: (1) difficulty in coordinating with FEC's service providers on the development of a time-phased plan to convert the manual interface of payroll systems and processes to automated systems, and (2) the opinion of OCFO personnel that the costs to convert the manual accounts receivable processes exceed the benefits of automating the system.

FEC uses spreadsheets and an outdated PeopleSoft platform to perform selected accounting operations. The financial management processes that still utilize significant manual operations include:

- Accounting for collections of fines and penalties. The OCFO requests accounts receivable information from three divisions. After the OCFO obtains the relevant information, the data is input into a spreadsheet. A standard voucher is prepared monthly and submitted to the service provider to record the accounting information into the FEC's core accounting system. Collections, however, are processed to the general ledger when the payments are received. Therefore, only at the end of each month after the standard voucher is posted to the general ledger does the accounts receivable reflect an accurate balance.

- The payroll system does not interface with the accounting system; therefore, FEC must use a PeopleSoft application that is no longer supported. This process also requires FEC to perform manual operations to reconcile the payroll data and prepare standard vouchers to input the payroll data into its accounting system. OCFO is actively working with its payroll service provider to interface the payroll system and the core accounting system.

OMB Circular No. A-127, *Financial Management Systems*, defines a core financial system as the system of record that maintains all transactions resulting from financial events. It may be integrated through a common database or interfaced electronically to meet defined data and processing requirements. The core financial system is specifically used for collecting, processing, maintaining, transmitting, and reporting data regarding financial events. Other uses include supporting financial planning, budgeting activities, and preparing financial statements. Any data transfers to the core financial system must be: traceable to the transaction source; posted to the core financial system in accordance with applicable guidance from the Federal Accounting Standards Advisory Board (FASAB); and in the data format of the core financial system.

OCFO officials concurred that FEC should consider automating manual processes whenever it is appropriate and cost-effective to do so. However, OCFO officials believe that it is not cost-effective to convert its manual accounts receivable system. Concerning the continued use of the PeopleSoft application that is no longer supported, OCFO officials advised that FEC has held several meetings over the course of FY 2010 to evaluate the potential risks, benefits, and cost-effectiveness of a direct interface between the National Finance Center (NFC) Payroll and Personnel System and General Services Administration (GSA) Pegasys Financial Management System.

We continue to believe that it is important for FEC to convert its manual processes to automated systems that are integrated or interfaced with the core accounting system.

Recommendation

2. Convert FEC manual systems and processes to automated systems that are integrated or interfaced with the core accounting system.

Agency Response

Management concurs that it is important for agencies to consider automating manual processes whenever it is appropriate and cost-effective to do so. As an example, the FEC converted its fixed assets to the General Services Administration (GSA) Fixed Asset System (Subsidiary Ledger) which has a direct interface within the GSA Financial Management System, effective in FY 2010.

Management disagrees with the recommendation that all manual processes should be automated. OMB Circular A-127, as revised, 2009, states that a financial management system *"includes the core financial systems and the financial portions of mixed systems necessary to support financial management, including automated and manual processes, procedures, and controls, data, hardware, software, and support personnel dedicated to the operation and maintenance of system functions."* While the OCFO does have some manual steps in its financial process, the office has implemented compensating controls consistent with industry best practices to eliminate unnecessary risks.

The FEC continues to evaluate the roles and responsibilities of all stakeholders to establish an electronic interface between NFC and GSA payroll and financial management systems and plans to complete the integration of those systems in FY 2011.

Additionally, the Accounts Receivable balance is immaterial to the FEC's financial statements and the volume of transactions is minimal. The expense of migration to an automated process is currently not in the best interest of the FEC. Doing so would provide little benefit to the agency or the Federal Government. This practice is consistent with the latest draft of A-127 circulated October 15, 2010.

Auditor Comments

In recent testimony before the U.S. House Oversight and Government Reform Subcommittee on Government Management, Organization, and Procurement; the Controller, Office of Management and Budget, stated that the financial management environment is changing from producing annual audited financial statements to producing financial reports more frequently, at a more granular level, and accompanied by non-financial information. The Controller further noted that agencies' financial systems are not sufficiently flexible or integrated with non-financial systems. In particular, OMB and Treasury, in coordination with the CFO Council, are working to deploy central, automated solutions that will reduce the cost and complexity of agency financial operations. The Controller concluded that federal agencies need to modernize their systems.

In addition, we noted that a recent GAO report and correspondence from OMB provide that OMB has plans underway to, "…upgrade the quality and performance of federal financial management systems by leveraging shared service solutions and implementing other government wide reforms that foster efficiencies in federal financial operations. According to OMB, the goals … are to (1) provide timely and accurate data for decision making; (2) facilitate stronger internal controls that ensure integrity in accounting and other stewardship activities; (3) reduce costs by providing a competitive alternative for agencies to acquire, develop, implement, and operate financial management systems through shared service solutions; (4) standardize systems, business processes, and data elements; and (5) provide for seamless data exchange between and among federal agencies by implementing a common language and structure for financial information and system interfaces."

We continue to believe that it is important for FEC to convert its manual processes to automated systems that are integrated or interfaced with the core accounting system. It should be noted that this problem was also reported by the predecessor auditors as part of a material weakness in the 2008 audit report, and in our 2009 financial statement audit report.

2. IT Security Control Weaknesses

FEC has either implemented corrective actions or has plans developed to address most of the IT control weaknesses we reported in our 2009 financial statement audit report. However, we found in our 2010 audit that some controls were not effectively implemented, and for two areas FEC did not agree to implement our recommendations. We attributed these conditions, in part, to the complexity of issues involved, and the funding necessary to complete all planned actions. As a result, FEC information and information systems are at additional risk until these corrective actions are fully implemented. Details of the issues noted during our 2010 audit are discussed below.

a. Configuration Management and FDCC Security Controls

Additional actions are necessary before FEC meets best practices for configuration control, and Federal Desktop Core Configuration (FDCC) requirements. While FEC has established baseline configuration standards for a number of its systems, these standards were not effectively implemented for the laptops we tested.

The FEC established baseline configuration security standards that identify specific services, such as Universal Plug and Play, Netmeeting Remote Desktop Sharing, Remote Desktop Help Session Manager, and Remote Registry access that should be disabled unless there is a specific business need for these services. However, our audit tests showed that these services had not been disabled, and users could manually start these services on laptop computers.

In addition, the baseline configuration security standards required that on Windows XP machines the "administrator account" be renamed, and that access to administrator authorities is limited to users requiring such access. Based on our tests, we determined that users were provided local administrator rights allowing them to change settings, as well as the ability to start "services" manually. By using these authorities, users could, among other activities, override the FEC control setting which requires re-authentication after 30 minutes of inactivity.

FEC has not yet fully implemented FDCC security control requirements that OMB established in 1997 as "best practices" security requirements for Windows computers. FEC has established a project to adopt selected control requirements and estimates that full implementation of selected controls will not be implemented until 2012. Our tests showed the following FDCC requirements have not yet been adopted by FEC.

Access Control Objective	FEC Settings	FDCC Requirements	Meets or exceed FDCC
Enforce password history	5 passwords remembered	24	No
Maximum password age	180 days	60	No
Minimum password age	0 days	1	No
Minimum password length	8 characters	12 characters	No
Suspend inactive account	FEC activates screen saver; does not suspend session	15 minutes	No

FEC plans to implement the FDCC requirements that the agency agrees to adopt in a phased approach for new workstations. FEC estimated implementation would be completed by 2012.

NIST Special Publications 800-53, *Recommended Security Controls for Federal Information Systems*, provides the minimum controls that an agency should adopt in order to implement a configuration management control process.

We discussed these issues during our audit with Office of the Chief Information Officer (OCIO) officials who concurred with our recommendations. OCIO officials advised they meet about 75 percent of FDCC requirements, and have plans to meet additional requirements when the FEC implementation process has been completed.

Recommendations

3. Ensure that FEC baseline configuration standards are implemented in accordance with FDCC requirements for all workstations.

4. Perform periodic assessments of baseline configuration settings as part of FEC's continuous monitoring program.

Agency Response

Management partially concurs with these recommendations and plans to make use of these best practices once the FEC's FDCC project is fully implemented. However, the FEC reserves the right to implement only those settings that it considers advantageous to its computing environment. As indicated, FEC is already 75 percent FDCC compliant, and has developed a plan and timetable to achieve near 93 percent compliance. Per FDCC specifications, any recommended setting not implemented will include a documented justification.

Auditor Comments

FEC officials have partially concurred in our recommendations. However, FEC officials have reserved the right to implement only those settings that the agency considers advantageous to its operations. As discussed in OMB's implementing guidance, OMB has determined that the FDCC settings provide the best approach to strengthening the security over workstations that operate in a Windows environment. We continue to believe that FEC should follow OMB guidance in this important IT security area.

b. Scanning Process Needs Strengthening

While FEC has established a framework to perform periodic vulnerability scanning, including a process to address the vulnerabilities identified through its scanning processes, workstations connected to the network are currently excluded from the FEC's vulnerability scanning program. Without scanning of the individual workstations, FEC cannot detect potential vulnerabilities and assure that the devices are properly configured to meet FDCC and/or FEC security configurations.

NIST Special Publications 800-53 establishes vulnerability scanning as one of the recommended security controls in the risk assessment control area. The control requirement provides that the organization scans for vulnerabilities in the information system and hosted applications, including when new vulnerabilities potentially affecting the system/applications are identified and reported.

During our audit, we discussed this matter with OCIO officials and they advised us that they plan to perform additional workstation scanning once the FEC's FDCC project is fully implemented. OCIO officials added that they realize additional workstation scanning will help ensure continued adherence to best practices.

Recommendation

5. Include all components of the general support system, including workstations, into the organization's vulnerability scanning process to ensure that the general support system, in its entirety, is periodically assessed.

Agency Response

Management concurs with this recommendation, and plans to make use of additional workstation vulnerability scanning once the FEC's FDCC project is fully implemented. As a proactive solution and compensating control, the FEC has implemented an automated patching process to ensure all workstation operating system vulnerabilities are properly patched. Other compensating controls the Commission employs are real-time virus and adware detection. The Commission specifically scans workstations hard-drives, CD-ROMs, and flash drives for malicious code such as viruses; worms, trojan horses, spyware, keyboard loggers etc. Additional levels of workstation security includes workstation firewalls, real-time virus and adware detection and prevention, operating system and application password standards, two factor authentication, whole hard drive encryption, and 15 minute account lock-out.

Auditor Comments

Since FEC officials have agreed to implement the recommendation, we have no additional comments.

c. Termination of Separated Employees Access Authorities

Controls established by FEC to ensure that separated employees access to the FEC network are timely removed did not function as designed. FEC policies and standards require the access authorities to be disabled within one business day, except for emergency situations when the account will be disabled immediately.

FEC implemented the FEC System Access (FSA) system to control the addition and termination of users to its systems. We performed tests of this system as part of our 2010 tests of IT controls. We sampled 11 persons who had separated from FEC during the 2010 fiscal year, and obtained information from OCIO personnel as to the date the individuals' access to the FEC network was disabled or terminated. OCIO officials advised us that operational problems occurred, and FEC did not have the dates that these employees were removed from the network.

We performed additional tests of personnel who separated after June 2, 2010, to determine if the problem impacting our original sample was corrected. We identified 14 persons who separated after June 2, 2010. Of this number, we found that seven employees' accounts were not disabled until 5 to 41 days after the employee separated.
We discussed this condition during the audit with OCIO officials who advised that they investigated the situation, and verified that there was a lack of communication between the affected offices. OCIO officials advised us that management has formed a team to resolve any residual communication issues, implement additional fail-safe methods to ensure the OCIO is notified about separations in a timely manner, and implement a policy and associated procedures to ensure consistency throughout the entire termination process.

Recommendation

6. Implement additional controls to ensure that former employees' access to the network is terminated in accordance with FEC policies.

Agency Response

Management concurs with this finding and recommendation. Management investigated the situation and verified that there was indeed a lack of communication between the affected offices. Since that time, the Commission has formed a management team to first resolve any residual communication issues and secondly develop and implement a policy (and associated procedures) to ensure access to FEC information resources are properly terminated.

Auditor Comments

Since FEC officials have agreed to implement the recommendation, we have no additional comments.

d. Access Controls Need Further Strengthening

FEC needs to further strengthen access controls by implementing a user access authority certification process, and by implementing best practice controls over dial-up access to the FEC network.

FEC acquired software in October 2009 to assist the agency in identifying users' specific access authorities, and had established a project to develop processes to implement this control requirement. However, because of the complexities involved with the configuration of the system, identifying the files and folders to which users have access, and ensuring the documentation provided to managers is informative and useful; the project implementation has been delayed.

We also compared FEC's controls for remote access to best practice requirements, and found that FEC had not implemented sufficient controls for its dial-up access. Best practices require, among other things, the organization to employ automated mechanisms to facilitate the monitoring and control of remote access methods, and the use of cryptography to protect the confidentiality and integrity of remote access sessions. During the period of our review, we determined that the dial-up access for FEC currently did not meet the requirements relating to the use of cryptography to protect the information transmitted. In contrast, FEC requires personnel who access the network through connections other than dial-up access, to use multi-factor authentication, a virtual private network (VPN) connection, and full disk encryption.

During our audit, we discussed these issues with OCIO officials. Concerning the review of user access authorities, we were advised that management is currently reassessing the resources and timeline required to provide useful network access information to users' supervisors. In addition, OCIO officials advised that after performing a cost-benefit analysis of adding encryption to an already slow and rarely used dial-up service, the Commission has concluded it will be suspending its dial-up services as of September 30, 2010.

Recommendations

7. Assure sufficient resources are provided to complete the project dealing with the establishment of processes to enable periodic review of users' access authorities.

8. Require that dial-up access is properly secured as required by best practices, or terminate this type of access for users.

Agency Response

Management concurs with these recommendations and is currently reassessing the resources and timeline required to overcome the complexities involved with ensuring that technical information provided to non-technical business managers is informative and useful enough to make educated decisions about system access.

After performing a cost-benefit analysis of adding encryption to an already slow and rarely used dial-up service, the Commission has concluded it would be more cost efficient to concentrate its efforts on continuing to support its more secure and reliable high speed connection. With this in mind, the Commission has suspended its dial-up services as of September 30, 2010.

Auditor Comments

Since FEC officials have agreed to implement the recommendations, we have no additional comments.

e. Security Awareness Training

FEC needs to strengthen its control processes dealing with security awareness training and obtaining acknowledgement of rules of behavior for new employees and contractors. During our 2010 testing, we reviewed records detailing security awareness training provided to FEC employees and contractors. We found that for new employees and contractors the FEC does not require these personnel to receive the security awareness training, and acknowledge rules of behavior, prior to granting access to the FEC general support system. For example, we identified 10 users that received the training two weeks or longer after coming onboard, or the records showed the individuals had never completed the training.

OMB Circular A-130, Appendix III, General Support Systems, the document we used to determine best practices, requires that agencies provide security awareness training and rules of behavior to personnel prior to granting access to an agency's systems.

OCIO officials advised us that the FEC believes strengthening its Security Awareness Program would benefit the Commission. To this end, the FEC has decreased the training completion period for new employees to one business week from the date of hire. In our opinion, and as required in OMB Circular A-130, it is important that new employees and contractors become aware of privacy and security requirements prior to being allowed access to agency information and information systems.

Recommendation

9. Revise FEC procedures to require that all new personnel and contractors take the security awareness training, and acknowledge rules of behavior prior to being granted access to FEC systems.

Agency Response

Management partially concurs with this finding and recommendation. Although six of the 10 cited were still within FEC policy of three weeks to complete security awareness training and the remaining four would have been notified of their non-compliance during the 2010 security awareness completion review, the FEC does believe strengthening its Security Awareness Program would benefit the Commission. To this end, the FEC has decreased the three week completion period for new employees to one business week.

Auditor Comments

FEC officials partially concurred with our recommendation, and agreed to reduce the period for completing the security awareness training to one business week. We concur with this alternate approach to our recommendation.

f. Contingency Planning and COOP

In 2009, we reported that the FEC had developed a Plan of Action and Milestones (POA&M) and made progress in developing a contingency plan and Continuity of Operations Plan (COOP) document that meets federal requirements and best practices. For 2010, we found that FEC had not yet completed the testing of the contingency plan and had not finalized the COOP. The FEC POA&M showed that the anticipated completion date for full development of the COOP and contingency plan, including testing of the plans is scheduled for November 2010. FEC officials advised us that the project was delayed due to funding issues.

Recommendation

10. Monitor the POA&M to ensure that the documents are completed and fully tested by the end of the 2010 calendar year.

Agency Response

Management concurs with this recommendation.

Auditor Comments

Since FEC officials have agreed to implement the recommendation, we have no additional comments.

g. FEC Would Further Strengthen IT Security Program by Fully Adopting Best Practices

FEC's IT security program would be further strengthened if the agency adopted the best practices included in the NIST computer security controls publications. FEC is exempt from the Federal Information Security Management Act (FISMA)[1] requirements, but could voluntarily adopt these best practices as other federal entities have elected to do.

NIST is required by law to develop IT security standards and guidelines, and to consult with other federal agencies and offices, as well as the private sector to improve information security and avoid unnecessary and costly duplication of efforts in establishing security control requirements. NIST, in addition to its comprehensive public review and vetting process, collaborates with the Office of the Director of National Intelligence, the Department of Defense, and the Committee on National Security Systems to establish a common foundation for information security across the federal government. NIST notes that a common

[1] The E-Government Act (P.L. 107-347) recognizes the importance of information security to the economic and National security interests of the United States. Title III of the E-Government Act, entitled the Federal Information Security Management Act (FISMA), emphasizes the need for organizations to develop, document, and implement an organization-wide program to provide security for the information systems that support its operations and assets.

foundation for information security will provide the federal government and their support contractors, more uniform and consistent ways to manage the risk to organizational operations that results from operations and use of information systems. In addition, NIST notes that a common foundation for information security will also provide a strong basis for reciprocal acceptance of security authorization decisions and facilitate information sharing.

During our 2010 audit, we identified four other federal entities that were also exempt from FISMA requirements. To determine how these agencies addressed the establishment of IT security standards, we reviewed selected documentation from the agencies. Details follow.

Agency	Actions Taken by Agency
Government Accountability Office	GAO's 2009 Performance and Accountability Report notes that even though GAO is not obligated by law to comply with FISMA, GAO has adopted FISMA requirements to strengthen its information security program. GAO added that FISMA and related federal guidance from the Office of Management and Budget constitute the cornerstone of its security program, establishing the procedures and practices that strengthen their protections through the implementation of security "best practices. GAO establishes its security standards based on the federal guidance found in the National Institute of Standards and Technology (NIST) 800 series and Federal Information Processing Standards publications. GAO further noted that as existing NIST guidance is updated and new guidance disseminated, GAO has adjusted its internal information technology security policies and procedures.
The Smithsonian Institution	The Institution's website notes that the agency voluntarily complies with FISMA requirements because they are consistent with the agency's IT strategic goals.
Department of Defense	Employ security controls equal or higher than FISMA minimum requirements.
Central Intelligence Agency	Employ security controls equal or higher than FISMA minimum requirements.

During our audit, we discussed this matter with OCIO officials who advised that they do not concur that FEC should adopt NIST standards as best practice. OCIO officials advised that it would be improper for the FEC to disregard the will of Congress. OCIO officials noted that it was not the original intent of NIST to impose a set of standards that all federal agencies must adhere to. OCIO officials advised that FEC does utilize NIST as one source of guidance when determining best practice.

As mentioned above, other exempt federal agencies have voluntarily adopted the FISMA requirements and NIST security standards. In addition, FEC's Office of General Counsel provided correspondence, as part of documentation to update those statues, regulations and policies that are applicable and not applicable to FEC, that indicated that if FEC elected, the agency could adopt exempted regulations as a model. Therefore, it appears that the General Counsel has already determined it is allowable for FEC to adopt exempted regulations.

As FEC officials discussed above, organizations have flexibility in applying the baseline security controls in accordance with the guidance provided in NIST Special Publication 800-53. NIST notes that the minimum controls could be tailored up, down, or an agency could adopt another control commensurate with risk. FEC has rated the GSS as a moderate risk system and should adopt the NIST minimum controls to address the risks to this system, or other controls commensurate with risk. Due to FEC's significant reliance on information technology to support the agency's mission, adoption of the NIST IT security standards framework would improve the agency's ability to protect IT systems from constantly changing information security threats and risks. In addition, if FEC does not adopt a set of best practice security controls, FEC will have difficulty in setting security standards for FEC IT contractors' performance and will not have benchmarks to effectively monitor contractors performing sensitive IT security operations for FEC.

FEC officials have indicated that when the "FEC deviates from the NIST model it is only after careful evaluation, and it is believed that the agency has either a better or more cost effective method of achieving its IT security goals." FEC has decided not to implement strengthened access controls due to user concerns. FEC did not provide an analysis of the risks to the system due to this lessening of minimum control requirements, establish alternative control processes, or perform any other analytical review that would support agency decisions for deviations from IT security best practices. While longer passwords, more frequent password changes, and less frequent use of the same password all add complexities to users, decisions should be primarily based on a risk-based analysis.

Recommendation

11. Adopt as a model the NIST IT security controls established in FIPS 200, *Minimum Security Requirements for Federal Information and Information Systems,* and SP 800-53, *Recommended Security Controls for Federal Systems and Organizations*.

Agency Response

Management disagrees with this finding and recommendation except to the extent it acknowledges that the FEC may choose to voluntarily apply National Institute of Standards and Technology ("NIST") IT security standards. As the report notes, information systems security standards promulgated by NIST are derived from the *Federal Information Security Management Act* ("FISMA"), 44 U.S.C. 3541 et seq. FISMA incorporates the *Paperwork Reduction Act's* definition of "agency," which specifically excludes the Commission. See 44 U.S.C. 3502(1) (B). Accordingly, FISMA's requirement that agencies follow NIST guidelines is not applicable to the Commission. Nevertheless, the FEC has voluntarily adopted some of these best practices on a case-by-case basis, based on its own assessment of risk, and reserves the right to implement only practices that it considers advantageous to its computing environment.

Auditor Comments

We believe that FEC's IT security program would be strengthened by adopting and meeting the NIST minimum security requirements. As noted in the report, other agencies that are exempt from FISMA compliance have agreed to adopt the NIST security requirements. For example, GAO has stated that it adopted FISMA requirements to strengthen its information security program, and that FISMA and related federal guidance from the Office of Management and Budget constitute the cornerstone of its security program, establishing the procedures and practices that strengthen their protections through the implementation of security "best practices." We believe that FEC would achieve the same level of assurance if it adopted the FISMA requirements.

A summary of the status of prior year findings is included as Appendix 1.

We noted other control deficiencies over financial reporting and its operation that we have reported to the management of the FEC and those charged with governance in a separate letter dated November 12, 2010.

COMPLIANCE WITH LAWS AND REGULATIONS

The results of our tests of compliance with certain provisions of laws and regulations, as described in the Responsibilities section of this report, disclosed no instance of noncompliance with laws and regulations that is required to be reported under *Government Auditing Standards* and OMB Bulletin 07-04 (as amended).

Under OMB Bulletin 07-04, auditors are generally required to report whether the agency's financial management systems substantially comply with the federal financial management systems requirements, applicable federal accounting standards, and the United States Government Standard General Ledger at the transaction level specified in the Federal Financial Management Improvement Act (FFMIA). The Accountability of Tax Dollars Act, which requires the FEC to prepare and submit audited financial statements to Congress and the Director of OMB, did not extend to FEC the requirement to comply with FFMIA.

RESPONSIBILITIES

Management Responsibilities

Management of the FEC is responsible for: (1) preparing the financial statements in conformity with generally accepted accounting principles; (2) establishing, maintaining, and assessing internal control to provide reasonable assurance that the broad control objectives of the Federal Managers' Financial Integrity Act (FMFIA) are met; and (3) complying with applicable laws and regulations. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control policies.

Auditor Responsibilities

Our responsibility is to express an opinion on the financial statements based on our audit. We conducted our audit 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 OMB Bulletin 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: (1) examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements; (2) assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In planning and performing our audit, we considered the FEC's internal control over financial reporting by obtaining an understanding of the agency's internal control, determining whether internal controls had been placed in operation, assessing control risk, and performing tests of controls in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements.

We limited our internal control testing to those controls necessary to achieve the objectives described in OMB Bulletin 07-04 (as amended) and *Government Auditing Standards*. We did not test all internal controls relevant to operating objectives as broadly defined by FMFIA. Our procedures were not designed to provide an opinion on internal control over financial reporting. Consequently, we do not express an opinion thereon.

As required by OMB Bulletin 07-04 (as amended), with respect to internal control related to performance measures determined to be key and reported in Management's Discussion and Analysis, we made inquiries of management concerning the methods of preparing the information, including whether it was measured and presented within prescribed guidelines; changes in the methods of measurement or presentation from those used in the prior period(s) and the reasons for any such changes; and significant assumptions or interpretations underlying the measurement or presentation. We also evaluated the consistency of Management's Discussion and Analysis with management's responses to the foregoing inquiries, audited financial statements, and other audit evidence obtained during the examination of the financial statements. Our procedures were not designed to provide assurance on internal control over reported performance measures, and, accordingly, we do not provide an opinion thereon.

As part of obtaining reasonable assurance about whether the agency's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, and significant provisions of contracts, noncompliance 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 the FEC. Providing an opinion on compliance with certain provisions of laws, regulations, and significant contract provisions was not an objective of our audit and, accordingly, we do not express such an opinion.

DISTRIBUTION

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

Leon Snead & Company, PC

Leon Snead & Company, P.C.
November 12, 2010

Appendix 1

Status of Prior Year Reportable Conditions, and Non-Compliance with Significant Laws and Regulations

Recommendation	Status As Of September 30, 2010
1. Strengthen controls over the accruals of accounts payable, and ensure that supervisory reviews of accounts payable accruals are performed.	Recommendation open – reported in current year significant deficiency.
2. Update OCFO policies to incorporate the new strengthened processes for indentifying and posting accounts payable accruals.	Recommendation closed.
3. Re-emphasize, in writing, to purchase cardholders and managers their responsibilities associated with managing the purchase card program payment process and the need for effective internal controls as discussed in FEC Procurement Procedures.	Recommendation closed.
4. Update and issue the Accounting Manual within the next six months.	Recommendation closed.
5. Establish a policy that requires OCFO policies and procedures to be periodically reviewed and updated such as on a two to three year cycle.	Recommendation closed.
6. Partner with FEC service providers to develop a time-phased plan to convert the manual systems and processes to automated systems that are integrated or interfaced with the core accounting system. Establish a goal of converting these systems by the end of 2010.	Recommendation open – reported in current year significant deficiency.
7. Formally adopt as a model for FEC the NIST IT security controls established in FIPS 200, *Minimum Security Requirements for Federal Information and Information Systems,* and SP 800-53, *Recommended Security Controls for Federal Systems and Organizations*.	Recommendation open – reported in current year significant deficiency.
8. Perform an annual independent assessment to determine whether FEC's agency-wide IT security program meets minimum security controls established by NIST.	Recommendation closed.[2]
9. Implement a process to require users' supervisors to recertify a user's access authorities annually, and maintain documentation to support actions taken to address any changes required by the reviews.	Recommendation open – reported in current year significant deficiency.
10. Adopt Federal Desktop Core Configuration (FDCC) standards and implement these standards by the end of the 2010 fiscal year.	Recommendation open – reported in current year significant deficiency.
11. Include workstations and devices attached to the network in periodic scans performed by FEC.	Recommendation open – reported in current year significant deficiency.
12. Maintain documentation showing actions taken to address the problems identified by the vulnerability scans.	Recommendation closed.
13. Implement best practice controls over FEC's dial-up access.	Recommendation open – reported in current year significant deficiency.

[2] This recommendation is closed since the OIG has the authority to perform such an audit.

Appendix 1

14. Review the circumstances surrounding the untimely removal of the separated employee's access to FEC's network, and ensure controls are in place to remove the employee's access immediately upon departure.	Recommendation open – reported in current year significant deficiency.
15. Develop an OCIO policy that requires standards, guidelines and policies to be dated, authenticated with a signature, and scheduled for review and update.	Recommendation closed.
16. Prepare a detailed POA&M for items identified in the risk assessment of the GSS.	Recommendation closed.
17. FEC should develop and enforce policies and procedures for debt collection that will ensure compliance with the DCIA and OMB A-129.	Recommendation closed.

Appendix 2

Federal Election Commission
2010 Financial Statement Audit
Management Responses to Audit Findings

Auditor Recommendation #1: Provide additional training to personnel involved in accounts payable control processes, and stress to supervisors that reviews of accounts payable accruals must be more effective. Ensure when errors are noted, the reviewer follows-up to ensure corrections are made.

Management Response to Recommendation #1: Management concurs that controls over the accounts payable accrual process should be strengthened to ensure that potential misstatements are identified and corrected in a timely manner. However, FEC management does not concur that the $140 thousand misstatement noted in the auditor's report contributes to a significant deficiency in internal control over financial reporting. The results of audit testing and FEC management's own subsequent review of the accounts payable accrual indicated that this error was an isolated event and not indicative of a systemic breakdown in internal controls. In addition, the noted misstatement is immaterial to the FEC's financial statements. Total liabilities for the FEC were $7.7 million as of September 30, 2010, and the overstatement to accounts payable of $140 thousand represented two tenths of a percent (0.20%) of the Net Cost of Operations.

During FY 2011, management will perform the following to strengthen controls over the accounts payable accrual process:

- Perform a comprehensive review of the accounts payable accrual processes; and
- Provide additional training to ensure that agency guidelines are followed and that transactions are processed, reviewed, and reconciled consistently, completely, timely, and accurately.

Auditor Recommendation #2: Convert FEC manual systems and processes to automated systems that are integrated or interfaced with the core accounting system.

Management Response to Recommendation #2: Management concurs that it is important for agencies to consider automating manual processes whenever it is appropriate and cost-effective to do so. As an example, the FEC converted its fixed assets to the General Services Administration (GSA) Fixed Asset System (Subsidiary Ledger) which has a direct interface within the GSA Financial Management System, effective in FY 2010.

Management disagrees with the recommendation that all manual processes should be automated. OMB Circular A-127, as revised, 2009, states that a financial management system *"includes the core financial systems and the financial portions of mixed systems necessary to support financial management, including automated and manual processes, procedures, and controls, data, hardware, software, and support personnel dedicated to the operation and maintenance of system functions."* While the OCFO does have some manual steps in its financial process, the office has implemented compensating controls consistent with industry best practices to eliminate unnecessary risks.

Appendix 2

The FEC continues to evaluate the roles and responsibilities of all stakeholders to establish an electronic interface between NFC and GSA payroll and financial management systems and plans to complete the integration of those systems in FY 2011.

Additionally, the Accounts Receivable balance is immaterial to the FEC's financial statements and the volume of transactions is minimal. The expense of migration to an automated process is currently not in the best interest of the FEC. Doing so would provide little benefit to the agency or the Federal Government. This practice is consistent with the latest draft of A-127 circulated October 15, 2010.

Auditor Recommendation #3: Ensure that FEC baseline configuration standards are implemented in accordance with FDCC requirements for all workstations.

Auditor Recommendation #4: Perform periodic assessments of baseline configuration settings as part of FEC's continuous monitoring program.

Management Response to Recommendations #3 and #4: Management partially concurs with these recommendations and plans to make use of these best practices once the FEC's FDCC project is fully implemented. However, the FEC reserves the right to implement only those settings that it considers advantageous to its computing environment. As indicated, FEC is already 75 percent FDCC compliant, and has developed a plan and timetable to achieve near 93 percent compliance. Per FDCC specifications, any recommended setting not implemented will include a documented justification.

Auditor Recommendation #5: Include all components of the general support system, including workstations, into the organization's vulnerability scanning process to ensure that the general support system, in its entirety, is periodically assessed.

Management Response to Recommendation #5: Management concurs with this recommendation, and plans to make use of additional workstation vulnerability scanning once the FEC's FDCC project is fully implemented. As a proactive solution and compensating control, the FEC has implemented an automated patching process to ensure all workstation operating system vulnerabilities are properly patched. Other compensating controls the Commission employs are real-time virus and adware detection. The Commission specifically scans workstations hard-drives, CD-ROMs, and flash drives for malicious code such as viruses; worms, trojan horses, spyware, keyboard loggers etc. Additional levels of workstation security includes workstation firewalls, real-time virus and adware detection and prevention, operating system and application password standards, two factor authentication, whole hard drive encryption, and 15 minute account lock-out.

Auditor Recommendation #6: Implement additional controls to ensure that former employees' access to the network is terminated in accordance with FEC policies.

Management Response to Recommendation #6: Management concurs with this finding and recommendation. Management investigated the situation and verified that there was indeed a

Appendix 2

lack of communication between the affected offices. Since that time, the Commission has formed a management team to first resolve any residual communication issues and secondly develop and implement a policy (and associated procedures) to ensure access to FEC information resources are properly terminated.

Auditor Recommendation #7: Assure sufficient resources are provided to complete the project dealing with the establishment of processes to enable periodic review of users' access authorities.

Auditor Recommendation #8: Require that dial-up access is properly secured as required by best practices, or terminate this type of access for users.

Management Response to Recommendations #7 and #8: Management concurs with these recommendations and is currently reassessing the resources and timeline required to overcome the complexities involved with ensuring that technical information provided to non-technical business managers is informative and useful enough to make educated decisions about system access.

After performing a cost-benefit analysis of adding encryption to an already slow and rarely used dial-up service, the Commission has concluded it would be more cost efficient to concentrate its efforts on continuing to support its more secure and reliable high speed connection. With this in mind, the Commission has suspended its dial-up services as of September 30, 2010.

Auditor Recommendation #9: Revise FEC procedures to require that all new personnel and contractors take the security awareness training, and acknowledge rules of behavior prior to being granted access to FEC systems.

Management Response to Recommendation #9: Management partially concurs with this finding and recommendation. Although six of the 10 cited were still within FEC policy of three weeks to complete security awareness training and the remaining four would have been notified of their non-compliance during the 2010 security awareness completion review, the FEC does believe strengthening its Security Awareness Program would benefit the Commission. To this end, the FEC has decreased the three week completion period for new employees to one business week.

Auditor Recommendation #10: Monitor the POA&M to ensure that the documents are completed and fully tested by the end of the 2010 calendar year.

Management Response to Recommendation #10: Management concurs with this recommendation.

Auditor Recommendation #11: Adopt as a model the NIST IT security controls established in FIPS 200, *Minimum Security Requirements for Federal Information and Information Systems,* and SP 800-53, *Recommended Security Controls for Federal Systems and Organizations*.

Management Response to Recommendation #11: Management disagrees with this finding and recommendation except to the extent it acknowledges that the FEC may choose to

Appendix 2

voluntarily apply National Institute of Standards and Technology ("NIST") IT security standards. As the report notes, information systems security standards promulgated by NIST are derived from the *Federal Information Security Management Act* ("FISMA"), 44 U.S.C. 3541 et seq. FISMA incorporates the *Paperwork Reduction Act's* definition of "agency," which specifically excludes the Commission. See 44 U.S.C. 3502(1)(B). Accordingly, FISMA's requirement that agencies follow NIST guidelines is not applicable to the Commission. Nevertheless, the FEC has voluntarily adopted some of these best practices on a case-by-case basis, based on its own assessment of risk, and reserves the right to implement only practices that it considers advantageous to its computing environment.

BALANCE SHEET

As of September 30, 2010 and 2009 (in dollars)

Assets (Note 2)	2010	2009
Intragovernmental:		
Fund Balance with Treasury (Note 3)	$ 12,922,081	$ 10,911,130
Total Intragovernmental	12,922,081	10,911,130
Accounts receivable, net (Note 4)	15,482	203,999
General property and equipment, net (Note 5)	4,621,490	6,546,474
Total assets	**$ 17,559,053**	**$ 17,661,603**
Liabilities (Note 6)		
Intragovernmental:		
Accounts payable	$ 117,692	$ 29,594
Employer contributions and payroll taxes payable	432,326	462,082
Deferred rent	609,419	696,479
Custodial liability (Note 11)	15,482	203,999
Other	6,507	-
Total Intragovernmental	1,181,426	1,392,154
With the public:		
Accounts payable	1,972,779	1,524,033
Accrued payroll and benefits	1,988,376	1,752,371
Unfunded leave	2,516,625	2,514,822
Contingent Liability (Note 7)	60,110	-
Other	3,724	3,208
Total liabilities	**7,723,040**	**7,186,588**
Net Position		
Unexpended appropriations	8,406,931	7,145,579
Cumulative results of operations	1,429,082	3,329,436
Total net position	**9,836,013**	**10,475,015**
Total liabilities and net position	**$ 17,559,053**	**$ 17,661,603**

The accompanying notes are an integral part of these statements.

STATEMENT OF NET COST

For the Years Ended September 30, 2010 and 2009 (in dollars)

Program Costs:	2010	2009
Administering and Enforcing the FECA		
Gross costs	$ 69,768,762	$ 66,826,731
Net program costs	69,768,762	66,826,731
Net cost of operations (Note 9)	**$ 69,768,762**	**$ 66,826,731**

The accompanying notes are an integral part of these statements.

STATEMENT OF CHANGES IN NET POSITION

For the Years Ended September 30, 2010 and 2009 (in dollars)

	2010	2009
Cumulative results of operations		
Beginning balances	$ 3,329,436	$ 4,764,660
Beginning balances, as adjusted	$ 3,329,436	$ 4,764,660
Budgetary financing sources		
Appropriations used	64,733,066	62,985,321
Other financing sources (non-exchange)		
Imputed financing	3,135,342	2,406,186
Total financing sources	67,868,408	65,391,507
Net cost of operations	(69,768,762)	(66,826,731)
Net change	(1,900,354)	(1,435,224)
Cumulative results of operations	**$ 1,429,082**	**$ 3,329,436**
Unexpended appropriations		
Beginning balances	$ 7,145,579	$ 6,866,188
Beginning balances, as adjusted	$ 7,145,579	$ 6,866,188
Budgetary financing sources		
Appropriations received	66,500,000	63,618,000
Other adjustments	(505,582)	(353,288)
Appropriations used	(64,733,066)	(62,985,321)
Total budgetary financing sources	1,261,352	279,391
Total unexpended appropriations	**8,406,931**	**7,145,579**
Net position	**$ 9,836,013**	**$ 10,475,015**

The accompanying notes are an integral part of these statements.

STATEMENT OF BUDGETARY RESOURCES

For the Years Ended September 30, 2010 and 2009 (in dollars)

	2010	2009
Budgetary Resources (Note 10)		
Unobligated balance, brought forward, October 1	$ 2,085,876	$ 1,961,438
Recoveries of prior year obligations	588,194	561,893
Budget authority		
Appropriations received	66,500,000	63,618,000
Spending authority from offsetting collections		
Collected	21,622	4,113
Total budget authority	$ 66,521,622	$ 63,622,113
Permanently not available	(505,582)	(353,288)
Total budgetary resources	**$ 68,690,110**	**$ 65,792,156**
Status of Budgetary Resources		
Obligations incurred		
Direct	$ 66,333,780	$ 63,706,280
Unobligated balances		
Apportioned	367,800	325,307
Unobligated balances not available	1,988,530	1,760,569
Total status of budgetary resources	$ **68,690,110**	**$ 65,792,156**
Change in Obligated Balance		
Obligated balance, net		
Unpaid obligations, brought forward, October 1	$ 8,825,254	$ 8,642,189
Obligations incurred, net	66,333,780	63,706,280
Gross outlays	(64,005,089)	(62,961,322)
Recoveries of prior year unpaid obligations, actual	(588,194)	(561,893)
Obligated balance, net, end of period		
Unpaid obligations	10,565,751	8,825,254
Total, unpaid obligated balance, net, end of period	$ 10,565,751	$ 8,825,254
Net Outlays		
Gross outlays	64,005,089	62,961,322
Offsetting collections	(21,622)	(4,113)
Net outlays	**$ 63,983,467**	**$ 62,957,209**

The accompanying notes are an integral part of these statements.

STATEMENT OF CUSTODIAL ACTIVITY

For the Years Ended September 30, 2010 and 2009 (in dollars)

	2010	2009
Revenue Activity		
Sources of cash collections		
Civil penalties	$ 985,372	$ 1,275,568
Miscellaneous receipts	122,970	27,228
Administrative fines	103,669	407,274
Total cash collections	1,212,011	1,710,070
Accrual adjustments	(188,517)	(326,188)
Total custodial revenue (Note 11)	**$ 1,023,494**	**$ 1,383,882**
Disposition Of Collections		
Transferred to U.S. Treasury	$ 1,212,011	$ 1,710,070
Amounts yet to be transferred	(188,517)	(326,188)
Total disposition of collections	**$ 1,023,494**	**$ 1,383,882**
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 of 1971* (FECA), 2 U.S.C. 431 et seq., as amended ("the Act"). The Commission is also responsible for administering the public funding programs (26 U.S.C. §§ 9001-9039) for presidential campaigns and conventions, which include certification and audits of all participating candidates and committees, and enforcement of public funding legislation.

The financial activity presented relates to the execution of the FEC congressionally approved budget. Consistent with Federal Accounting Standards Advisory Board's (FASAB) *Statement of Federal Financial Accounting Concept No. 2, "Entity and Display*," the Presidential Election Campaign Fund is not a reporting entity of the FEC. Financial activity of the fund is budgeted, apportioned, recorded, reported and paid by the U.S. Department of Treasury (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) for the Federal Government 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.

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. Intragovernmental assets and liabilities are those from or to other federal entities. Intragovernmental earned revenues are collections or accruals of revenue from other federal entities and intragovernmental 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 Federal 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. The FEC also has non-entity assets, which primarily consist of receivables from fines and penalties. These custodial collections are not available to the FEC to use in its operations and must be transferred to Treasury.

Fund Balance with Treasury

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

Accounts Receivable

The FEC's accounts receivable represent amounts due from the public for fines and penalties assessed by the FEC and referred to Treasury for collection. The FEC establishes an allowance for the loss on accounts receivable from the public that are deemed uncollectible accounts, which is included in Accounts Receivable, 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. General P&E consists of items that are used by the FEC to support its mission. Depreciation or amortization on these assets is calculated using the straight-line method with no salvage value. Depreciation or amortization begins the day the asset is placed in service. Maintenance, repairs and minor renovations are expensed as incurred. Expenditures that materially increase the value, capacity or useful life of existing assets are capitalized. Refer to Note 5 *General Property and Equipment, Net* for additional details.

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. The FEC has an intragovernmental liability to Treasury for fines, penalties and miscellaneous receipts due from the public but not yet transferred. These funds may not be used to fund FEC operations.

Accounts Payable

Accounts payable consists 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 consists of disbursements in transit recorded by the FEC but not paid by Treasury.

Accrued Payroll and Employer Contribution

Accrued payroll and benefits represent salaries, wages and benefits earned by employees, but not disbursed as of the statement date. Accrued payroll is payable to employees and therefore not classified as intragovernmental. Employer contributions and payroll taxes payable are 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 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*. 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 the *Federal Employee's Compensation Act*. The future workers' compensation estimate was generated by DOL from an application of actuarial procedures developed to estimate the liability for the *Federal Employee's Compensation Act*, 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 and provided a matching contribution. The FEC matches this withholding, and the sum of the withholding and the matching funds are transferred to the CSRS.

For each fiscal year, the Office of Personnel Management (OPM) calculates the Federal 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 Federal 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. The FEC recognized approximately $3,135,000 and $2,406,000, respectively as of September 30, 2010 and 2009, as an imputed cost and related imputed financing source for the difference between the estimated service cost and the contributions made by the FEC and its employees.

FERS contributions made by employer agencies and covered employees are comparable to the Federal 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 1 percent of base pay to their account and matches contributions up to an additional 4 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 and FERS not paid by the FEC is in accordance with *Statement of Federal Financial Accounting Standards (*SFFAS*) No. 5, Accounting for Liabilities of the Federal Government*, and is included in the FEC's financial statements as an imputed financing source.

Commitments and Contingencies

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. SFFAS No. 5 as amended by SFFAS No. 12, contains the criteria for recognition and disclosure of contingent liabilities. A contingency is recognized when a past event or exchange transaction has occurred, a future outflow or other sacrifice of resources is probable, and the future outflow or sacrifice of resources is measurable. A contingency is disclosed where 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.

According to OMB Circular A-136, as revised, in addition to the contingent liabilities required by SFFAS No. 5, the following commitments should be disclosed: 1) an estimate of obligations related to canceled appropriations for which the reporting entity has a contractual commitment for payment; and 2) amounts for contractual arrangements which may require future financial obligations. The FEC does not have commitments related to cancelled appropriations or amounts for contractual arrangements that would require future financial obligations.

Revenues and Other Financing Sources

Annual Appropriation

The FEC received all of its funding through an annual appropriation as provided by Congress.

Imputed Financing Sources

In accordance with OMB Circular A-136, as revised, 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 Statement of Net Cost (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 total of the FEC's expenditures. 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 program that reflects this strategic goal is to administer and enforce the *Federal Election Campaign Act* efficiently and effectively.

Net Position

Net position is the residual difference between asset and liabilities and consists of unexpended appropriations and cumulative results of operations. Unexpended appropriations include the portion of the FEC's appropriations represented by undelivered orders and unobligated balances. 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 cancelled, 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 Treasury 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 GAAP 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 as of September 30, 2010 and September 30, 2009:

	2010	2009
With the Public		
Accounts Receivable – Custodial	$ 15,482	$ 203,999
Total non-entity assets	15,482	203,999
Total entity assets	17,543,571	17,457,604
Total Assets	$ 17,559,053	$ 17,661,603

Note 3 – Fund Balance with Treasury

Fund Balance with Treasury consisted of the following as of September 30, 2010 and September 30, 2009:

	2010	2009
Fund Balance		
Appropriated Funds	$ 12,922,081	$ 10,911,130
Total	$ 12,922,081	$ 10,911,130

Status of Fund Balance with Treasury	2010	2009
Unobligated Balance		
Available	$ 367,800	$ 325,307
Unavailable	1,988,530	1,760,569
Obligated Balance not yet Disbursed	10,565,751	8,825,254
Total	$ 12,922,081	$ 10,911,130

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 unpaid delivered and undelivered orders.

Note 4 – Accounts Receivable, net

All accounts receivable are with the public and consist of the following as of September 30, 2010 and September 30, 2009:

	2010		
	Gross Accounts Receivable	Allowance	Net Accounts Receivable
With the Public			
Fines and Penalties	$ 64,044	$ 48,562	$ 15,482
Total Non-Entity	$ 64,044	$ 48,562	$ 15,482

	2009		
	Gross Accounts Receivable	Allowance	Net Accounts Receivable
With the Public			
Fines and Penalties	$ 297,498	$ 93,499	$ 203,999
Total Non-Entity	$ 297,498	$ 93,499	$ 203,999

Non-Entity receivables consist of civil penalties and administrative fines assessed by the FEC through its enforcement processes or conciliation agreements reached with parties. The 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 Treasury for collection when delinquent. The terms of the agreement between the FEC and the parties establish the conditions for collection.

Effective May 17, 2010, the FEC issued Rules and Regulations, 11 CFR Parts 8 and 111 (Notice 2010-10), for Collection of Administrative Debts; Collection of Debts Arising from Enforcement and Administration of Campaign Finance Laws to implement the *Debt Collection Improvement Act of 1996* ("DCIA"), Public Law 104-134, 110 Stat. 1321-358.

Note 5 – General Property and Equipment, Net

General Property and Equipment (P&E) is reported at acquisition cost. The capitalization threshold is established at $25,000 and a useful life of two 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. 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 the FEC to support its mission. Depreciation or amortization on these assets is calculated using the straight-line method with no salvage value. Depreciation or amortization begins the day 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.

Effective FY 2009, the estimated useful life of assets such as office furniture, office equipment, telecommunications equipment and audio/visual equipment is five years and the estimated useful life of information technology equipment is three years.

The office 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 leasing entity. The 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 office 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. Leasehold improvements are amortized over the lesser of five years or the remaining of the lease term.

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

The general components of capitalized property and equipment, net of accumulated depreciation or amortization, consisted of the following as of September 30, 2010 and September 30, 2009, respectively:

2010

Asset Class	ServiceLife (years)	Acquisition Value	Accumulated Depreciation/ Amortization	Net Book Value
Software	3	$ 13,005,597	$ 9,878,952	$ 3,126,645
Computers and peripherals	3	3,701,260	2,698,103	1,003,157
Furniture	5	852,754	818,878	33,876
Software-in-Development	n/a	457,812	-	457,812
Total		$ 18,017,423	$ 13,395,933	$ 4,621,490

2009

Asset Class	Service Life (years)	Acquisition Value	Accumulated Depreciation/ Amortization	Net Book Value
Software	3	$ 12,969,440	$ 8,015,792	$ 4,953,648
Computers and peripherals	3	3,545,498	2,301,334	1,244,164
Furniture	5	852,754	787,719	65,035
Software-in-Development	n/a	283,627	–	283,627
Total		$ 17,651,319	$ 11,104,845	$ 6,546,474

Note 6 – Liabilities Not Covered By Budgetary Resources

Liabilities Not Covered by Budgetary Resources consisted of the following as of September 30, 2010 and 2009:

Liabilities Not Covered by Budgetary Resources	**2010**	**2009**
Intragovernmental		
Custodial Fines and Civil Penalties	$ 15,482	$ 203,999
Deferred Rent	609,419	696,479
Total Intragovernmental	$ 624,901	$ 900,478
With the Public:		
Unfunded Annual Leave	2,516,625	2,514,822
Contingent Liability	60,110	-
FECA Liability	3,724	3,208
Total Liabilities Not Covered by Budgetary Resources	$ 3,205,360	$ 3,418,508
Total Liabilities Covered by Budgetary Resources	4,517,680	3,768,080
Total Liabilities	$ 7,723,040	$ 7,186,588

The FEC accrues a liability related to the *Federal Employee's Compensation Act* as of September 30, 2010 and September 30, 2009.

Beginning FY 2008, the FEC entered into a new lease agreement for its office building that provided a rent abatement of $870,598, which covers the equivalent of 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 ten-year lease.

Note 7 – Commitments and Contingencies

As of September 30, 2010, the FEC had a contingent liability in the amount of $60,110 as the result of an arbitrator's award of attorneys' fees. In FY 2011, the FEC will pay the amount awarded.

Note 8 – Leases

The FEC did not have any capital leases as of September 30, 2010 or 2009. The FEC has a commitment under an operating lease for its office space. Future payments due under the lease through September 30, 2017 are:

Future Operating Lease Payments

2010			2009		
Fiscal Year	**Lease Payment**		**Fiscal Year**	**Lease Payment**	
2011	$	5,732,526	2010	$	5,755,351
2012		5,793,993	2011		5,818,278
2013		5,857,305	2012		5,883,092
2014		5,922,515	2013		5,949,852
2015		5,989,682	2014		6,018,614
2016 and thereafter		12,188,986	2015 and thereafter		18,489,353
Total	**$**	**41,485,007**	**Total**	**$**	**47,914,540**

In May 2010, the FEC received a billing adjustment which reduced the future payments required under the operating lease.

Note 9 – Statement of Net Cost

The FEC's costs are consolidated into one program, "Administering the FECA," and consisted of the following as of September 30, 2010 and September 30, 2009, respectively:

	2010	2009
Intragovernmental gross costs	$ 17,997,548	$ 9,328,231
Intragovernmental net costs	17,997,548	9,328,231
Gross costs with the public	51,771,214	57,498,500
Net costs with the public	51,771,214	57,498,500
Net Cost of Operations	$ 69,768,762	$ 66,826,731

Costs incurred for goods and services provided by other federal entities are reported in the full costs of the FEC's program and for FY 2010 employer benefits for payroll, excluding TSP, were included in the intragovernmental gross costs.

Note 10 – Statement of Budgetary Resources

The Statement of Budgetary Resources (SBR) compares budgetary resources with the status of those resources. For the year ended September 30, 2010, budgetary resources were $68,690,110 and net outlays were $63,983,467. For the year ended September 30, 2009, budgetary resources were $65,792,156 and net outlays were $62,957,209.

Apportionment Categories of Obligations Incurred

The FEC receives apportionments of its resources from OMB. Apportionments are for resources that can be obligated without restriction, other than to be in compliance with legislation for which the resources were made available.

For the years ended September 30, 2010 and 2009, direct obligations incurred amounted to $66,333,780 and $63,706,280, 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 2010 actual budgetary execution information is scheduled for publication in February 2011, 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 2009 SBR and the related President's Budget reflected the following:

2009	Budgetary Resources	Obligations Incurred	Distributed Offsetting Receipts	Net Outlays
Statement of Budgetary Resources	$ 65,792,156	$ 63,706,280	–	$ 62,957,209
Budget of the United States Government	64,000,000	63,000,000	–	63,000,000
Difference	$ 1,792,156	$ 706,280	$ –	$ (42,791)

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

Note 11 – Custodial Revenues and Liability

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

Custodial Revenue	**2010**	**2009**
Fines, Penalties and Other Miscellaneous Revenue	$ 1,023,494	$ 1,383,882
Custodial Liability		
Receivable for Fines and Penalties	$ 64,044	$ 297,498
Less: Allowance for Doubtful Accounts	(48,562)	(93,499)
Total Custodial Liability	$ 15,482	$ 203,999

The Custodial Liability account represents the amount of custodial revenue pending transfer to Treasury. Accrual adjustments reflected on the Statement of Custodial Activity represent the difference between the FEC's opening and closing accounts receivable balances. Accounts receivable are the funds owed to the FEC (as a custodian) and ultimately to Treasury. The accrual adjustment for civil penalties is comprised of a net decrease of approximately $168,000 and $332,000 of custodial activities for FY 2010 and FY 2009, respectively. The accrual adjustment for administrative fines is comprised of a net decrease of approximately $21,000 in FY 2010 and a net increase of approximately $6,000 in custodial activity for FY 2009, respectively.

Note 12 – Undelivered Orders at the End of the Period

Undelivered orders as of September 30, 2010 and September 30, 2009 totaled $6,048,071 and $5,057,173, 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.

	2010	2009
Resources used to finance activities:		
Budgetary resources obligated		
Obligations incurred	$ 66,333,780	$ 63,706,280
Less: Recoveries and offsetting collections	(609,815)	(566,007)
Net obligations	65,723,965	63,140,273
Other resources		
Imputed financing from costs absorbed by others	3,135,342	2,406,186
Total resources used to finance activities	68,859,307	65,546,459
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	990,898	154,952
Resources that fund expenses recognized in prior periods	87,060	86,565
Resources that finance the acquisition of assets but do not affect cost of operations	932,138	1,526,773
Total resources used to finance items not part of the net cost of operations	2,010,096	1,768,290
Total resources used to finance the net cost of operations	66,849,211	63,778,169
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 liability	1,803	353,550
Other	60,627	–
Total	62,430	353,550
Components not requiring or generating resources		
Depreciation and amortization	2,589,436	2,517,816
Revaluation of assets or liabilities	267,685	177,196
Total	2,857,121	2,695,012
Total components of the net cost of operations that will not require or generate resources in the current period	2,919,551	3,048,562
Net cost of operations	$ 69,768,762	$ 66,826,731

SECTION IV

OTHER ACCOMPANYING INFORMATION

FEDERAL ELECTION COMMISSION
WASHINGTON, D.C. 20463
Office of Inspector General

MEMORANDUM

TO: The Commission

FROM: Inspector General

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

DATE: October 14, 2010

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 (FEC). 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) 2010.*

The Inspector General has identified three management and performance challenges for inclusion in the FEC's FY 2010 PAR:

Governance Framework
Human Capital Management
Information Technology Security

The Inspector General first identified information technology security as a challenge in 2004, the first year the Inspector General prepared a report of this kind. In 2005, human capital management was added, and in 2008, governance framework was also identified as a challenge for the FEC. In all three cases, these areas have continued to be challenges each year. While the FEC has made some progress in addressing these areas, there still needs to be a considerable amount of progress before these issues are no longer considered challenges.

In addition, since the first FEC PAR released in FY 2004, the Inspector General (IG) has identified *Financial Reporting* as a management challenge. From FY 2004 to the present, the FEC has made continuous improvements to address the many challenges the agency has faced with financial reporting.

Among the FEC's accomplishments in financial management are the following:

- revised the Statement of Net Cost to clearly reflect the FEC's strategic plan;
- reorganized the FEC reporting structure to have the CFO report directly to the Commission;
- restructured staff of the Office of the CFO (OCFO) -
  - filled the financial systems analyst vacancy,
  - elevated accounting technicians to financial analyst positions,
  - cross-trained staff;
- implemented and revised OCFO policies and procedures; and
- migrated to a Financial Management Line of Business (FMLoB) with the General Services Administration to help address the lack of a non-integrated financial management system and assist in financial reporting.

Although all financial management weaknesses have not been fully addressed, the IG acknowledges that the FEC has made significant progress to address the many challenges in this area since FY 2004. Based on the FEC's progress and achievements over the last seven years, the IG has concluded that *Financial Reporting* is no longer a management challenge for FY 2010.

The Inspector General's annual assessment of management and performance challenges 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 15, 2010.

Lynne A. McFarland

Lynne A. McFarland
Inspector General

Attachment

Cc: Alec Palmer, Acting Staff Director/Chief Information Officer
Christopher Hughey, Acting General Counsel
Mary G. Sprague, Chief Financial Officer
Judy McLaughlin, Director Office of Human Resources

GOVERNANCE FRAMEWORK

The Inspector General first reported *Governance Framework* as a management challenge in the 2008 Performance and Accountability Report (PAR). The 2008 PAR documented the agency's challenge to recruit and retain staff in key senior leadership positions; this continues to be a challenge and is discussed in more detail in the *Human Capital Management* challenge that follows.

In addition, the 2008 PAR challenge also highlighted the need to develop and implement a strategic plan to effectively govern the agency and ensure compliance with guidance issued by the Office of Management and Budget (OMB) and other federal agencies. The 2009 PAR further elaborated on the agency's challenge to create a strong governance framework that clearly links the organizational goals to individual performance plans, as well as adequately measure performance and report results. Both of these areas continue to be challenges for the FEC.

The agency has made progress establishing cross-organizational workgroups aimed at improving the FEC's governance framework. For instance, in fiscal year (FY) 2010:

- Several employees from each business area participated in continuity of operations and disaster recovery planning (COOP/DRP). During the initial business impact assessments phase, facilitated by a contractor and supervised by the FEC's Information Technology Division (ITD), each business area defined critical and essential business processes in order to plan recovery efforts in the event of a disaster. Using the impact assessments, each business area can document continuity of operations plans. Once completed, the plans of each business area form the COOP for the entire agency, which is scheduled to be finalized in November 2010.

- The agency contracted to have an enterprise content management (ECM) system study performed. ECM is a strategy for managing documents, images, email, forms and other information, improving collaboration, and enabling compliance with external laws and regulations, as well as internal policies and procedures. During the study, staff from each division met with the contractor and completed a detailed inventory of their enterprise content such as critical systems, forms, documents, and other work products, as well as an assessment of information management needs and cross-organizational information dependencies. The contractor reported fourteen findings and made eight high-level recommendations to begin addressing the findings.

- The FEC recently transferred records management responsibilities to the Office of the Commission Secretary. The Commission elevated the role of Records Officer to a more senior position in the agency in order to address known program weaknesses and ensure whole of organization compliance with the *Federal Records Act of 1950*, as amended. The new Records Officer has taken steps to obtain program information from the Office of Inspector General, support from the agency's National Archives and Records Administration representative, and conducted outreach with FEC divisions. These efforts were taken to obtain a thorough understanding of the program status before implementing a plan to ensure the agency has adequate systems, processes, monitoring and reporting to comply with the Records Act.

- The FEC recently released Directive 69, *FEC Directive on Legal Guidance to the Office of Compliance*. The directive codifies previous internal operating procedures included in the Audit Division's audit programs and formalizes additional procedures. The directive includes date driven deadlines for the Office of General Counsel (OGC) to respond to legal guidance requests from the Office of Compliance. By defining the internal service delivery standard in a directive and including a requirement for monthly status reporting by both the OGC and the Office of Compliance, the Commission implemented an example of a governance framework structure that promotes accurate and transparent performance reporting and holds divisions accountable for the performance results.

The examples listed are noteworthy first steps towards improving governance, organizational efficiency and ensuring compliance with laws and regulations. Some of the projects are significant and may require several years for full implementation, and afterwards the projects will require continuous monitoring. For the items listed, management has acknowledged the various operational risks, determined the resources required and assigned responsibility for progressing improved business processes. Management has also obtained cross-organizational input and recognized that each business area or division must participate in order to achieve the desired results for the agency as a whole. At this point in time, the items listed are projects and not yet components of a strong governance framework. The governance framework will not be completely established until the project outcomes are fully defined, performance standards are established, the results are monitored and reported, and FEC employees are held accountable for program performance.

Despite the progress noted above, there are still weaknesses in the agency's governance framework. For instance, in 2007 the Commission rescinded many policy directives and has not yet replaced them with new guidance for agency staff. In addition, policies for human resource management are not adequately kept up to date and are not widely distributed to all FEC staff when finalized. Further, we have stated in follow-up audits that agency management does not comply with FEC Directive 50, *Audit Follow-Up, April 20, 2006*. As a result, audit recommendations are not implemented timely and the list of outstanding recommendations continuously increases. The agency still lacks detailed business plans for the various offices with clear performance measures, and improvements are necessary to adequately define and monitor employee performance. The OIG believes the Commission has made progress over the last year on improving the governance framework, however, a continued emphasis on strategic planning, accountability, and correcting identified weaknesses are critical to ensuring sustained progress.

HUMAN CAPITAL MANAGEMENT

This past year has again been a period of instability with respect to obtaining and retaining staff in key leadership positions at the FEC. The former Staff Director officially left in October 2009 and the Commission has not named a permanent replacement. Instead, the Chief Information Officer has acted as the Staff Director since August 2009, while still managing the Information Technology Division. In addition, recently the agency's General Counsel and the Associate General Counsel for Enforcement resigned. After an extended vacancy, the Acting Staff Director has recently been working to fill the position of Deputy Staff Director for Planning and Administration, a position which has not been permanently staffed since July 2008. The Commission plans to recruit for a permanent Equal Employment Opportunity (EEO) Officer soon, a position that has been filled with "acting" officers since February 2008.

The Office of Human Resources (OHR) and Labor Relations is vital to ensuring a human capital management framework is developed and implemented at the Commission, and that the framework supports the agency's overall goals and objectives. The Commission's OHR, however, has experienced a high staff turnover in the past year. The OHR Director and four other OHR staff left in February 2010, as did the agency's Administrative Services Manager. Since that time, another senior OHR staff member resigned resulting in a 75% turnover in OHR staff in the last nine months. The Commission has filled vacant OHR positions with experienced staff, however it begins fiscal year (FY) 2011 in the exact position as FY 2008 with essentially a new team of OHR staff working to address a long list of projects and programs aimed at improving human capital management at the Commission.

In June 2009, the Office of Personnel Management (OPM) performed an evaluation of the Commission's Human Capital Management. The review encompassed the five areas of Human Capital Assessment and Accountability Framework (HCAAF): Strategic Alignment; Leadership/Knowledge Management; Results Oriented Performance Culture; Talent Management; and Accountability. In November 2009, OPM provided a final report to the Commission, and the new Director of OHR plans to use the results of the OPM review, as well as the Transit Benefit Follow-up Audit performed by the Office of the Inspector General, to address known program weaknesses. Using corrective action plans (CAPs) developed as a result of the review and audit, the Director of OHR has begun delegating responsibility for implementing recommendations to various OHR members and will include performance goals in OHR staff performance plans to ensure transparency and accountability.

According to the OHR Director, in addition to addressing outstanding audit recommendations, the primary goal of OHR staff in the coming year will be to provide high quality and personally accountable OHR services to Commission employees. Currently, the OHR lacks redundancy among its staff that is necessary to provide efficient and effective customer service to Commission employees. In order to improve customer service, the new OHR Director intends to use a hybrid approach of the generalist and specialist models: OHR will maintain specialists who are experts in their respective service areas, and these specialists will be cross-trained to provide support for other service areas within OHR. While not yet finalized, performance plans for all OHR staff are being developed to ensure they are held accountable for improving customer service and addressing prior audit findings. Once performance plans are finalized, OHR staff will have clearly defined performance standards and measures to ensure they can be rated on customer service quality.

The OIG recognizes that the OHR has both challenges and opportunities related to the large turnover in staff during the prior fiscal year. We encourage the OHR team to harness the opportunities provided by the "clean slate" of new staff to improve customer service and create a comprehensive and effective human capital management system for the agency. OHR should review the status of existing human capital programs and perform assessments to determine whether the initiatives are providing the expected benefits to the agency. We strongly encourage the OHR team to evaluate, revise if necessary, and finalize the agency's Strategic Human Capital Plan. Many internal and external resources are available to assist the OHR as it begins the process of building the foundation for strong human capital management at the Commission: OPM; the Small Agency Council; the Chief Human Capital Officers Council; human capital staff in other agencies; the agency's Personnel Committee; FEC division management and staff; and the OIG. OHR should use all available internal and external resources to ensure quality customer service for Commission employees and correct existing human capital framework weaknesses.

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. The Government Accountability Office (GAO) releases a *High Risk List* every two years to identify the high risk areas that exist government-wide. Since 1997, GAO's *High Risk List* has identified "Protecting the Federal Government's Information Systems" as a risk related to many government agencies. GAO has cited the underlying cause for this weakness in IT security controls is that agencies have not fully or effectively implemented agency-wide information security programs. An agency-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. The program should also represent the foundation for an entity's security control structure and a reflection of senior management's commitment to addressing security risks.

Although the FEC continues to make progress in addressing the agency's IT security challenges, controls still require improvement and strengthening. As reported by GAO in 2009, 21 of the 24 major federal agencies had weaknesses in their agency-wide information security programs. Currently, the FEC shares some of the same weaknesses that were identified by GAO in these major federal agencies. GAO has stated that monitoring and evaluating policy and controls effectiveness is one of the key elements to implementing an agency-wide information security program.

The FEC has taken important steps to establish and implement an effective information security program, such as:

- completing a certification and accreditation for the general support system to provide a form of quality control;
- implementing a framework of policies and standards to mitigate risks associated with the management of its information resources; and
- contracting with a vendor to complete a risk assessment and analysis of FEC security controls.

Although the IG recognizes the progress in IT security, steps still need to be taken to ensure that the FEC has a complete and robust security program. The FEC continues to experience weaknesses relating to their continuous monitoring program. Specifically, the security scanning for vulnerabilities and security weaknesses does not currently include individual workstations that are part of the general support system. Although weaknesses remain in the monitoring program, there has been some progress in this area in 2009. For example, the FEC has strengthened their monitoring program by (1) establishing an alert system for FEC's general support system audit logs to notify key officials of inappropriate or suspicious activity and (2) network scanning for vulnerabilities has increased; however, the continuous monitoring program still has room for improvement.

Further, the FEC's corrective action plan (CAP) to address the weaknesses in access controls has been delayed on several occasions. The expected completion date provided by FEC in their 2009 CAP was mid-year fiscal year 2010. The OIG acknowledges the progress that FEC has made by purchasing software in October 2009 to assist the agency in addressing the reported weakness; however, the full implementation of formal access control policies and procedures still remains incomplete.

The FEC also has weaknesses in their control processes for terminating access authorities and providing security awareness training. The independent public accountants (IPA) review and testing for the 2010 financial statement audit identified several instances in which the FEC did not disable network access for separated employees in a timely manner. In addition, the IPA identified instances where employees did not receive security awareness training in a timely manner; in some cases the training was never completed by the FEC employee. FEC has stated that they will make the necessary adjustments to strengthen these control processes; however, corrective action and continuous monitoring is needed to fully correct the weaknesses identified.

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 OIG 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 NIST, the OIG 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 ensure that the agency's vital operations are safe and secure according to government standards.

APPENDIX

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
CIO	Chief Information 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

91

GAAP	Generally Accepted Accounting Principles
GAO	Government Accountability Office
GPRA	Government Performance and Results Act
GSA	General Services Administration
HLOGA	Honest Leadership and Open Government Act
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
NFC	U. S. Department of Agriculture National Finance Center
NIST	National Institute of Standards and Technology
NPRM	Notices of Proposed Rulemaking
OCFO	Office of the Chief Financial Officer
OCIO	Office of the Chief Information Officer
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
SHCP	Strategic Human Capital Plan
SNC	Statement of Net Cost
SOF	Statement of Financing
TSP	Thrift Savings Plan
USC	United States Code