



**U.S. SECURITIES AND EXCHANGE COMMISSION**  
FY 2011 Performance and Accountability Report



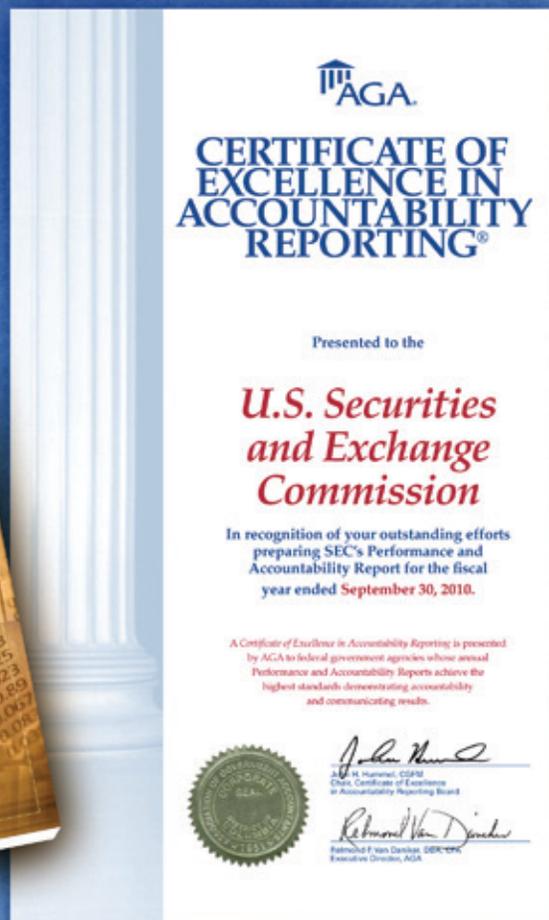
## About This Report

The U.S. Securities and Exchange Commission's (SEC) FY 2011 Performance and Accountability Report provides program performance and financial information that enables Congress, the President, and the public to assess the SEC's performance and accountability over the resources entrusted to it. This report, available at <http://www.sec.gov/about/secpar2011.shtml> provides information that satisfies requirements contained in the following statutes:

- Accountability of Tax Dollars Act of 2002
- Improper Payments Information Act of 2002, as amended
- Reports Consolidation Act of 2000
- Government Management Reform Act of 1994
- GPRA Modernization Act of 2010
- Federal Managers Financial Integrity Act of 1982
- Dodd-Frank Wall Street Reform and Consumer Protection Act Subtitle F. Sec. 963. Annual Financial Controls Audit and Sec. 922. Whistleblower Protection



For the fifth year in a row, the SEC received a Certificate of Excellence in Accountability Reporting from the Association of Government Accountants. The award is presented to Federal Government agencies whose annual reports achieve the highest standards demonstrating accountability and communicating results.



# Contents

---

<b>Message from the Chairman</b> .....	<b>2</b>
<b>Management's Discussion and Analysis</b> .....	<b>5</b>
Vision, Mission, Values and Goals	6
History and Purpose	7
Organizational Structure and Resources	8
FY 2011 Year in Review	12
Looking Forward	28
Financial Highlights	32
Performance Highlights	38
Strategic and Performance Planning Framework	38
Performance Measures Overview	39
Performance Results Summary	40
Management Assurances	45
Annual Assurance Statement	45
<b>Performance Section</b> .....	<b>51</b>
A Reader's Guide to the SEC's Performance Information	52
Verification and Validation of Performance Data	53
FY 2011 Performance Summary by Strategic Goal	53
Program Assessments and Evaluations	95
<b>Financial Section</b> .....	<b>101</b>
Message from the Chief Financial Officer	102
Report of Independent Auditors	104
Management's Response to Audit Opinion	121
Financial Statements	124
Notes to the Financial Statements	129
Required Supplementary Information (Unaudited)	155
Investor Protection Fund Financial Statements	158
Notes to the Investor Protection Fund Financial Statements	161
<b>Other Accompanying Information</b> .....	<b>167</b>
Inspector General's Statement on Management and Performance Challenges	168
Management's Response to Inspector General's Statement	175
Summary of Financial Statement Audit and Management Assurances	183
Improper Payments Elimination and Recovery Act Reporting Details	184
<b>Appendixes</b> .....	<b>186</b>
Appendix A: Chairman and Commissioners	186
Appendix B: Major Enforcement Cases	189
Appendix C: SEC Divisions and Offices	204
Appendix D: Acronyms	206

**Available on the Web at <http://www.sec.gov/about/secpar2011.shtml>**

To contact the SEC, please see <http://www.sec.gov> or "Contact Us" at <http://www.sec.gov/contact.shtml>.

For further information on selected terms and topics, please see "Fast Answers" at <http://www.sec.gov/answers.shtml>.

## Message from the Chairman



The United States Securities and Exchange Commission is charged with protecting investors; maintaining fair, orderly, and efficient markets; and facilitating capital formation. During fiscal year 2011, the SEC improved its ability to carry out this mission by making significant progress against a broad program of needed change. We brought

greater energy and sophistication to core agency functions; began implementing far-reaching and complex financial reform legislation; advanced an investor-focused agenda rooted in the agency's unique expertise; and improved the productivity of our 3,800-member staff.

Despite funding constraints, SEC staff worked diligently to build an agency whose ability to support capital markets and protect investors large and small continued to improve. SEC staff performed traditional oversight and enforcement tasks with an increased efficacy derived from improved technology, increasing levels of staff expertise, innovative management strategies and a more effective organizational structure.

In the Division of Enforcement, new specialized units continued to build expertise in complex, high-priority areas, including asset management, structured and new products, complex trading strategies and current market structure. Complementing this new organization was the increasing use of sophisticated analytic tools and data-based templates that identify suspicious patterns and activities, allowing Enforcement to more quickly identify and pursue unlawful conduct. Enforcement also strengthened and improved its coordination with the Office of Compliance Inspections and Examinations' (OCIE's) National Examination Program (NEP), resulting in targeted exam and investigation efforts

that brought swift enforcement action. And regional offices continued to play a key role in the development of specialized skills and innovative approaches that help the agency identify and promptly investigate possible violations in key areas such as asset valuation, microcap fraud, and cross-border misconduct.

These changes resulted in significant victories for the agency. In 2011, the SEC filed 735 enforcement actions, an 8.6 percent increase from 2010 and more cases than ever previously filed by the Division in a single fiscal year. Eighty-five of those actions were designated National Priority Cases – cases with the greatest significance and highest impact – an increase of 80 percent from 2010. In addition, in the last two fiscal years, the Commission distributed over \$3.6 billion in disgorgement and penalties to harmed investors.

In 2011, the Division of Enforcement continued to work with criminal prosecutors to break up one of the largest insider trading schemes ever uncovered. To date, five separate Federal district court actions have been filed, involving charges against 22 individuals, including high-ranking corporate executives and hedge fund managers, and against seven entities involved in the scheme.

In addition, the SEC continued to bring actions stemming from misconduct related to the financial crisis. To date, the Division of Enforcement has filed 36 actions in financial crisis-related cases, charging 81 individuals and entities. Nearly half of the individuals charged were CEOs, CFOs and senior officers. Fifteen of those actions were filed in 2011, a 25 percent increase over 2010. In connection with these actions, the Commission has barred twenty-four individuals from the industry, from serving as officers and directors, and/or from appearing before the Commission. In addition, \$1.97 billion in penalties, disgorgement and other monetary relief has been ordered, most of which has been or will be returned to harmed investors.

The benefits of OCIE's 2010 restructuring and the creation of its NEP became clear in 2011, the first full year in which both were in place. The NEP has improved OCIE's ability to assess and evaluate risk, allowing the SEC to better monitor systemically relevant institutions; aiding registrants in their compliance efforts; and guiding OCIE as it targets examination of high-risk entities. In addition, the NEP has improved the quality of examinations through more effective training and hiring and new tools that streamline the examination process.

OCIE also contributed to the agency's rulemaking process, building on its role as the SEC's "eyes and ears" in the field to bring a front-line perspective to rulemakings affecting a broad mix of agency priorities.

Other offices and divisions within the SEC focused forcefully and effectively on oversight and rulemakings in support of the agency's investor protection and market stability initiatives. Highlights included:

- Working with self-regulating organizations, the exchanges and the Commodity Futures Trading Commission to address structural weaknesses revealed by the market turmoil on May 6, 2010, and taking steps to reduce excess market volatility going forward.
- Moving to better protect investors against fraud by investment professionals, with proposals to strengthen audits of broker-dealers and oversight of their handling of clients' securities and cash.
- Creating three new offices within the Division of Corporation Finance, concentrating staff focus and agency oversight on portions of the financial markets that showed serious weakness in the financial crisis – including asset-backed securities and the largest financial firms – through rulemaking and enhanced disclosure reviews.
- Increasing scrutiny of registrant disclosure in areas particularly important to contemporary investment decisions, such as liquidity, loss contingencies, and reverse mergers, and improving the quality of disclosed information.
- Creating a cross-agency "college of regulators" to improve oversight of financial service firms and meeting regularly to share information about the regulated firms.
- Recovering over \$240 million for wronged investors from overseas accounts through efforts by the Office of International Affairs, in collaboration with the Division of Enforcement and foreign regulatory and law enforcement bodies.
- Drafting and adopting a large trader reporting rule, designed by the Division of Trading and Markets and the Division of Investment Management, to enhance the agency's ability to identify large market participants, collect information on their trading, and analyze their trading activity – especially in the aftermath of unusual or suspicious activity.

The agency's most significant rulemaking task was implementing many of the SEC-related mandates of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act). This has been a resource-intensive undertaking for the SEC, but one which the Commission has approached with energy and a detailed, cross-agency strategy that has made for steady progress. Of the more than 90 mandatory rulemaking provisions included in the Dodd-Frank Act, the SEC had proposed or adopted rules for three-quarters by the close of FY 2011, and had moved forward on many of the dozens of rules stemming from Dodd-Frank Act provisions that give the SEC discretionary rulemaking authority, as well. Additionally, the SEC had issued 12 of the more than 20 studies and reports that it is required to complete under the Act.

Importantly, each rulemaking or report has been informed by a determined effort to gather criticism, insight, and ideas from a broad range of market participants. The SEC has convened stakeholders for a series of roundtables on key rulemakings, senior staff have met with hundreds of individuals representing investors, industry groups, affected businesses and academics, and thousands of comments have been received and analyzed at the agency's highest levels.

The result has been a series of proposals and rules that balance the goals of protection and stability against the imperatives of complex, dynamic and highly-integrated financial markets. A new whistleblower program created in response to Dodd-Frank Act requirements, for example, was designed to complement, rather than replace, existing corporate compliance programs. While it provides incentives for insiders and others with information about unlawful conduct to come forward, it also encourages them to first attempt to work within their company's own compliance structure.

In response to Dodd-Frank Act requirements, the agency has worked to implement new rules regarding key areas of the financial markets that were not appropriately regulated prior to the recent crisis.

- The SEC is working with the Commodity Futures Trading Commission to develop the regulatory blueprint and requirements for a transparent, efficient and competitive marketplace for over-the-counter swaps and derivatives.
- Information about the identities, size, gatekeepers and disciplinary history of hedge fund and other private fund advisers was made available to both regulators and the investing public, enabling more efficient investing and more effective oversight.
- The SEC proposed rules that will improve the integrity of the process which yielded so many flawed ratings of subprime mortgage products, by increasing transparency of the rating process and of the agencies that produce ratings, and by protecting against conflicts of interest when entities or individuals provide ratings for their clients.

These are just a few of the areas in which the SEC is turning the legislative language of the Dodd-Frank Act into effective and intelligent regulation.

I am also pleased to report that the SEC has succeeded in its remediation efforts and has no material weaknesses in its internal controls over financial reporting. The SEC's independent auditor, the U.S. Government Accountability Office, also affirms that the SEC's financial statements are presented fairly in all material respects, in conformity with the U.S. generally accepted accounting principles (U.S. GAAP). Finally, based on our review, we can confirm that the financial and performance data presented in this report are fundamentally complete, reliable, and conform to Office of Management and Budget guidance.

The SEC's many different actions and initiatives come together in service of a single, unifying principle: Investors who fuel America's capital markets and growing businesses must be confident that those markets are fair, orderly and fully transparent. We hope that the information contained in this report provides readers with a full understanding of the activities and challenges of the SEC in 2011 – a year that saw the SEC take great strides in a number of vital areas, and set the stage for continued progress in 2012.



**Mary L. Schapiro**

Chairman

November 15, 2011

# MANAGEMENT'S DISCUSSION AND ANALYSIS



**T**he U.S. Securities and Exchange Commission's (SEC) Management's Discussion and Analysis (MD&A) serves as a brief overview of this entire report. It provides a concise description of the agency's performance measures, financial statements, systems and controls, compliance with laws and regulations, and actions taken or planned. It also provides an assessment of the SEC's programs and financial performance, and the efficiency and effectiveness of the SEC's operations.

## Vision, Mission, Values and Goals

### Vision

The SEC strives to promote a market environment that is worthy of the public's trust and characterized by transparency and integrity.

### Mission

The mission of the SEC is to protect investors; maintain fair, orderly, and efficient markets; and facilitate capital formation.

### Values

Integrity	Teamwork
Accountability	Fairness
Effectiveness	Commitment to Excellence

*In order to comply with the GPRA Modernization Act of 2010, the SEC is developing an addendum to the fiscal year (FY) 2010 - FY 2015 Strategic Plan. The addendum will reflect the agency's mission, vision, values, and strategic goals through FY 2014, and highlight specific initiatives the agency plans to undertake in the coming 24 months. Additionally, the addendum will include an updated performance measurement framework, as well as updates to existing performance measures that will be used to gauge the agency's progress in accomplishing the strategic goals and outcomes. The addendum will be finalized and available on the SEC's website at <http://www.sec.gov> in February 2012.*

## Strategic Goals and Outcomes

### Goal 1: Foster and enforce compliance with the Federal securities laws

- Outcome 1.1:** The SEC fosters compliance with the Federal securities laws.
- Outcome 1.2:** The SEC promptly detects violations of the Federal securities laws.
- Outcome 1.3:** The SEC prosecutes violations of Federal securities laws and holds violators accountable.

### Goal 2: Establish an effective regulatory environment

- Outcome 2.1:** The SEC establishes and maintains a regulatory environment that promotes high-quality disclosure, financial reporting, and governance, and that prevents abusive practices by registrants, financial intermediaries, and other market participants.
- Outcome 2.2:** The U.S. capital markets operate in a fair, efficient, transparent, and competitive manner, fostering capital formation and useful innovation.
- Outcome 2.3:** The SEC adopts and administers rules and regulations that enable market participants to understand clearly their obligations under the securities laws.

### Goal 3: Facilitate access to the information investors need to make informed investment decisions

- Outcome 3.1:** Investors have access to high-quality disclosure materials that are useful to investment decision making.
- Outcome 3.2:** Agency rulemaking and investor education programs are informed by an understanding of the wide range of investor needs.

### Goal 4: Enhance the Commission's performance through effective alignment and management of human, information, and financial capital

- Outcome 4.1:** The SEC maintains a work environment that attracts, engages, and retains a technically proficient and diverse workforce that can excel and meet the dynamic challenges of market oversight.
- Outcome 4.2:** The SEC retains a diverse team of world-class leaders who provide motivation and strategic direction to the SEC workforce.
- Outcome 4.3:** Information within and available to the SEC becomes a Commission-wide shared resource, appropriately protected, that enables a collaborative and knowledge-based working environment.
- Outcome 4.4:** Resource decisions and operations reflect sound financial and risk management principles.

## History and Purpose

---

During the peak of the Depression, Congress passed the Securities Act of 1933. This law, together with the Securities Exchange Act of 1934 (Exchange Act), which created the SEC, was designed to restore investor confidence in our capital markets by providing investors and the markets with more reliable information and clear rules of honest dealing. The main purposes of these laws were to ensure that:

- Companies publicly offering securities for investment dollars must tell the public the truth about their businesses, the securities they are selling, and the risks involved in investing.
- People who sell and trade securities – brokers, dealers and exchanges – must treat investors fairly and honestly, putting investors' interests first.

The SEC consists of five presidentially appointed Commissioners, with staggered five-year terms. One of them is designated by the President as Chairman of the Commission (see Appendix A: Chairman and Commissioners). President Franklin Delano Roosevelt appointed Joseph P. Kennedy, to serve as the first Chairman of the SEC.

By law, no more than three of the Commissioners may belong to the same political party. The Commission convenes regularly at meetings that are open to the public and the news media unless the discussion pertains to confidential subjects, such as whether to begin an enforcement investigation.

Each year the SEC brings hundreds of civil enforcement actions against individuals and companies for violation of securities laws. Examples of infractions include insider trading, accounting fraud, and providing false or misleading information about securities or the companies that issue them. One of the major sources of information that the SEC relies on to bring enforcement action is investors themselves – another reason that educated and careful investors are so critical to the functioning of efficient markets. To help inform investors, the SEC offers the public a wealth of educational information on its website at <http://www.investor.gov>, as well as an online database of disclosure documents at <http://www.sec.gov/edgar> that public companies and other market participants are required to file with the SEC.

## Organizational Structure and Resources

### SEC Office Locations

The SEC's headquarters are in Washington, D.C., and it has 11 regional offices located throughout the country. The regional offices are responsible for investigating and litigating potential violations of the securities laws. The offices also have examination staff, who impact regulated entities such as investment advisers, investment companies and broker-dealers. The map below shows the locations of the regional offices, and the states that are included in each region.

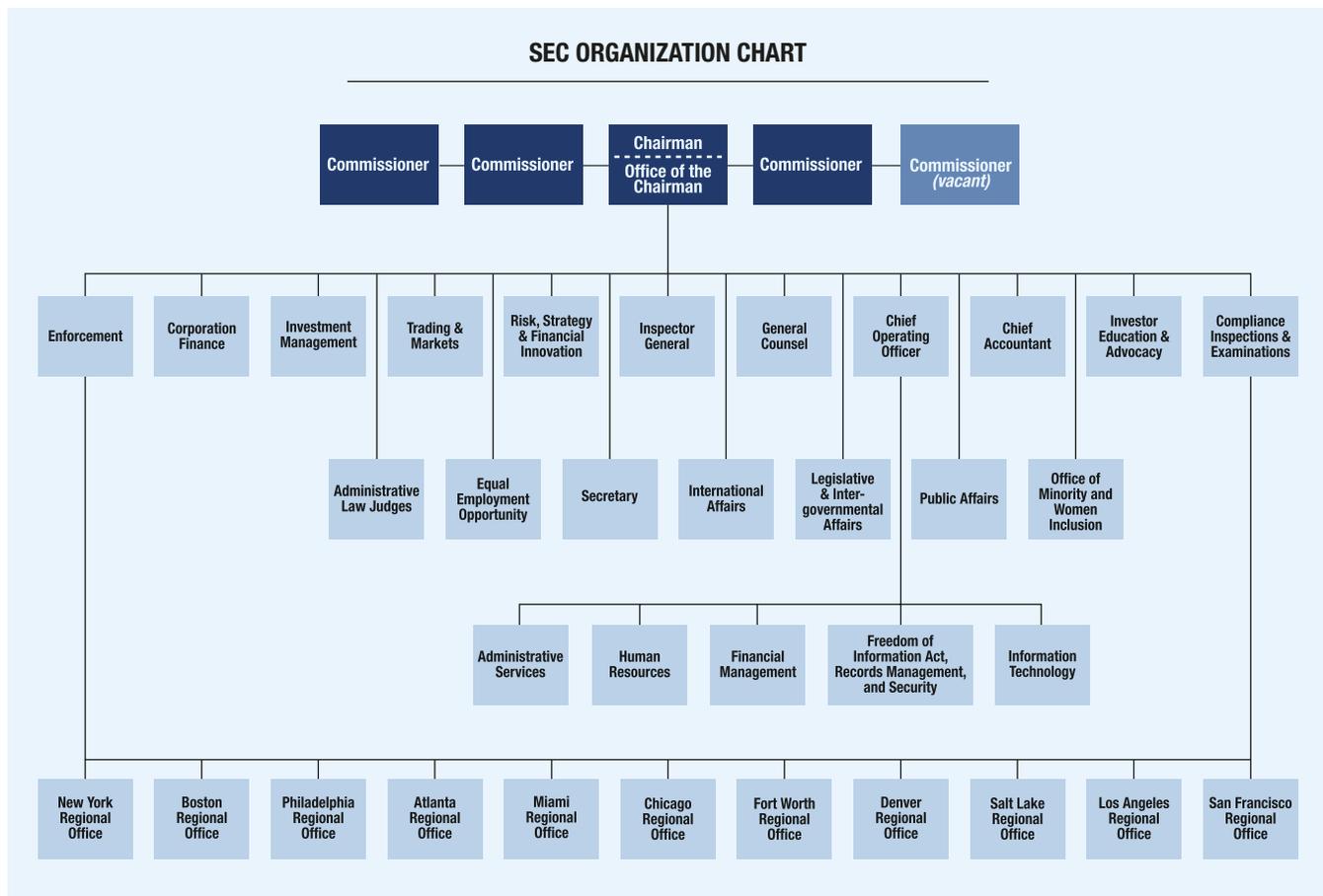
CHART 1.1



## SEC Organization Structure

The SEC is an independent Federal agency established pursuant to the Exchange Act. It is headed by a bipartisan five-member Commission, comprised of the Chairman and four Commissioners, who are appointed by the President and confirmed by the Senate (see *Appendix A: Chairman and Commissioners*). The Chairman serves as the Chief Executive Officer. The SEC is organized into five main divisions: Enforcement; Corporation Finance; Investment Management; Trading and Markets; and Risk, Strategy, and Financial Innovation. In FY 2011, the SEC's budgetary authority amounted to \$1,673 million, consisting of an appropriation for salaries and expenses in the amount of \$1,185 million, carryover balances of \$36 million for the expenses of the agency, and \$452 million in the Investor Protection Fund. In FY 2011, the agency employed 3,844 full-time equivalents (FTE), including 3,806 permanent and 38 temporary FTEs. The below SEC organization chart is as of September 30, 2011.

CHART 1.2



## SEC Programs

The SEC organizes its divisions and offices under the 10 major programs outlined below in *Table 1.1, SEC Programs and Program Descriptions*.

**TABLE 1.1**  
**SEC PROGRAMS AND PROGRAM DESCRIPTIONS**

Program	Divisions and Offices	Program Descriptions
Enforcement	Division of Enforcement and enforcement staff within the SEC's regional offices	This program investigates and brings civil charges in Federal district court or in administrative proceedings based on violations of the Federal securities laws. An integral part of the program's function is to seek penalties and the disgorgement of ill-gotten gains in order to return funds to harmed investors. Also organized within the Enforcement program is the new Office of the Whistleblower, created to administer the SEC's Whistleblower Program that rewards individuals who provide the agency with tips that lead to successful enforcement actions under the Dodd-Frank Act.
Compliance Inspections and Examinations	Office of Compliance Inspections and Examinations and examinations staff within the SEC's regional offices	This program conducts the SEC's examinations of registrants such as investment advisers, investment companies, broker-dealers, self-regulatory organizations (SROs), credit rating agencies, transfer agents, and clearing agencies.
Corporation Finance	Division of Corporation Finance	This program performs functions to assure that investors have access to materially complete and accurate information, and to deter fraud and misrepresentation in the public offering, trading, voting, and tendering of securities.
Trading and Markets	Division of Trading and Markets	This program conducts activities to establish and maintain standards for fair, orderly and efficient markets, while fostering investor protection and confidence in the markets.
Investment Management	Division of Investment Management	This program seeks to minimize the financial risks to investors from fraud, mismanagement, self-dealing, and misleading or incomplete disclosure in the investment company and investment adviser segments of the financial services industry.
Risk, Strategy, and Financial Innovation	Division of Risk, Strategy, and Financial Innovation	The division provides economic analyses as part of Commission's rulemaking process; supports its rule review, examination and enforcement programs with data-driven, risk-based analytical methods; and oversees its Tips, Complaints and Referrals (TCR) and interactive data programs.
General Counsel	Office of the General Counsel	The Office of the General Counsel (OGC) serves as the chief legal officer of the Commission and provides independent legal analysis and advice to the Chairman, Commissioners, and operating divisions on all aspects of the Commission's activities. The General Counsel also defends the Commission in Federal district courts, represents the Commission in all appellate matters and <i>amicus curiae</i> filings, and oversees the SEC's bankruptcy program.
Other Program Offices	<ul style="list-style-type: none"> <li>• Office of the Chief Accountant;</li> <li>• Office of Investor Education and Advocacy;</li> <li>• Office of International Affairs; and</li> <li>• Office of Administrative Law Judges</li> </ul>	<p>These offices are responsible for:</p> <ul style="list-style-type: none"> <li>• serving as the chief advisor to the Commission on all accounting and auditing policy and overseeing private sector standards setting;</li> <li>• serving investors who contact the SEC, ensuring that retail investors' perspectives inform the Commission's regulatory policies and disclosure program, and improving investors' financial literacy;</li> <li>• advancing international regulatory and enforcement cooperation, promoting converged high regulatory standards worldwide, and facilitating technical assistance programs in foreign countries; and</li> <li>• adjudicating allegations of securities law violations.</li> </ul>

(Continued on next page)

**TABLE 1.1** *Continued from previous page*

Program	Divisions and Offices	Program Descriptions
Agency Direction and Administrative Support	<ul style="list-style-type: none"> <li>• The Chairman and Commission;</li> <li>• Office of Legislative and Intergovernmental Affairs;</li> <li>• Office of Public Affairs;</li> <li>• Office of the Secretary;</li> <li>• Office of the Chief Operating Officer;</li> <li>• Office of Information Technology;</li> <li>• Office of Freedom of Information Act, Records Management, and Security;</li> <li>• Office of Financial Management;</li> <li>• Office of the Executive Director<sup>1</sup>;</li> <li>• Office of Human Resources;</li> <li>• Office of Administrative Services;</li> <li>• Office of Equal Employment Opportunity; and</li> <li>• Office of Minority and Women Inclusion</li> </ul>	<p>The Chairman is responsible for overseeing all aspects of agency operations, and the Chairman and Commissioners are responsible for the review and approval of enforcement cases and formal orders of investigation and the development, consideration, and execution of policies and rules. The other offices in Agency Direction and Administrative Support are responsible for:</p> <ul style="list-style-type: none"> <li>• working with Members of Congress on issues that affect the Commission;</li> <li>• coordinating the SEC's communications with the media, the general public, and foreign visitors;</li> <li>• reviewing all documents issued by the Commission, and preparing and maintaining records of Commission actions;</li> <li>• maximizing the use of SEC resources by overseeing the strategic planning, information technology, financial management, records management, human resources, and administrative functions of the agency;</li> <li>• ensuring that the SEC is an equal opportunity employer in full compliance with all Federal equal employment opportunity laws; and</li> <li>• enhancing the diversity of the SEC's workforce, contractors, and regulated entities in accordance with existing Federal laws and regulations.</li> </ul>
Inspector General	Office of Inspector General	<p>The Office of Inspector General (OIG) is an independent office that conducts audits of programs and operations of the SEC and investigations into allegations of misconduct by staff or contractors. The mission of OIG is to detect fraud, waste, and abuse and to promote integrity, economy, efficiency, and effectiveness in the SEC's programs and operations.</p>

As shown in the *Statement of Net Cost*, on page 125, the SEC presents its net costs of operations by the programs outlined above, consistent with the presentation used by the agency in submitting its budget requests. A detailed discussion of program achievements and program contributions to accomplishing the mission of the SEC can be found in the *Performance Section*.

<sup>1</sup> The Office of the Executive Director was eliminated in FY 2011, but the costs of the Office during the early months of the fiscal year are included under Agency Direction and Administrative Support. The Office of the Executive Director was responsible for management of the agency's human resources, budget management, and administrative services functions. When the Office was eliminated, these functions were transferred under the Office of the Chief Operating Officer.

## FY 2011 Year in Review

---

### A More Modern and Effective SEC

In fiscal year 2011, the U.S. Securities and Exchange Commission continued to improve its effectiveness in pursuit of its investor protection and market integrity missions. This progress was the result of an ongoing, comprehensive effort to improve basic agency functions and organization; align regulation, enforcement and oversight strategies and priorities with evolving financial market conditions; and equip the SEC's 3,800 professionals with the tools and training required to perform at the highest level.

Institutional enhancements begun two years ago continued to bear fruit, as a changing culture increased the capacity and improved the performance of the SEC. New hiring and training strategies lifted staff performance while the creation of specialized teams in the enforcement and examination programs helped the agency increase in-house expertise in those areas. Reorganization of key divisions and offices and an increased emphasis on collaboration and intra-agency communication made the SEC more creative and responsive.

Core functions, including examination and enforcement, benefitted from new and upgraded information systems which allowed staff to focus resources on high-risk registrants and to discover suspicious conduct more rapidly. Other divisions and offices looked beyond traditional priorities to identify emerging threats and opportunities within the financial markets, adjusting strategies and priorities to better protect investors and markets in a rapidly-changing environment.

Recognizing the historic significance of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act), the SEC supported its many Dodd-Frank Act-related rulemakings with aggressive efforts to solicit and consider ideas and criticisms from market participants of all types, and to align action with domestic and foreign regulators (with whom the SEC must coordinate policy in order to limit exploitable regulatory inconsistencies).

And the SEC continued to upgrade human resources and back office functions, improving resource allocation, increasing the value of the SEC's human capital, and allowing

staff to focus on the SEC's investor protection and market stability mission – all while capturing savings through further efficiencies in administrative tasks.

It should be noted, however, that savings and efficiencies alone will not free up sufficient resources to allow the SEC to effectively carry out a mission that is expanding significantly as a result of the Dodd-Frank Act.

The SEC is better positioned today than it has been in many years to respond quickly to events and developments in the financial world; to keep regulatory pace with the continuing evolution of the financial markets; and to deter, identify, and pursue wrongdoers. It is important that the agency's funding increases in step with these increasing responsibilities, in order to ensure that investors and markets continue to benefit from the SEC's improving performance.

### Enforcement: A Record Performance

A reorganized Division of Enforcement is collaborating more closely than ever with other SEC offices and increasingly utilizing technology as a way to identify and halt unlawful activity before it occurs or results in additional investor harm. The Division's aggressive strategy sends a clear message that securities law violations will be discovered and punished.

Enforcement's broad focus has meant successful actions against a wide range of unlawful conduct, ranging from fraud committed by large financial institutions whose actions contributed to the financial crisis – including Countrywide Financial, J.P. Morgan, and Wachovia – to smaller frauds that did not generate headlines but nonetheless threatened the savings of vulnerable individuals.

Having completed the most significant restructuring since its establishment almost 40 years ago, Enforcement continued to enhance its effectiveness by focusing resources on the misconduct that most harms investors and markets, by developing risk-based initiatives that anticipate suspicious behavior before a fraud takes hold, and by using the agency's new IT resources to create analytical tools and to process the increasing amounts of data that accompany its investigations.

The Division of Enforcement has built closer ties with the Office of Compliance Inspections and Examinations (OCIE), as well. And, the Division is developing specialized skills and new approaches for investigating possible violations in key areas such as valuation, aberrational performance by hedge funds and investment advisers, and microcap fraud.

These changes have allowed Enforcement to move faster and more strategically to attack securities laws violations, and to achieve record results in the process.

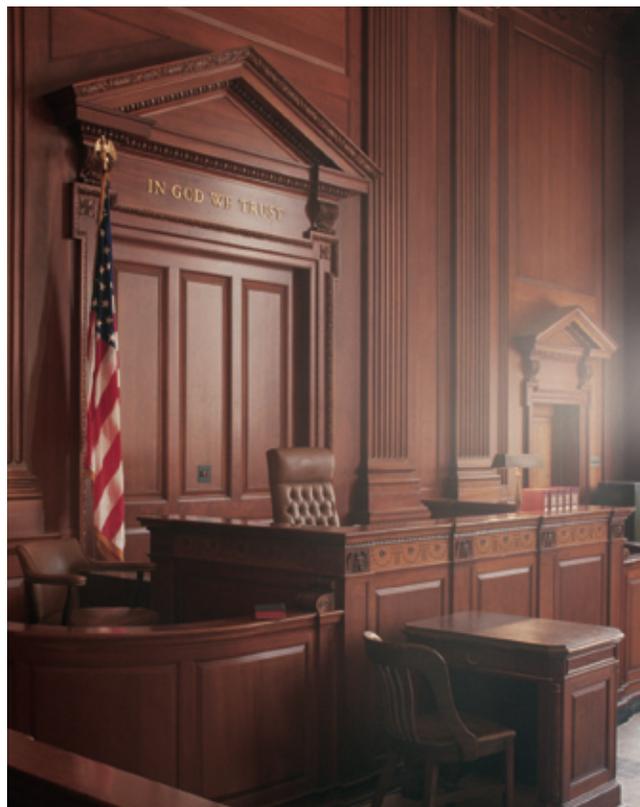
The SEC brought 735 enforcement actions in FY 2011, more than have ever been filed by the Commission in a fiscal year. Eighty-five of those actions were designated National Priority Cases – the Division's most important and complex. In addition to the improvement in the quantity and quality of the filed enforcement actions, the Division obtained orders for \$2.8 billion in penalties and disgorgement; utilized enhanced remedies available under the Dodd-Frank Act to bar numerous wrongdoers from future work in the securities industry; and obtained relief that sent a strong deterrent message, including asset freezes, trading suspensions, and penny stock bars.

A fuller description of Division of Enforcement actions filed in FY 2011 can be found in *Appendix B: Major Enforcement Cases*, but this brief survey conveys the breadth and effectiveness of those efforts:

### Financial Crisis

Since 2008, the SEC has filed 36 actions against 81 individual and corporate defendants alleging a wide range of misconduct arising from the financial crisis. Fifteen of these actions were filed in 2011, up from 12 filed in 2010.

- Among the most significant of these actions was that filed against J.P. Morgan Securities, LLC, for misleading investors in a complex mortgage securities transaction executed just as the housing market was starting to plummet. The SEC charged J.P. Morgan for structuring and marketing a synthetic collateralized debt obligation (CDO) without informing investors that a hedge fund helped select the assets in the CDO portfolio and that the fund had a short position in more than half of those assets. J.P. Morgan settled the SEC's charges by paying \$153.6 million, which represented a full return of losses



to harmed investors. J.P. Morgan also agreed to improve its processes for the review and approval of mortgage securities transactions and to return more than \$56 million to investors who were harmed in a second CDO transaction.

- Countrywide Financial Chief Executive Officer (CEO) Angelo Mozilo agreed to pay a record \$22.5 million penalty to settle SEC charges that he and two other former Countrywide executives failed to disclose to investors the significant credit risk that Countrywide was taking on as it increased its share of the subprime mortgage market. Mozilo was permanently barred from serving as an officer or director of a publicly-traded company and agreed to disgorge \$45 million in ill-gotten gains. A total of \$67.5 million is being returned to harmed investors.
- The SEC settled charges filed previously against Morgan Keegan & Company and Morgan Asset Management, which agreed to pay \$200 million to settle fraud charges. Two Morgan Keegan employees also agreed to pay penalties for their alleged misconduct, including one who is now barred from the securities industry. The Memphis-

based firms, former portfolio manager James C. Kelsoe Jr. and comptroller Joseph Thompson Weller were accused by the SEC of causing the false valuation of subprime mortgage-backed securities in five funds managed by Morgan Asset Management, from January 2007 to July 2007. The SEC's order issued in settling the charges also found that Morgan Keegan failed to employ reasonable pricing procedures and consequently did not calculate accurate "net asset values" (NAV) for the funds. Morgan Keegan nevertheless published the inaccurate daily NAVs and sold shares to investors based on the inflated prices.

- In separate actions, the SEC charged RBC Capital Markets LLC and brokerage firm Stifel, Nicolaus & Co. with defrauding five Wisconsin school districts by selling them unsuitably risky and complex CDO investments. Stifel and former Stifel Senior Vice President David W. Noack were charged with misrepresenting the risk of the investments and failing to disclose material facts to the school districts. The sales took place despite significant concerns within RBC Capital about the suitability of the product for municipalities like the school districts. RBC Capital agreed to settle the SEC's charges by paying a total of \$30.4 million, which will be distributed in varying amounts to the harmed school districts through a Fair Fund. The SEC's case against Stifel, Nicolaus & Co. is continuing.
- The SEC charged Wells Fargo Securities LLC – formerly known as Wachovia Capital Markets LLC – with misconduct by Wachovia in the sale of two CDOs tied to the performance of residential mortgage-backed securities as the housing market was beginning to show signs of distress. The SEC's order found that Wachovia violated securities laws by charging undisclosed excessive markups in the sale of certain interests to investors in one CDO, and by misrepresenting to investors in another CDO the value at which it had acquired assets from affiliates. In settling the action, Wells Fargo agreed to pay more than \$11 million in disgorgement and penalties, most of which will be returned to harmed investors.

## Fraudulent Schemes

Supporting investor confidence in the financial markets means bringing cases not only against major financial firms and their executives, but also against individuals and smaller firms whose misdeeds can steal a lifetime's savings or devastate an investor's future.

- The SEC charged three senior executives at the Akron, Ohio-based Fair Finance Company with orchestrating a \$230 million fraudulent scheme involving at least 5,200 investors – many of them elderly. The SEC alleges that after purchasing Fair Finance Company, Chief Executive Officer Timothy S. Durham, Chairman James F. Cochran, and Chief Financial Officer Rick D. Snow deceived investors, selling interest-bearing certificates whose proceeds were supposed to be used to purchase and service discounted consumer finance contracts. Instead, Durham and Cochran schemed to divert investor proceeds to themselves and others, as well as to struggling and unprofitable entities that they controlled.
- The SEC charged internet-based investment company Imperia Invest IBC with securities fraud and obtained an emergency court order freezing Imperia's assets. The SEC alleged that Imperia solicited several million dollars from U.S. investors and promised them returns of 1.2 percent per day – while in reality siphoning the funds into foreign bank accounts and not paying a single penny back. Imperia allegedly raised more than \$7 million from approximately 14,000 investors worldwide. More than half the funds were collected from U.S. investors who are members of the Deaf community.

## Insider Trading

The Commission has aggressively pursued practices that damage the integrity of financial markets and discourage investors who seek a fair and level playing field. Most notably, the SEC discovered and developed information that ultimately led to criminal convictions for Galleon hedge fund founder Raj Rajaratnam and others, and to Commission charges against 22 individuals – including high-ranking corporate executives and hedge fund managers – and against seven entities involved in the scheme (in November 2011, Rajaratnam was ordered to pay a record \$92.8 million to resolve SEC charges in the case).

There have been other important cases, as well.

- The SEC charged a former Mariner Energy Inc. board member and his son with insider trading on confidential information about an impending takeover of the oil and gas company. Acting on a tip from his father, H. Clayton Peterson, son Drew Clayton Peterson purchased Mariner Energy stock for himself, his relatives, his clients and a close friend in advance of an announcement that Apache Corporation would be acquiring Mariner. Peterson also tipped several other close friends, who traded on the nonpublic information ahead of the April 2010 acquisition announcement. The insider trading by the Petersons and others generated more than \$5.2 million in illicit profits.
- The SEC charged former Nasdaq managing director Donald L. Johnson with insider trading on confidential information he stole while working in two units at Nasdaq that communicated with companies in advance of market-moving public announcements. The SEC alleged that Johnson used the stolen information to trade in the stock of six companies on at least nine occasions, realizing illicit profits of more than \$755,000.
- The SEC charged Cheng Yi Liang, a chemist at the U.S. Food and Drug Administration (FDA), with insider trading on confidential information concerning upcoming announcements of FDA drug approval decisions, generating more than \$3.6 million in illicit profits and avoided losses. Liang illegally traded in advance of 28 public announcements about FDA drug approval decisions, involving 20 publicly-traded companies, for profits and losses avoided totaling over \$3.7 million. In each instance, Liang traded in the same direction as the announcement. Liang went to great lengths to conceal his insider trading, including trading in multiple accounts, none of which were in his name.

### **Municipal Securities**

The SEC focused increased attention on the lightly-regulated municipal securities market, in which well-connected individuals and firms use influence and collusion to win lucrative fund management contracts or otherwise short-change the municipalities whose interests they are supposed to be serving.

- In a series of cases, the SEC charged J.P. Morgan Securities LLC, UBS Financial Services Inc., and Banc of America Securities, LLC with rigging more than 200 municipal bond re-investment transactions, generating tens of millions of dollars in ill-gotten gains. Together, the settlements of these three cases resulted in the return of \$134 million to harmed municipalities and conduit borrowers in more than 40 states. In addition, the companies paid a total of \$391 million to settle parallel cases brought by other Federal and state authorities.

### **Misleading Investors**

The SEC continued its vigilant enforcement of regulations regarding entities such as mutual funds, investment advisers, and broker-dealers who are entrusted with a significant portion of the investing public's assets.

- The Commission charged Charles Schwab Investment Management and Charles Schwab & Co. Inc. with making misleading statements about the Schwab YieldPlus Fund – at one time, the largest ultra-short bond fund. The misleading statements included descriptions of the fund as a cash alternative that offered only slightly higher risk than a money market fund. The fund suffered a significant decline during the credit crisis of 2007 and 2008. The Schwab entities agreed to pay more than \$118 million to settle the SEC's charges. The SEC also charged the responsible Schwab executives, who are currently litigating the SEC's claims.

### **OCIE Referrals**

Increased cooperation with OCIE, which collaborates with Enforcement when its examinations reveal suspicious activity, resulted in several important cases, including the Stifel, Nicolaus & Co case described above.

- Three AXA Rosenberg entities, as well as the co-founder of the firm, Barr Rosenberg, were charged with securities fraud for concealing a significant error in the computer code of the quantitative investment model that they developed and used to manage client assets. AXA Rosenberg agreed to settle the SEC charges by paying \$217 million to cover investor losses, to pay an additional \$25 million penalty and to take other remedial

steps. Separately, Barr Rosenberg agreed to settle the SEC's charges by paying a \$2.5 million penalty and agreeing to be barred from the securities industry.

- The SEC filed an emergency action and obtained emergency relief to halt a multi-million dollar misappropriation of investor assets by registered investment adviser MK Capital Management, LLC and its principal, Francisco Illarramendi. The Commission subsequently amended its complaint to allege that Illarramendi and MK Capital had misappropriated investor assets and misused two hedge funds they managed in a Ponzi scheme involving hundreds of millions of dollars. The SEC obtained a court order freezing the assets of the hedge funds and ordered that all assets of the hedge funds, including \$230 million held in offshore accounts, be repatriated to the United States. Illarramendi was permanently barred by the SEC from serving in the securities industry.

The Division of Enforcement's 2011 performance reinforces what a growing number of individuals and entities are discovering: recent improvements in the Division's structure, expertise, management, technology, and staff capacity are allowing the Commission not only to bring more – and more complex – cases, but to obtain better results on investors' behalf.

## **OCIE: Protecting Investors through More Effective Examinations**

In 2011, OCIE significantly expanded its ability to contribute to the SEC's mission – improving its ability to identify risk and target examinations and resources accordingly, changing structure to more effectively acquire and deploy expertise, and collaborating across the agency to improve both the examination and the rulemaking processes. OCIE's National Exam Program (NEP) anchored this improving performance by weaving a number of key initiatives into a single effective effort.

Collaboration with the Division of Risk, Strategy and Financial Innovation (RSFI) allows the NEP to continuously improve its targeting and risk indicators and to focus exams on registrants that are most likely to merit them. A recently-established Office of Risk Analysis and Surveillance within OCIE guides that targeting strategy across different program areas and

sharpens focus on registrants and practices that pose the greatest risk to investors and market integrity.

As part of its risk assessment efforts, OCIE began developing risk profiles of systemically relevant institutions, including large broker-dealers, clearing agencies and exchanges. OCIE has completed risk profiles of each of the 21 national securities exchanges and self regulatory organizations (SROs), enabling NEP to understand individual risk, and risk among the exchanges as a group. OCIE has audited all ten nationally recognized statistical rating organizations, and publicly reported the findings. OCIE has begun risk-monitoring of clearing agencies and it is moving to develop risk profiles of the largest and most systemically significant broker-dealers.

Continuing improvements in risk-based targeting allow the NEP to extend resources and staffing strained by the continued growth in the number and complexity of the registrants OCIE is charged with examining. Further, specialized groups now focus on complex and high-risk areas of the financial marketplace.

OCIE also is working to extend its capacity by establishing an infrastructure that reflects the SEC's increasingly diverse registrant population, including private fund advisers, credit rating agencies, and quantitative/high-frequency trading advisers.

A major restructuring is underway within OCIE, including the development of specialized working groups (SWGs) in six key areas and over thirty other significant improvement initiatives. The SWGs will serve as forums in which the NEP and other agency staff can collaborate and discuss current issues, initiatives, and concerns related to each specialized area. They will serve as an ongoing resource for training and for disseminating this specialized knowledge, as well.

OCIE is hiring exam staff with industry experience and specialized expertise in targeted areas, and enhancing the resources and tools available to examination staff. These efforts also include new training: OCIE has worked with SEC University to develop targeted training in areas like risk management and on specific topics related to new responsibilities created by the Dodd-Frank Act, such as examining private fund advisers. Development of a new certified examiner program is underway, as well.

The examination process itself has been improved. Once examination targets are identified, an open architecture staffing system allows the NEP to assemble more effective teams by bringing together different combinations of individuals, with varying areas of expertise, to address the unique challenges each examination presents.

OCIE is increasingly collaborating with other organizations, inside and outside the SEC, to improve the quality of examinations and of disclosures made by registered entities. The Office is reaching out to state regulators, local and national law enforcement agencies and – where appropriate – foreign regulators, sharing information and examinations strategies.

Within the SEC, OCIE is collaborating with the Division of Trading and Markets (TM) on examinations of broker-dealers, SROs, and transfer agents. This allows OCIE to identify important areas of focus and has led to TM requests that firms change certain practices. OCIE also teams with the Division of Investment Management (IM) for examinations of various investment funds and their management, collaborating on reviews of money market fund filings and using data provided by IM in its risk assessment of registrants.

Key OCIE actions that led to Division of Enforcement action include:

- Identifying the sale of millions of dollars of micro-cap securities through false and misleading statements, followed by swift action to protect investors' assets, including freezes, trading halts and/or fines. The micro-cap review demonstrates the benefits of OCIE's recently-created specialized groups, one of which focuses on these securities.
- Discovering that a broker was churning two accounts owned by the Sisters of Charity – one account for care of nuns in assisted living facilities and a second supporting the sisters' charitable endeavors – in order to generate excess commissions for the broker.
- Identifying information that led to the charging of Raymond James with misrepresenting and omitting material information in connection with the sale to customers of over \$2.4 billion in market value of auction rate securities.



OCIE's effort to promote voluntary compliance, good governance and risk management within the industry serves both investors and registrants: it diminishes the need for formal action while ensuring that investors have access to accurate, timely information. As part of this effort, OCIE has conducted Chief Compliance Officer Outreach (CCO Outreach) events designed to encourage open communications and coordination on compliance issues between the SEC and the mutual fund, investment adviser, and broker-dealer industries. OCIE published two public reports as part of a new initiative to create more transparency about issues identified in its examinations. Additionally, OCIE created an expansive large-firm monitoring program and improved communication efforts with senior management and fund boards at a number of large organizations. A primary goal of these efforts is to increase awareness, engagement and support on key risk and regulatory issues.

Finally, OCIE is contributing to the SEC's rulemaking process, imparting practical knowledge and information gathered during examinations while taking part in over 50 working groups implementing various Dodd-Frank Act rulemaking provisions. Other rulemakings have benefitted from significant OCIE input, as well, including large trader reporting rules, amendments to the Advisers Act and the consolidated audit trail rule proposal.

## Operating Divisions: Progress throughout the Agency

Enforcement, examination and rulemaking are the SEC's most visible functions. However, the importance of other efforts cannot be overstated. The SEC ensures that investors have access to timely, accurate and complete information, that markets function efficiently, that regulations are anchored in sound economics and that the agency as a whole is keeping up with changes in the financial marketplace.

The **Division of Corporation Finance** (CF), which oversees corporate disclosure of information, established new offices concerned with three vital facets of the financial world: an office focused on the largest financial institutions; the Office of Structured Finance, which deals with disclosure reviews and policy-making in asset-backed securities and other structured products; and the Office of Capital Market Trends. These offices are increasing the attention paid to market sectors that have proved systemically significant in recent years, aiding rulemaking and improving the SEC's familiarity with and expertise in these increasingly important areas.

CF's Office of Disclosure Operations worked in 2011 to enhance investor protection by targeting specific disclosure issues that had previously received little attention: requesting disclosure of overseas cash holdings which, if repatriated, would result in material, negative consequences; questioning whether current litigation contingency disclosure practices comply with existing requirements; and working with Enforcement, the Office of the Chief Accountant (OCA) and the Office of International Affairs (OIA) to combat an uptick in problems with reverse mergers by stepping up scrutiny of the Form 8-Ks filed in their wake.

In support of the SEC's call to facilitate capital formation for small enterprises, CF also began reviewing restrictions on communications in public offerings, the impact of the ban on general solicitation in private offerings, triggers for public reporting under Section 12(g) of the Exchange Act and regulatory questions around subjects including secondary trading platforms and new capital raising strategies.

In addition to very significant rulemaking responsibilities regarding derivatives trading, the **Division of Trading and**

**Markets** (TM) addressed a broad spectrum of issues as it worked to help stabilize the financial markets and protect the interests of large and retail investors.

TM received and processed over 2,000 SRO filings from exchanges, clearing agencies, the Financial Industry Regulatory Authority (FINRA), and the Municipal Securities Rulemaking Board (MSRB), including those regarding complex fee structures, new products, and revamped governance structures. TM led Commission monitoring of – and, as appropriate, response to – market activities in connection with significant events, including Hurricane Irene and the August 2011 market volatility, helping markets continue to function normally despite significant stress.

TM also continued to solicit stakeholder views on the structure of today's financial markets and on potential changes that might improve market integrity or help maintain a level playing field for investors of all types.

TM established a new Office of Derivatives Policy to focus on implementing the derivatives provisions of the Dodd-Frank Act. TM also continued to expand the clearance and settlement program, an effort that culminated in the establishment of a new Office of Clearance and Settlement. Traditionally focused on securities clearing agencies and transfer agents, the Office of Clearance and Settlement is now also responsible for implementing Dodd-Frank Act regulations for clearing agencies that clear security-based swaps, and for overseeing security-based swap data repositories.

The Dodd-Frank Act expanded the SEC's regulatory authority over previously-exempted advisers to hedge funds and other private funds, an important expansion of agency responsibility. The **Division of Investment Management** (IM) formed a new Private Funds group headed by an experienced hedge fund attorney to spearhead this regulatory program and to gear up for the task of collecting and conveying information that will be reported to the SEC by these entities for use by the Financial Stability Oversight Council (FSOC).

IM also worked with FSOC members to share information newly filed by money market funds with the SEC and the related analyses. This has facilitated critical consultations with other agencies responsible for monitoring systemic risk related to the European debt crisis.

The **Division of Risk, Strategy, and Financial Innovation** (RSFI) was created in 2009 as the SEC's internal "think tank," and provides the agency with sophisticated analyses that integrate economic, financial, and legal expertise. A linchpin of the SEC's effort to break down silos and bring together critical data from across the agency, RSFI is the "business owner" of the SEC's new TCR (tips, complaints and referrals) System, generating data and statistics on the system's operations and helping to define further system development.

RSFI provided critical support in the successful federal insider trading prosecutions of Raj Rajaratnam and Winifred Jiau, analyzing expert testimony and other documents proffered by the defense and allowing prosecutors to successfully challenge key portions of the defense's strategies.

The Division has contributed substantially to the Dodd-Frank Act rulemaking process, particularly with regard to the over-the-counter derivatives market. And RSFI is at the center of the SEC's work to provide detailed economic analysis of proposed agency actions.

RSFI also worked closely with OCIE, refining risk models that help OCIE direct exam resources in light of current trends and suspected abuses, and it participated in exams as part of RSFI's work developing tools, algorithms, and analytics that enhance the effectiveness of field teams at these exams.

Consistent with its "think tank" role, RSFI economists conducted research on financial and economic issues relevant to the SEC's mission, for publication in peer-reviewed academic journals, on relevant subjects such as "Short Selling in Initial Public Offerings" and "Venture Capital Reputation, Post-IPO Performance, and Corporate Governance."

The **Office of the Chief Accountant** (OCA) continued to coordinate and monitor progress towards convergence of U.S. Generally Accepted Accounting Principles and International Financial Reporting Standards (IFRS). OCA published both a report on progress against the staff's IFRS work plan and a Staff Paper exploring a possible method for incorporation of IFRS. OCA also worked with the SEC's **Office of International Affairs** (OIA) to develop recommendations and a final report regarding the IFRS Monitoring Board Governance Review.

In connection with OCA's role in overseeing the Public Company Accounting Oversight Board (PCAOB), the SEC approved a PCAOB rulemaking to update its Audit Risk Assessment Standards. These standards are designed to benefit investors by enhancing the effectiveness of the auditor's assessment of and response to the risks of material misstatement.

The SEC also approved temporary rules establishing the PCAOB's Interim Program of Inspection for Audits of Broker-Dealers. These rules are part of the PCAOB's initial steps to implement the expanded authority over auditors of broker-dealers granted it in the Dodd-Frank Act.

Since the Commission's appointment of three new PCAOB Board Members in February, 2011, OCA has been working closely with the new Board and PCAOB staff on several Board initiatives, including its consideration of potential changes to the auditors' reporting model.

OCA is also working with the PCAOB and the SEC's OIA on continuing negotiations with certain jurisdictions – most notably in the European Union and China – aimed at obtaining for the PCAOB the ability to adequately inspect audits by registrants' accountants. These negotiations occur at a time when the reliability of financial reports and audit practices in some jurisdictions has been called into question, leading to investor losses and the de-listing of a number of entities.

In addition to its work with OCA, OIA is working closely with Enforcement to ensure that the SEC's reach is as global as the financial markets have become – tracing and freezing \$317 million of fraud proceeds located overseas and repatriating \$241 million to harmed investors. It helped coordinate more than one thousand assistance requests between Enforcement and its foreign counterparts, while working to increase – from 71 nations to 80 – the number of signatories to a memorandum of understanding regarding compliance with and enforcement of securities laws. In addition, OIA brokered information-sharing agreements between the PCAOB and the United Kingdom and the Swiss Audit Oversight Authorities, allowing the PCAOB to inspect the auditors of foreign companies listed on U.S. exchanges and registered with the SEC.



OIA also created and led a Task Force on International Implementation – an intra-agency task force coordinating the international aspects of the Dodd-Frank Act. The Task Force's work is diminishing the risk that Dodd-Frank Act regulation will conflict with regulations in other countries, and create the potential for regulatory arbitrage.

The **Office of Investor Education and Advocacy (OIEA)** redesigned and expanded its investor.gov website, adding information on a variety of topics, and materials aimed at the particular needs of specific groups, such as service members, teachers and retirees. OIEA completed a Dodd-Frank Act study on ways to improve investors' access to registration information about investment professionals. In addition, it began a multi-part study on financial literacy among retail investors underway.

### **A Critical Market Response: May 6th and Market Confidence**

In 2011, the SEC continued efforts to address the unusual market volatility that occurred on May 6, 2010.

At 2:42 on the afternoon of May 6, 2010, stock prices on U.S. exchanges began to fall with almost unprecedented speed – 573 points in five minutes – leaving the nation's most prominent stock index down over 900 points from the previous day's close. At the worst end of the spectrum, more than 300 securities suffered declines of more than 60 percent. And then, just as suddenly, the markets reversed themselves, recovering to pre-crash levels within minutes.

These unusual price swings caused significant harm to many investors, including those who lost money when “stop loss” programs led to automatic selling during the dramatic – but quickly reversed – decline. In addition to financial losses, the sudden disruptions also delivered a significant blow to the confidence of investors of all types – individual retail investors, large institutions and all those in between.

Recognizing the significance of the market's unusual fluctuations, the SEC acted immediately, working with the exchanges, FINRA and the Commodity Futures Trading Commission (CFTC) to determine causes of the volatility and to take action to reduce the possibility of other, similar, events occurring in the future.

Beginning in May 2010, the SEC – spearheaded by the Division of Trading and Markets – joined with FINRA and the exchanges to propose the single-stock circuit breakers which would ultimately be applied to most U.S. equity securities.

On October 1, 2010, staffs of the SEC and CFTC presented a comprehensive analysis of the causes and consequence of the May 6 volatility, as the SEC's efforts to enhance market integrity continued into the new fiscal year.

- In 2011, the SEC adopted a rule effectively prohibiting brokers and dealers from offering customers “unfiltered” or “naked” access to the exchanges by requiring that risk controls – designed to prevent inadvertent risk threats to market stability – be in place before access is provided. The rule requires brokers to put in place risk management controls and supervisory procedures to help prevent erroneous orders, ensure compliance with regulatory requirements, and enforce pre-set credit or capital thresholds.
- The SEC approved rules proposed by FINRA and the exchanges that provide more certainty regarding the circumstances under which trades will be considered “clearly erroneous” and canceled. After May 6, a variety of market participants reported that the uncertainty over which trades would be canceled contributed to participants' decision to withdraw from trading, further exacerbating the market's volatility.
- The SEC also approved rules proposed by FINRA and the exchanges requiring that market makers maintain a

quote within a certain percentage of the prevailing bid and offer, which reduces the likelihood that stub quotes – offers to buy or sell a stock at a price so far away from the prevailing market that they are not intended to be executed – will be executed against. Executions against quotes as low as a penny a share and as high as \$100,000 represented a significant proportion of the trades that were executed at extreme prices on May 6 and were subsequently broken.

- The SEC considered a proposed national market system (NMS) plan filed by national securities exchanges and FINRA that would establish a new “limit up-limit down” mechanism to address extraordinary market volatility in U.S. equity markets. Limit up-limit down would prevent trades in listed equity securities from occurring outside a specified price band, which would be set at a percentage level above and below the average price of the security over the immediately preceding five-minute period.
- The Commission published for comment changes proposed by SROs to rules governing market-wide circuit breakers. Among other things, the proposals would lower the thresholds that trigger the respective Level 1, 2 and 3 market-wide circuit breakers from 10 percent, 20 percent and 30 percent, to 7 percent, 13 percent and 20 percent. They also would replace the Dow Jones Industrial Average with the S&P 500 Index as the pricing reference against which to measure market decline.
- The Commission adopted a rule establishing large trader reporting requirements that will enhance the agency's ability to identify large market participants, as well as to collect and analyze information on their trading activity. This will both speed analysis of unexpected market behavior and aid the SEC's Division of Enforcement in investigations of suspicious activity.

## **Dodd-Frank Act Regulations: Implementing Financial Reform**

The Dodd-Frank Act is the most significant piece of securities legislation since the 1930s, one that both imposes significant new investor protection and market stability responsibilities on the SEC, and provides new tools with which to meet those responsibilities. 2011 was the busiest portion of the multi-

year implementation agenda written by Congress into the law and the SEC – in collaboration with other regulatory bodies and in close communication with stakeholders representing every facet of the financial marketplace – made significant progress against that agenda.

Of the more than 90 mandatory rulemaking provisions in the Dodd-Frank Act, the SEC had proposed or adopted rules for three-quarters of them by the close of 2011, as well as a number of the rules stemming from the dozens of other provisions that give the SEC discretionary rulemaking authority. Additionally, the SEC had issued 12 of the more than 20 studies and reports that it is required to complete under the Act.

### **Derivatives**

One of the most complex and important responsibilities assigned to the SEC in the Dodd-Frank Act is the building – from the ground up, together with the Commodity Futures Trading Commission (CFTC) – a regulatory system for an over-the-counter derivatives market that has grown in notional value to hundreds of trillions of dollars. A new, transparent derivatives market, with a variety of trading platforms and central clearing, will diminish risk and encourage competition, which can increase liquidity and improve pricing.

By the close of 2011, the SEC had begun to lay the groundwork for regulating security-based swaps – the agency's part of this complex new derivatives market – with a series of proposals regarding its fundamental legal, structural and definitional issues.

- The SEC, jointly with the CFTC, proposed rules further defining a number of key terms, including “swap,” “security-based swap,” “security-based swap agreement,” “swap dealer,” “security-based swap dealer,” “major swap participant,” and “major security-based swap participant.” These rules seek to clarify whether and how derivatives market participants will be subject to regulation, either as a result of the products in which they transact or the activities they undertake.
- The SEC proposed rules governing the registration and operation of security-based swap data repositories (SDRs), new entities that will collect transaction informa-



tion on securities-related swap transactions and publicly disseminate it in real time. These rules also prescribe the manner in which transactions must be reported to SDRs, and how SDRs should disseminate transaction information.

- The SEC proposed rules regarding clearance of security-based swaps that are not covered by the end-user exemption. These rules would establish a process through which clearing agencies provide information to the SEC about the security-based swaps they plan to accept for clearing. The rules would also set minimum operational and governance standards for clearing agencies. Additionally, the SEC proposed rules setting forth the requirements to which end-users must adhere when they engage in security-based swap transactions that are exempt any from mandatory clearing requirement that may apply.
- The SEC proposed rules establishing a framework for the registration and regulation of swap execution facilities (SEFs) – platforms on which security-based swaps required to be cleared may be traded. These regulations would encourage transparent and fair trading of security-based swaps.
- The SEC took steps to provide for the registration and regulation of security-based swap dealers and major security-based swap participants by, among other things, proposing rules establishing business conduct standards applicable to those entities.

### **Asset-Backed Securities**

The collapse of the market for one type of asset-backed securities (ABS), those backed by residential subprime mortgages, was a precipitating event for the global financial crisis. Mortgage originators, able to transfer the risk of foreclosure to securitizers, allowed underwriting standards to collapse. Securitizers then transferred their risk to investors, who lost billions when mortgage-holders began defaulting on

an unprecedented scale. The SEC is pursuing regulations that would encourage high underwriting standards by aligning the interests of originators and securitizers with those of investors, and by ensuring that investors in these securities have access to the information needed to invest rationally.

- Risk retention requirements would ensure that securitizers have “skin in the game” and, thus, incentive to ensure quality underwriting. The SEC joined the Federal Reserve Board, the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, the Federal Housing Finance Agency and the Department of Housing and Urban Development in seeking public comment on a proposed rule that would require sponsors of ABS to retain at least five percent of the credit risk of the assets underlying the security.
- The SEC adopted rules requiring issuers of asset-backed securities to disclose the history of repurchase requests received and repurchases made, and requiring issuers of asset-backed securities to conduct a review of the assets underlying those securities.
- The SEC also adopted rules implementing the Dodd-Frank Act provision which requires ABS issuers in registered transactions to review the assets underlying the ABS and disclose the nature of the review.
- The SEC proposed a rule prohibiting material conflicts of interest between those who package and sell asset-backed securities and those who invest in them, helping ensure that entities which create and sell asset-backed securities cannot benefit at the expense of their clients, from the failure of those same securities.
- The SEC re-proposed for public comment rules requiring greater accountability and enhanced quality around ABS when issuers seek to use an expedited registration process known as “shelf registration.” First proposed before that enactment of the Dodd-Frank Act, the revised proposal would require that an executive officer of the issuer certify the accuracy of the disclosure, that the securitization be designed to ensure cash flows sufficient to service expected payments, that a risk manager be appointed to review assets upon the occurrence of certain trigger events, and that dispute resolution procedures be in place in the event of a repurchase request.

## Credit Rating Agencies

The collapse of billions of dollars of triple-A rated mortgage-backed securities was a key element of the financial crisis. Over-reliance on opinions issued by nationally recognized statistical rating organizations (NRSROs or, simply, rating agencies) left investors exposed to risks that were, in fact, far greater than the securities’ initial ratings implied (many of these triple A securities were eventually downgraded to “junk” status).

Independent of financial reform legislation, the SEC had previously proposed rules that would lessen reliance on rating agencies by requiring that investors have access to data on the assets, including individual mortgage data, underlying ABS.

- In response to the Dodd-Frank Act, the SEC proposed rules and amendments intended to increase transparency and improve the integrity of credit ratings by requiring that NRSROs report on internal controls, protect against conflicts of interest, establish professional standards for credit analysts, publicly disclose the methodology used to determine individual ratings and enhance their public disclosures about the performance of their credit ratings.
- The SEC removed credit ratings as eligibility requirements for companies seeking to use “short-form” registration when registering securities for public sale. The SEC also proposed amendments to existing rules that would remove references to credit ratings in several rules under the Exchange Act, including rules concerning broker-dealer financial responsibility, distributions of securities, and confirmations of reserve requirements for broker-held excess margin securities. In addition, the SEC proposed removing credit rating references in certain rules and forms under the Investment Company Act of 1940, including Rule 2a-7, governing the operations of money market funds.

## Executive Compensation

- The SEC adopted rules concerning shareholder approval of executive compensation and “golden parachute” compensation arrangements, requiring that say-on-pay

votes occur at least once every three years and that a “frequency” vote be held at least once every six years. Companies also are required to provide additional disclosure regarding “golden parachute” compensation arrangements made with certain executive officers in connection with merger transactions.

- The SEC, jointly with the Federal Reserve and five other financial regulatory agencies, proposed a rule that would require certain financial institutions – including broker-dealers and investment advisers with \$1 billion or more in assets – to disclose the structure of their incentive-based compensation practices, and which would prohibit such institutions from maintaining compensation arrangements that encourage inappropriate risks.
- The SEC also proposed rules requiring the Commission to direct the national securities exchanges and national securities associations to prohibit the listing of any equity security of an issuer that does not comply with new compensation committee and compensation adviser requirements.

### Private Funds

- The SEC adopted rules requiring advisers to hedge funds and other private funds to register with the SEC and reallocating regulatory responsibility for smaller advisers to the states. In addition, the Commission approved rules that implement exemptions from registration for three types of private fund advisers: advisers solely to venture capital funds; advisers solely to private funds with less than \$150 million in assets under management in the U.S.; and certain private advisers without a place of business in the U.S.
- In a joint release with the CFTC, the Commission proposed a new rule that would require hedge fund advisers and other private fund advisers to report systemic risk information on a new form, Form PF (this proposal was adopted in October, 2011).
- The SEC adopted a rule defining “family offices” that will be excluded from the definition of an investment adviser under the Investment Advisers Act, and therefore not subject to regulation under the Act.

### Other Significant Dodd-Frank Act Rulemakings

- The SEC proposed a rule creating a new process by which municipal advisers must register with the SEC, submitting detailed information and certifying that they have met or will meet the qualifications and regulatory obligations required of them. Required information would include contact information, a list of municipal advisory activities in which they engage, and disciplinary history. When adopted, this rule will supersede a more limited temporary rule adopted shortly after the passage of the Dodd-Frank Act.
- The SEC proposed rules that would require reporting issuers to disclose annually whether they use “conflict minerals” that originate from the Democratic Republic of the Congo or adjoining countries and are “necessary to the functionality or production” of a product that the issuer either manufactures or contracts to be manufactured.
- The SEC proposed rules that would require resource extraction issuers to disclose payments made by themselves, a subsidiary or any entity they control to the U.S. or foreign governments, including taxes, royalties, fees (including license fees), production entitlements and bonuses. Additionally, rules were proposed outlining the way in which mining companies must disclose to investors certain information about mine safety and health standards.
- The SEC created a Whistleblower Program that rewards insiders who provide the agency with high-quality tips that lead to successful enforcement actions. To be considered, a whistleblower must voluntarily provide the SEC with original information that leads to the successful enforcement by the SEC of a Federal court or administrative action and monetary sanctions totaling more than \$1 million. Under the program, whistleblowers will enjoy new protections. The new rules encourage company employees to report suspected wrongdoing internally, providing companies a strong incentive to have a credible, effective compliance program in place.

## Dodd-Frank Act Studies

In addition to rulemakings, the Dodd-Frank Act requires the SEC to produce a number of reports. Among them:

- The SEC submitted to Congress a staff study on the standard of conduct applicable to broker-dealers and investment advisers who provide personalized investment advice to retail investors. The study concluded that, although retail investors generally expect that investment professionals (whether investment advisers or broker-dealers) are acting in their best interests, those investors are confused by the different standards of conduct that apply under the two regimes. The study concluded that retail customers should not have to parse legal distinctions to determine whether the advice they receive is provided in accordance with their expectations, and that a retail investor receiving personalized investment advice about securities should receive the same regulatory protections, regardless of whether the investor chooses to work with an investment adviser or a broker-dealer.
- To address this conclusion, the study made two primary recommendations; that the Commission exercise its discretionary rulemaking authority to implement a uniform fiduciary standard of conduct (which would be “no less stringent” than the standard that applies to investment advisers today) for broker-dealers and investment advisers when they provide personalized investment advice about securities to retail investors; and that the Commission consider harmonization of broker-dealer and investment adviser regulation when those financial professionals provide the same or substantially similar services to retail investors and when such harmonization adds meaningfully to investor protection.
- The SEC submitted, with the CFTC, a joint staff study required by the Dodd-Frank Act on “the feasibility of requiring the derivatives industry to adopt standardized computer-readable algorithmic descriptions which may be used to describe complex and standardized financial derivatives.” The joint study concluded that current technology is capable of representing derivatives using a common set of computer-readable descriptions and that these descriptions are precise enough to use for the calculation of net exposures and to serve as part or all of a binding legal contract.

- The Commission submitted to Congress a staff study on the need for enhanced examination and enforcement resources for investment advisers that are registered with the Commission.

## Beyond the Dodd-Frank Act: An Investor-Focused Rulemaking Agenda

The SEC’s rulemaking efforts extend beyond the boundaries of the Dodd-Frank Act, addressing priorities in areas not covered by that legislation.

- The SEC proposed amendments to the broker-dealer financial reporting rule that would strengthen the audits of broker-dealers and the SEC’s oversight of broker-dealers’ handling of their customers’ securities and cash. Building on rules adopted in December, 2009 that strengthened custody controls for investment advisers, the proposed rules would reinforce the annual reporting and audits of broker-dealers by improving the focus on compliance with financial responsibility rules and related controls.
- The SEC made available to investors the detailed information that money market funds file with the agency, including information about a fund’s investments and the market-based price of its portfolio known as its “shadow NAV” or mark-to-market valuation. The information is available on the SEC’s website and is updated monthly.
- The SEC issued a concept release seeking public comment on the treatment of real estate investment trusts (REITs) and other mortgage-related pools under the Investment Company Act. At the same time, the Commission issued an advance notice of proposed rulemaking, seeking public input on possible amendments the agency might consider proposing to Rule 3a-7, which provides a conditional exclusion from the definition of “investment company” under the Investment Company Act for certain issuers of asset-backed securities.
- The SEC also issued a concept release seeking public comment on the use of derivatives by mutual funds and other investment companies registered under the Investment Company Act. The agency acted, among other causes, in light of recent significant growth in the

holding of derivatives by mutual funds, exchange-traded funds and closed-end funds.

### **Increasing SEC Effectiveness through Structural Improvements**

In 2011, the SEC continued to make strategic structural improvements, striving to build a more effective and well-managed agency, one in which organizations are appropriately aligned, administrative and logistical support is dynamic and efficient, operational controls are effective in mitigating operational risk, and all functions are supported with appropriate, upgraded information technology.

One area of significant focus this year was the work of the Boston Consulting Group (BCG), which was hired in response to a Dodd–Frank Act requirement that the SEC engage an independent consultant to conduct a broad assessment of the SEC's internal operations, structure, funding, and relationship with self-regulatory organizations (SROs).

BCG reported their findings in March, 2011, including numerous recommendations designed to increase the SEC's efficiency and effectiveness. In the months following the release of the BCG report, the SEC has developed the necessary program management and oversight infrastructure to respond to its key recommendations.

In 2011, the SEC continued to improve back office functions in its largest divisions and offices, creating “managing executive” positions to handle important support areas such as

information technology, workflow, data collection and analysis and human resources. The management professionals who have filled these positions have both improved deployment of limited resources and personnel and freed legal, examination and other professionals to focus their skills on mission-critical work.

On a broader level, several commission-wide infrastructure support functions previously housed under the Office of the Executive Director were consolidated with those residing in the Office of the Chief Operating Officer (OCOO), achieving economies of scale and improving management of the interdependencies between them. The physical security operation, previously fragmented in three separate offices, has been consolidated as well. Across infrastructure areas more generally, the SEC is moving its leasing operation to General Services Administration (GSA) and reducing the size of associated functions such as the construction branch.

The Office of Financial Management (OFM) made significant progress in improving internal controls, eliminating a material weakness from 2010. Also, OFM has been preparing for the migration of the SEC's financial system to a Federal Shared Service Provider (FSSP), with the transition on track for FY 2012 implementation.

In direct response to one of the BCG report's recommendations, the SEC has implemented a continuous cost reduction program that has identified a number of areas of potential savings, and has begun pulling back on these expenditures and repurposing the funds towards other mission-critical activities.

A number of significant technology infrastructure improvements were led by the Office of Information Technology (OIT), including implementation of a major component of the Enforcement Case Management system (HUB). This multi-year project is currently in the initial pilot of the software. Also in 2011, Electronic, Data Gathering, Analysis, and Retrieval (EDGAR) filers were migrated from a client-based filing application called EDGARLink onto a totally on-line filing interface called EDGARLink On-line, thus making filing with the Commission easier than ever. The SEC significantly reduced the technology implementation cost associated with new Dodd-Frank Act rules and realized an estimated savings of approximately



\$35 million by utilizing the EDGAR Filing Systems as the Dodd Frank Act filing data repository.

OIT also developed an enterprise architecture strategy and framework based on recommendations from a 2011 Mitre assessment and the BCG study's recommendations. This framework will be a strategic roadmap for better alignment of IT investments with the SEC's business units.

In addition, the organizational design of the OIT was changed to emphasize increased alignment with internal clients, improve coordination and increase efficiencies by centralizing activities such as application development and project management.

The Office of Human Resources (OHR) improved the recruiting and hiring process and achieved a 10 percent reduction in the average length of time required to fill external vacancies. Additionally, and in concert with the recommendations of the BCG study, the SEC has taken a strategic approach to restructuring the composition of the SEC's workforce, and is actively prioritizing external hiring needs, rather than simply back-filling open positions created by attrition. OHR also rolled out a new performance management system to the agency, and provided in depth training in the system to over 700 managers.

In addition to hiring and performance strategies designed to improve SEC institutional capacity, the SEC continues to expand its training and professional development efforts.

SEC staff participated in 89 separate learning events at SEC University's College of Securities and Investor Protection (CSIP), together receiving more than 6,000 certifications for completing programs in subjects such as forensic accounting, detection of financial fraud, and quantitative high frequency trading; in securities, financial, accounting, statistics, and business training; and in industry- and position-specific expertise that supports the agency's goals.

Staff who attended more than 170 College of Education Administration trainings are bringing new and upgraded skills to the SEC's financial management, IT and administrative functions, while the College of Leadership Development has delivered a diverse array of leadership programs to the men and women whose management abilities will help SEC performance continue to improve in the years ahead.

A new Chief Data Office has been created to integrate strategic goals for enterprise data across the lines of business and Office of Information Technology (OIT). The ultimate goal is to create a streamlined and sharable data architecture.

Additionally, the SEC has established an Operational Risk Management organization to assist in identification and mitigation of the operational risks the agency faces.

The agency has dramatically improved its ability to process Freedom of Information Act (FOIA) requests, in spite of unprecedented volume. 2011 saw a 10 percent increase in the number of requests received, on top of a 33 percent increase in 2010. The Commission has received more than 10,000 requests each of the past two years, yet has processed more requests than it received. The SEC closed 2011 with fewer requests pending than in any year since 2001.

While most observers rightly focus on front-line SEC functions, such as oversight and rulemaking, the SEC's leadership understands that back office activities are key components of effective front-line operations. Significant improvements in personnel, training and IT functions will help the SEC make the financial marketplace safer and more stable for all investors.

## Conclusion

The SEC is matching its expanding responsibilities with an equally ambitious effort to enhance its performance at every level. The agency is improving internal logistics and staff abilities, focusing more effectively on emerging financial market developments, and infusing its rulemakings with ideas and strategies that reflect not just the growing expertise of SEC staff, but the intent of Congress and the experience of the market participants who will be most affected by agency actions.

The result is an agency increasingly responsive to the demands of the world's most important financial markets and those who participate in them – whether sophisticated professionals or the hundred million retail investors with assets in the market today.

## Looking Forward

---

In FY 2012, the SEC expects to continue the trajectory it has followed through the last two years: pursuing a regulatory agenda consistent with recent statutory changes and the accelerating evolution in the financial markets; examining the structure of those markets with respect to current regulation; increasing the quality of the information investors receive and of their communications with companies and boards; and improving the agency's own internal functions and infrastructure.

As the agency moves towards completion of the rulemaking and reports required by the Dodd-Frank Act, the agency will increasingly focus on other priorities – many of them informed by securities market changes in the last decade.

Other areas of agency focus will include the quality of the information received by investors from registered entities, including U.S. disclosure mandates and the quality of the principles underlying financial accounting in a global financial marketplace. The agency will also continue to examine the proxy process, seeking ways in which communication between shareholders and boards might be made more effective and less cumbersome.

And, the SEC will continue to study the strengths and weaknesses of contemporary financial markets, soliciting the perspectives of a broad variety of market participants, and working to determine where action may increase market stability and investor confidence.

In order to more effectively pursue these initiatives as it continues to exercise oversight in areas of established responsibility, the SEC expects to continue improving its internal operations, including human resources, IT and financial controls. The SEC will also continue its Mission Advancement Program, the agency-wide effort to implement the recommendations contained in the Boston Consulting Group (BCG) management study required by the Dodd-Frank Act.

### Rulemakings – Dodd-Frank and Beyond

- In 2012, the SEC plans to conclude the vast majority of the rulemaking required by the Dodd-Frank Act and subject to deadlines set by Congress.
- While the Dodd-Frank Act did not mandate a deadline for their adoption, the Commission will also consider additional executive compensation requirements. These will include rules mandating new listing standards relating to specified “clawback” policies, and new disclosure requirements for executive pay ratios, employee and director hedging, and the relationship between executive compensation and company performance.
- The Commission has already proposed a number of regulations required by Title VII of the Dodd-Frank Act related to the regulation of over-the-counter derivatives. While proposing and finalizing the remaining rules, the SEC will also continue working with other regulators and market participants to construct the new regulatory framework in a way that takes into account the steps market participants will need to take to comply with the new regulations, and the order in which those steps might best be taken. To that end, the SEC will seek public comment on a detailed implementation plan that will permit a roll-out of the new requirements in a logical, progressive, and efficient manner, while minimizing unnecessary disruption and costs.
- The SEC will continue to advance a number of studies required by the Dodd-Frank Act. Among these is a study of the credit rating process for structured finance products and the conflicts associated with the “issuer-pay” and the “subscriber-pay” models. A key part of this effort will be examining comments, proposals and data already received regarding the feasibility of establishing a system in which a public or private utility or a self-regulatory organization would assign agencies to individual rating projects, rather than continuing to rely on the current issuer-driven business model.

- The SEC will consider the recommendations of a staff study on the obligations of investment advisers and broker-dealers that there be a universal fiduciary standard of conduct which applies to both types of registrants when they are providing personalized investment advice to retail investors, and that regulations regarding the two professions be better harmonized.
- Other agency priorities arising from the Dodd-Frank Act will include rules intended to better protect investors in the asset-backed securities (ABS) market by improving the disclosure and offering process for ABS and prohibiting many material conflicts of interest by entities packaging and selling them; rules regarding the registration of municipal advisers; and rules requiring that reporting companies provide information about their use of certain “conflict minerals” in their products.
- One key rulemaking not related to the Dodd-Frank Act that the SEC expects to advance is the proposal to create a consolidated audit trail, which would allow regulators to track information related to trading orders received, routed and executed across multiple securities markets. The consolidated audit trail should allow the agency to rapidly reconstruct trading activity and quickly analyze both suspicious trading behavior and unusual market events.
- The SEC, working with a team from the Financial Stability Oversight Council, is considering further structural changes to money market funds, building on reforms adopted shortly after the financial crisis, during which the Reserve Primary Fund “broke the buck.” These reforms would seek to address funds’ susceptibility to runs and provide for a greater cushion in the case of an emergency.
- The SEC is also reviewing ways to reduce the regulatory burdens on smaller companies, particularly burdens associated with capital formation, in a manner consistent with the Commission’s investor protection mandate. This review will consider, among other things, the rules related to the triggers for public reporting, communications in public and private offerings, and new capital raising strategies.



## Responding to Current Market Structure

The SEC continues to examine a securities market structure where changes – particularly the emergence of high-speed, computer-driven trading – have outpaced the governing regulatory structure.

- Working with an eye towards preserving the efficiency, liquidity and competition benefits of current structure, the SEC will consider further possible reforms growing out of the unusual volatility markets displayed on May 6, 2010. These include the proposal by self-regulatory organizations to establish a new “limit up-limit down” mechanism and changes to the rules governing market-wide circuit breakers.
- An important issue related to high-frequency trading and the sophisticated electronic systems that drive today’s markets is the risk of volume-induced market disruptions or unauthorized access to systems and networks. In 2012, the SEC expects to consider whether to make compliance with existing, voluntary Automation Review Policies mandatory. Doing so would require market participants – most of whom are already in compliance with these policies – to meet standards for the capacity, resiliency, and security of their automated systems.

## Information and Communication

The quality of the communication between investors and the companies in which they invest is of paramount importance. Investors with access to accurate, timely information can make informed judgments about risk and allocate their capital efficiently. Investors are also more likely to take part in a market characterized by disclosure and communication, making additional capital available to growing enterprises.

- In 2012, the SEC will continue to encourage companies to enhance and clarify key information disclosed to investors, especially information that provides a better view into the risks companies face and the impact of operational decisions companies' management make.
- In addition, agency staff will develop recommendations related to the Commission's July 2010 "Proxy Plumbing" concept release, in which the Commission asked a number of questions about how communication between shareholders and company boards might be improved.
- The SEC will continue to consider incorporating International Financial Reporting Standards into the financial reporting system for U.S. domestic companies. The agency will take measured steps in accordance with the existing Work Plan towards the goal of global standards, while ensuring that the interests of U.S. investors in timely, accurate and comparable financial data remain the primary consideration.



## Internal Reforms

SEC management recognizes that increased operational efficiency is critical to carrying out its mission at a time when the agency's responsibilities are growing faster than available resources. This requires continued focus on the technical, financial and managerial functions that allow the agency to carry out day-to-day operations more efficiently and to respond quickly, creatively and effectively to unanticipated events.

- A key priority for the SEC will be building on the significant progress made in strengthening its internal controls. The centerpiece of this effort will be completing the migration of the agency's financial system and some of its financial operations to the Federal Shared Service Provider (FSSP) at the Department of Transportation. Once completed, this initiative will yield significant benefits for the SEC in terms of enhanced system functionality and more streamlined operations. The SEC also will continue its multi-year efforts to remediate audit findings with respect to IT security financial reporting, registrant deposits, and accounting for budgetary resources.
- The Office of Information Technology will focus on EDGAR and SEC.gov modernization – improving system performance, adding features and enhancing the ability to manage Dodd-Frank Act data. Enhancements to the Tips, Complaints and Referrals system, and the Division of Enforcement's HUB system – its primary database – will extend their functionality and improve their ability to support improved business process workflow, search and auditing. The SEC will also focus on improving data management and the procurement of robust analytical tools with which to better analyze data.
- The agency will continue its Mission Advancement Program, working to implement recommendations resulting from the Dodd-Frank-mandated BCG study of the SEC's management. Following the release of the study in early 2011, the program office created 17 recommendation analysis workstreams. These workstreams will yield in suggested approaches for implementation and an estimate of the resources required.

SEC senior leadership is actively engaged in these efforts and serves on an Executive Steering Committee (ESC) established to oversee the implementation of the resulting initiatives.

- The agency expects to realize significant operational efficiencies and enhanced service provision through organizational redesigns of the Offices of Human Resources, Administrative Services and Financial Management, coupled with a focus on business process improvement initiatives in each of those activities.

In the year ahead, the SEC will enhance operations, infrastructure and management as part of its ongoing effort to become a more effective and dynamic agency. Making these changes, while implementing the Dodd-Frank Act, addressing market structure concerns and ensuring that information needed to make rational investment decisions is disclosed in a clear and timely fashion, will allow the SEC to continue improving investor safeguards and strengthening the U.S. capital markets.

## Financial Highlights

This section provides an analysis of the financial position, results of operations, and the underlying causes for significant changes in balances presented in the SEC's FY 2011 financial statements.

### Overview of Financial Position

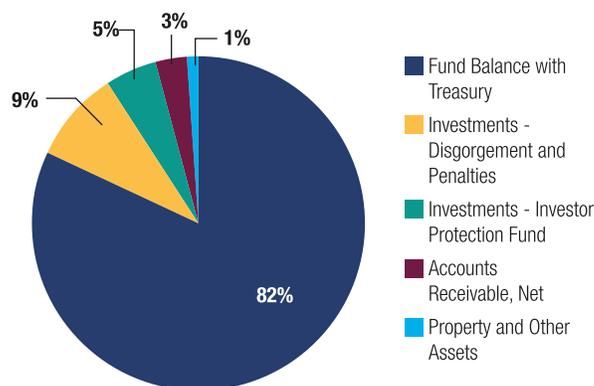
**Assets.** The SEC's total assets were \$8,517 million at September 30, 2011, an increase of \$355 million or 4 percent over FY 2010.

Investments, Net increased by \$278 million due to a \$453 million increase in Investor Protection Fund investments, and a \$175 million decrease in Disgorgement and Penalty related investments. Investor Protection Fund resources were invested in Treasury securities during the first quarter of FY 2011. The decrease in Disgorgement and Penalty investments is related to the SEC's continued efforts to accelerate distributions to harmed investors during FY 2011.

The increase in Accounts Receivable, Net of \$53 million is mainly comprised of a \$43 million increase in Section 31 fees receivable and a \$9 million increase in disgorgement and penalty accounts receivable (net) designated as payable to the U.S. Treasury General Fund upon collection.

Section 31 fees are payable to SEC twice a year: in March for the period September through December and in September for the period January through August. Thus, the year-end Section 31 accounts receivable balance is for securities transactions occurring during the month of September. The increase in Section 31 accounts receivable during FY 2011 is attributable to the increase in the fee rate from \$16.90 to \$19.20 and a 37 percent transaction volume increase when comparing September 2010 to September 2011.

**CHART 1.3  
ASSETS BY TYPE**



**TABLE 1.2  
ASSETS AS OF SEPTEMBER 30, 2011 AND 2010**

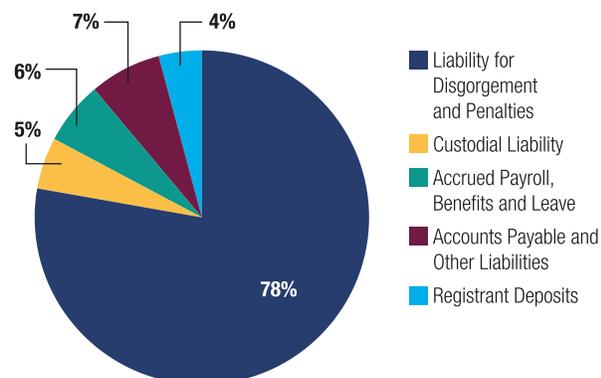
(DOLLARS IN MILLIONS)	FY 2011	FY 2010
Fund Balance with Treasury	\$ 6,996	\$ 6,989
Investments – Disgorgement and Penalties	750	925
Investments – Investor Protection Fund	453	-
Accounts Receivable, Net	214	161
Property and Equipment, Net	94	80
Other Assets	10	7
<b>Total Assets</b>	<b>\$ 8,517</b>	<b>\$ 8,162</b>

**Liabilities.** The SEC's total liabilities were \$1,106 million at September 30, 2011, a decrease of \$176 million or 14 percent from FY 2010. This decrease was mostly related to SEC's continued efforts to accelerate distributions to harmed investors. These distribution activities resulted in a \$158 million decrease in the Liability for Disgorgement and Penalties.

SEC's accrued liabilities for employee compensation and benefits decreased by \$16 million, mainly due to a shorter payroll accrual period at the end of FY 2011 when compared to FY 2010. On September 30, 2011, only five days remained in the pay period for which to accrue employee compensation and benefits, whereas on September 30, 2010, 14 days remained. In addition, Other Liabilities decreased by \$24 million due in part to the resolution of approximately \$10 million dollars in legal liabilities stemming from a complaint filed by the National Treasury Employees Union (NTEU) before the Federal Labor Relations Authority (FLRA) for retroactive wage adjustments.

**Ending Net Position.** The SEC's net position, comprised of both unexpended appropriations and the cumulative results of operations, increased by \$531 million or 8 percent between September 30, 2010 and September 30, 2011. The increase is primarily due to the increases in Section 31 and filing fee revenues discussed in the Results of Operations section below.

**CHART 1.4**  
**LIABILITIES BY TYPE**



**TABLE 1.3**  
**LIABILITIES AS OF SEPTEMBER 30, 2011 AND 2010**

(DOLLARS IN MILLIONS)	FY 2011	FY 2010
Liability for Disgorgement and Penalties	\$ 863	\$ 1,021
Custodial Liability	52	42
Accrued Payroll, Benefits and Leave	67	83
Accounts Payable	61	51
Registrant Deposits	47	45
Other Liabilities	16	40
<b>Total Liabilities</b>	<b>\$ 1,106</b>	<b>\$ 1,282</b>

## Results of Operations

**Earned Revenues.** Total earned revenues for the year ended September 30, 2011 increased by \$261 million or 19 percent over the total for FY 2010. The growth in Section 31 revenues of \$115 million was driven by an increase in transactional volume and higher average fee rates in FY 2011 as compared to FY 2010. The \$143 million increase in filing fee revenue was primarily driven by higher average fee rates. The SEC adjusts the rates periodically in order to meet the annual offsetting collection targets specified in the Investor and Capital Markets Fee Relief Act of 2002. Other revenue is mainly related to post judgment interest on disgorgement and penalty receivables.

Section 31 fee rates are per million dollars of securities transacted on exchanges and over-the-counter markets. In the first quarter of FY 2010, the Section 31 fee rate was \$25.70. This rate was reduced to \$12.70 in the second quarter, and then increased to \$16.90 for the third and fourth quarters. The rate remained unchanged through the first quarter of FY 2011, but was increased to \$19.20 for the second, third and fourth quarters of FY 2011. The overall securities transaction volume subject to Section 31 fees increased 8 percent between FY 2010 and FY 2011.

Filing fee rates are per million dollars of registered securities. In the first quarter of FY 2010, the filing fee rate was \$55.80. The rate increased to \$71.30 in the second quarter of FY 2010. The rate remained unchanged until the second quarter of FY 2011 when it increased to \$116.10 for the remainder of the fiscal year.

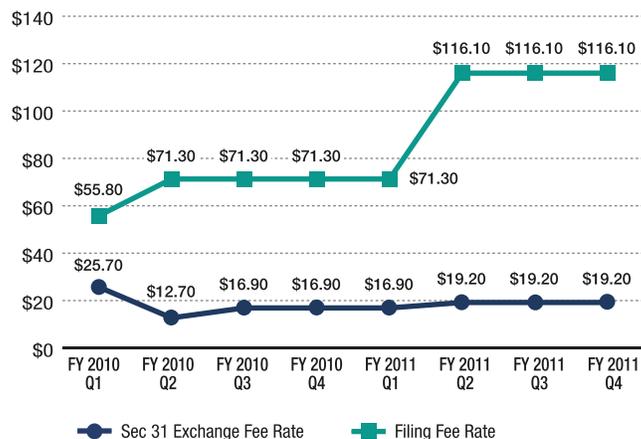
**Program Costs.** Total Program Costs were \$1,148 million for the year ended September 30, 2011, an increase of \$90 million or 9 percent when compared to the prior year. The SEC's salary and benefit costs increased by \$43 million when comparing FY 2011 to FY 2010. Other costs increased \$47 million.

The SEC's number of full-time equivalents (FTEs) increased by 96 employees when comparing FY 2010 to FY 2011. This increase in FTEs is directly related to the agency's continued focus on hiring new staff with the requisite skills and experience to further the SEC's mission.

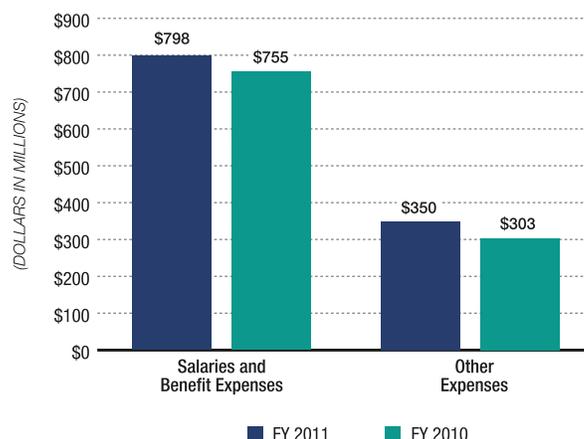
**TABLE 1.4  
EARNED REVENUES FOR THE YEARS ENDED  
SEPTEMBER 30, 2011 AND 2010**

(DOLLARS IN MILLIONS)	FY 2011	FY 2010
Section 31 Securities Transaction Fees	\$ 1,279	\$ 1,164
Section 6 (b) Securities Registration, Tender Offer, and Merger Fees	362	219
Other	3	—
<b>Total</b>	<b>\$ 1,644</b>	<b>\$ 1,383</b>

**CHART 1.5  
FILING FEE AND SECTION 31 EXCHANGE FEE RATES**



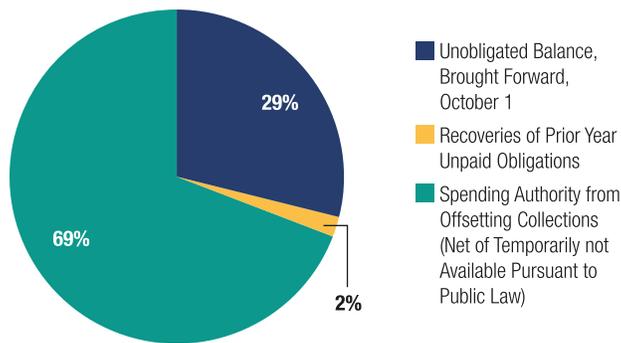
**CHART 1.6  
PROGRAM COSTS**



## Budgetary Resources

In FY 2011, the SEC's total budgetary resources equaled \$1,713 million, an 8 percent increase over the FY 2010 amount of \$1,593 million. SEC's budgetary resources are mostly derived from the following sources: (1) unobligated balances brought forward, (2) recoveries of prior year unpaid obligations, and (3) offsetting collections (net of amounts temporarily not available pursuant to public law).

**CHART 1.7  
SOURCES OF FUNDS**



**Unobligated Balance Brought Forward.** The SEC's unobligated balance, brought forward was \$489 million for FY 2011, an increase of \$462 million over the FY 2010 total. The increase is primarily related to the carry forward of \$452 million in unobligated balances in the SEC's Investor Protection Fund.

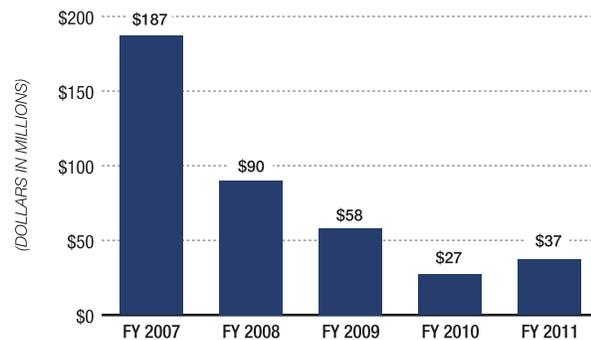
As detailed in *Chart 1.8, Unobligated Balance Brought Forward, General Funds – Salaries and Expenses*, the SEC has significantly reduced the amount of unobligated resources brought forward in its Salaries and Expenses Fund (X0100) since FY 2007.

**Recoveries of Prior Year Unpaid Obligations.** The SEC allocated significant resources to the review and de-obligation of unliquidated obligations from prior years during FY 2011. These efforts resulted in a \$20 million increase in recoveries when comparing FY 2010 to FY 2011.

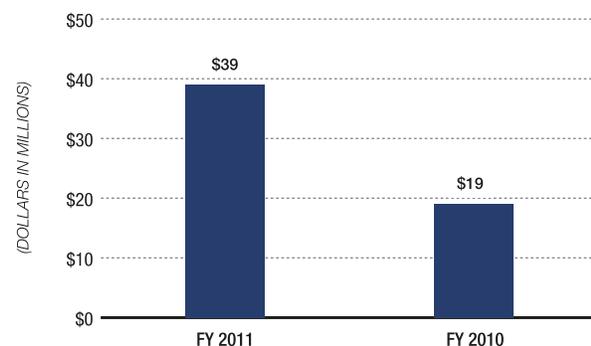
**TABLE 1.5  
TOTAL BUDGETARY RESOURCES FOR THE YEARS ENDED  
SEPTEMBER 30, 2011 AND 2010**

(DOLLARS IN MILLIONS)	FY 2011	FY 2010
Unobligated Balance, Brought Forward, October 1	\$ 489	\$ 27
Recoveries of Prior Year Unpaid Obligations	39	19
Appropriation – Investor Protection Fund	(1)	452
Spending Authority from Offsetting Collections, Earned, Collected	1,598	1,443
Amounts Temporarily not Available Pursuant to Public Law	(412)	(348)
<b>Total Budgetary Resources</b>	<b>\$ 1,713</b>	<b>\$ 1,593</b>

**CHART 1.8  
UNOBLIGATED BALANCE, BROUGHT FORWARD, GENERAL FUNDS  
— SALARIES AND EXPENSES**



**CHART 1.9  
RECOVERIES OF PRIOR YEAR UNPAID OBLIGATIONS**



**Offsetting Collections.** The SEC's budgetary authority from offsetting collections was \$1,598 for FY 2011. *Chart 1.10, Offsetting Collections vs. New Budgetary Authority*<sup>1</sup> presents the SEC's budgetary authority and offsetting collections related to transaction fees and filing fees from FY 2003 through 2011. Offsetting collections in excess of budgetary authority provided by Congress is recorded as Temporarily not Available Pursuant to Public Law on the Statement of Budgetary Resources and is not available for obligation until approved by Congress. The SEC's budgetary authority from fee collections was \$1,185 million for FY 2011.

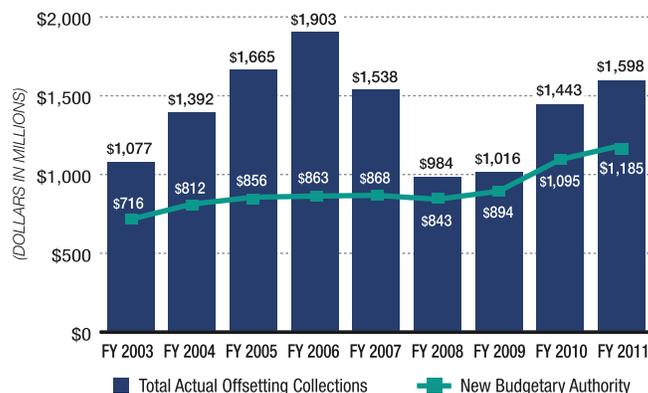
**Status of Budgetary Resources.** The SEC's Obligations Incurred increased by \$890 million or 81 percent during FY 2011. This increase was primarily related to the SEC's recognition of lease obligations totaling \$778 million to remedy issues noted in Comptroller General Decision B-322160, *Securities and Exchange Commission—Recording of Obligation for Multiple-Year Contract* and to accurately reflect the SEC's contractual obligations for leasing agreements in effect as of September 30, 2011. In addition, the SEC's Unobligated Balance decreased by \$769 million during FY 2011. This decrease was also attributable to the SEC's recognition of leasing obligations during FY 2011.

### Investor Protection Fund

The SEC prepares stand alone financial statements for the Investor Protection Fund as required by the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act). The financial statements are presented starting on page 157.

The Investor Protection Fund was established in the fourth quarter of FY 2010 to provide funding for a whistleblower award program and to finance the operations of the SEC Office of the Inspector General's Employee Suggestion Program. In FY 2010, \$452 million of non-exchange revenue was transferred to the Investor Protection Fund from SEC's disgorgement and penalties deposit fund. The \$452 million

**CHART 1.10**  
**OFFSETTING COLLECTIONS VS. NEW BUDGETARY AUTHORITY**  
SECTION 31 EXCHANGE AND FILING FEES



**TABLE 1.6**  
**INVESTOR PROTECTION FUND ACTIVITY**  
FOR THE YEARS ENDED SEPTEMBER 30, 2011 AND 2010

(DOLLARS IN THOUSANDS)	FY 2011	FY 2010
Balance of Fund at beginning of preceding fiscal year	\$451,910	\$ -
Amount deposited into or credited to the Fund during the preceding fiscal year	-	451,910
Amount of earnings on investments during the preceding fiscal year	990	-
Amount paid from the Fund during the preceding fiscal year to whistleblowers	-	-
Amount paid from the Fund during the preceding fiscal year for expenses incurred by Employee Suggestion Program	(112)	-
<b>Balance of the Fund at the end of the preceding fiscal year</b>	<b>\$ 452,788</b>	<b>\$ 451,910</b>

<sup>1</sup> *Chart 1.10 above only reflects offsetting collections related to fees collected on Section 31 securities transactions and Section 6(b), 13(e), 14(g), and 24f-2 filings and does not include reimbursable type collections and refunds as reported on the "Offsetting Collections" line of the Statement of Budgetary Resources.*

in fund assets represented Fund Balance with Treasury as of September 30, 2010. The \$452 million was invested in U.S. Treasury Securities during the first quarter of FY 2011.

The Investor Protection Fund recognized non-exchange revenues totaling \$990 thousand during FY 2011. The non-exchange revenue represents interest earnings on amounts invested in U.S. Treasury Securities. In addition, the Investor Protection Fund incurred expenses of \$112 thousand for salary and benefit cost in the OIG's Employee Suggestion Program.

Additional information regarding the Investor Protection Fund and the Office of the Whistleblower is available in the 2011 Annual Report on the Dodd-Frank Whistleblower Program. This report may be found at <http://www.sec.gov/whistleblower>.

## Limitations of the Financial Statements

The principal financial statements included in this report have been prepared by SEC Management to report the financial position and results of operations of the SEC, pursuant to the requirements of 31 U.S. Code Section 3515(b). While the statements have been prepared from the books and records of the SEC in accordance with GAAP for Federal entities and the formats prescribed by the Office of Management and Budget (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 understanding that they are for a component of the U.S. Government, a sovereign entity.

## Performance Highlights

This section provides key performance information for FY 2011. It outlines the SEC's strategic and performance planning framework, provides a brief discussion about how the SEC integrates its performance and budget data, and highlights the agency's progress toward reaching planned performance targets. Additionally, this section includes a list of performance indicators that provide useful information for understanding the agency's activities.

### Strategic and Performance Planning Framework

The SEC's FY 2011 strategic and performance planning framework, is based on the FY 2010 – FY 2015 Strategic Plan, available at <http://www.sec.gov/about/secstratplan1015f.pdf>. The Strategic Plan addresses the agency's mission, vision, values, and strategic goals and outcomes. The SEC's work is structured around four strategic goals, and 12 strategic outcomes that gauge the SEC's performance within each goal.

The SEC's goals and priorities in the Strategic Plan are influenced by several external environmental factors, including the demands of fulfilling the agency mission in complex and

global financial markets and changes in legislation affecting the agency. During the past few years, this environment has changed dramatically. While the Strategic Plan attempts to foresee various ways in which financial markets, regulated industries, and the legislative environment may change over time, no plan can anticipate all possible scenarios. Because the accompanying performance measures were significantly revised during the development of the FY 2010 – FY 2015 Strategic Plan, there is limited prior year performance information provided in this report.

TABLE 1.7

Strategic Goals with Resources Invested	Outcomes
<p><b>Foster and enforce compliance with the Federal securities laws</b></p> <p><b>Cost: \$622.9 million</b></p>	<p>The SEC fosters compliance with the Federal securities laws.</p> <p>The SEC promptly detects violations of the Federal securities laws.</p> <p>The SEC prosecutes violations of Federal securities laws and holds violators accountable.</p>
<p><b>Establish an effective regulatory environment</b></p> <p><b>Cost: \$126.4 million</b></p>	<p>The SEC establishes and maintains a regulatory environment that promotes high-quality disclosure, financial reporting, and governance, and prevents abusive practices by registrants, financial intermediaries, and other market participants.</p> <p>The U.S. capital markets operate in a fair, efficient, transparent, and competitive manner, fostering capital formation and useful innovation.</p> <p>The SEC adopts and administers rules and regulations that enable market participants to understand clearly their obligations under the securities laws.</p>
<p><b>Facilitate access to the information investors need to make informed investment decisions</b></p> <p><b>Cost: \$185.9 million</b></p>	<p>Investors have access to high-quality disclosure materials that are useful to investment decision making.</p> <p>Agency rulemaking and investor education programs are informed by an understanding of the wide range of investor needs.</p>
<p><b>Enhance the Commission's performance through effective alignment and management of human, information, and financial capital</b></p> <p><b>Cost: \$212.9 million</b></p>	<p>The SEC maintains a work environment that attracts, engages, and retains a technically proficient and diverse workforce that can excel and meet the dynamic challenges of market oversight.</p> <p>The SEC retains a diverse team of world-class leaders who provide motivation and strategic direction to the SEC workforce.</p> <p>Information within and available to the SEC becomes a Commission-wide shared resource, appropriately protected, that enables a collaborative and knowledge-based working environment.</p> <p>Resource decisions and operations reflect sound financial and risk management principles.</p>

## Performance Measures Overview

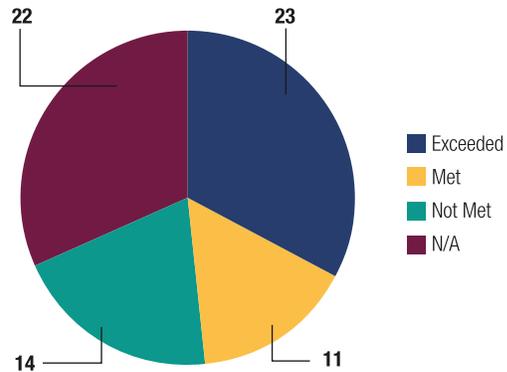
To assess the SEC's performance results against pre-established performance targets, a results rating methodology is used to assign one of the following three performance ratings for a given result:

Below Target	On Target	Above Target
Not Met	Met	Exceeded

The SEC's FY 2010 – FY 2015 Strategic Plan outlines 70 total performance targets. Several of these performance measures track multiple performance targets, and *Chart 1.11, Summary of FY 2011 Performance Results* shows the performance results for each of the 70 performance targets. Twenty-two of these targets are categorized as N/A if the performance target was not established or if FY 2011 data is not available. Several of these performance measures are under review as part of the FY 2011 Strategic Plan Addendum process in order to allow for more complete and accurate reporting.

The performance indicators, outlined in *Table 1.9, Performance Indicators Results Summary*, do not include planned targets because it would be inappropriate for the agency to conduct certain activities with an eye towards meeting predetermined targets. Therefore, results for performance indicators are not included in *Chart 1.11, Summary of FY 2011 Performance Results*.

**CHART 1.11  
SUMMARY OF FY 2011 PERFORMANCE RESULTS**



## Performance Results Summary

The SEC has established a series of performance measures for assessing program performance against strategic goals and planned outcomes. For each performance measure, one or more performance targets have been established. *Table 1.8, Performance Measures Results Summary* provides a summary of actual performance results during FY 2010 and FY 2011 for each performance measure, and *Table 1.9, Performance Indicators Results Summary* provides a summary of indicators by outcome within each strategic goal. A detailed discussion of the agency's program achievements and performance results is located in the *Performance Section* beginning on page 51.

TABLE 1.8

PERFORMANCE MEASURES RESULTS SUMMARY				
GOAL 1: Foster and Enforce Compliance with the Federal Securities Laws				
OUTCOME 1.1: The SEC fosters compliance with the Federal securities laws.	FY 2010 Actual	FY 2011 Target	FY 2011 Actual	FY 2011 Results
<b>MEASURE 1:</b> Number of new investor education materials designed specifically to help investors protect themselves from fraud	16	24	24	Met
<b>MEASURE 2:</b> Number of industry outreach and education programs targeted to areas identified as raising particular compliance risks	6	10	5	Not Met
<b>MEASURE 3:</b> Percentage of firms receiving deficiency letters that take corrective action in response to all exam findings	90%	90%	93%	Exceeded
<b>MEASURE 4:</b> Percentage of attendees at CCO outreach that rated the program as "Useful" or "Extremely Useful" in their compliance efforts	77%	80%	86%	Exceeded
OUTCOME 1.2: The SEC promptly detects violations of the Federal securities laws.	FY 2010 Actual	FY 2011 Target	FY 2011 Actual	FY 2011 Results
<b>MEASURE 5:</b> Percentage of cause and special exams (sweeps) conducted as a result of risk assessment process that includes multi-divisional input	N/A	N/A	N/A	N/A
<b>MEASURE 6:</b> Percentage of advisers deemed "high risk" examined during the year	N/A	N/A	N/A	N/A
<b>MEASURE 7:</b> Percentage of registrant population examined during the year:				
Investment advisers	9%	11%	8%	Not Met
Investment companies	10%	11%	13%	Exceeded
Broker-dealers (exams by SEC and SROs)	44%	45%	42%	Not Met
<b>MEASURE 8:</b> Percentage of non-sweep and non-cause exams that are concluded within 120 days	48%	50%	53%	Exceeded
OUTCOME 1.3: The SEC prosecutes violation of Federal securities laws and holds violators accountable.	FY 2010 Actual	FY 2011 Target	FY 2011 Actual	FY 2011 Results
<b>MEASURE 9:</b> Percentage of enforcement actions successfully resolved	92%	92%	93%	Exceeded
<b>MEASURE 10:</b> Percentage of first enforcement actions filed within two years	67%	70%	61%	Not Met
<b>MEASURE 11:</b> Percentage of debts where either a payment has been made or a collection activity has been initiated within six months of the due date of the debt	86%	90%	91%	Exceeded
<b>MEASURE 12:</b> Percentage of Fair Fund and disgorgement fund plans that distributed the final tranche of funds to injured investors within 24 months of the order appointing the fund administrator	N/A	N/A	N/A	N/A
<b>MEASURE 13:</b> Percentage of Fair Fund and disgorgement fund plans approved by final order within the prior fiscal year which had a first tranche of funds distributed under those plans within 12 months of such approval date	N/A	N/A	N/A	N/A

N/A – Signifies data does not currently exist or targets were not established

(Continued on next page)

TABLE 1.8 *Continued from previous page*

<b>PERFORMANCE MEASURES RESULTS SUMMARY</b> <i>(continued)</i>				
<b>GOAL 2: Establish an Effective Regulatory Environment</b>				
<b>OUTCOME 2.1: The SEC establishes and maintains a regulatory environment that promotes high-quality disclosure, financial reporting, and governance, and that prevents abusive practices by registrants, financial intermediaries, and other market participants.</b>	<b>FY 2010 Actual</b>	<b>FY 2011 Target</b>	<b>FY 2011 Actual</b>	<b>FY 2011 Results</b>
<b>MEASURE 1:</b> Survey on quality of disclosure	N/A	N/A	N/A	N/A
<b>MEASURE 2:</b> Number of consultations; joint events, reports, or initiatives; and joint examinations and other mutual supervisory efforts with SROs and other Federal, state, and non-U.S. regulators	N/A	N/A	N/A	N/A
<b>MEASURE 3:</b> Number of non-U.S. regulators trained	1,997	2,020	1,765	Not Met
<b>OUTCOME 2.2: The U.S. capital markets operate in a fair, efficient, transparent, and competitive manner, fostering capital formation and useful innovation.</b>	<b>FY 2010 Actual</b>	<b>FY 2011 Target</b>	<b>FY 2011 Actual</b>	<b>FY 2011 Results</b>
<b>MEASURE 4:</b> Percentage of transaction dollars settled on time each year	99%	99%	99%	Met
<b>MEASURE 5:</b> Average institutional transaction costs for exchange listed stocks on a monthly basis	N/A	N/A	N/A	N/A
<b>MEASURE 6:</b> Percentage of market outages at SROs and electronic communications networks (ECNs) that are corrected within targeted timeframes:				
Within 2 hours	74%	60%	88%	Exceeded
Within 4 hours	85%	75%	94%	Exceeded
Within 24 hours	100%	96%	100%	Exceeded
<b>OUTCOME 2.3: The SEC adopts and administers rules and regulations that enable market participants to understand clearly their obligations under the securities laws.</b>	<b>FY 2010 Actual</b>	<b>FY 2011 Target</b>	<b>FY 2011 Actual</b>	<b>FY 2011 Results</b>
<b>MEASURE 7:</b> Length of time to respond to written requests for no-action letters, exemptive applications, and written interpretive requests				
Trading and Markets – No-action letters, exemptive applications, and written interpretive requests (combined figure)	91%	85%	98.5%	Exceeded
Investment Management – No-action letters and interpretive requests	100%	75%	100%	Exceeded
Investment Management – Exemptive applications	100%	80%	100%	Exceeded
Corporation Finance – No-action letters and interpretive requests	97%	90%	97%	Exceeded
Corporation Finance – Shareholder proposals	100%	100%	100%	Met
<b>MEASURE 8:</b> Survey on whether SEC rules and regulations are clearly understandable	N/A	N/A	N/A	N/A
<b>MEASURE 9:</b> Time to complete SEC review of SRO rules that are subject to SEC approval				
Within 35 days	73%	40%	0%	Not Met
Within 45 days	99%	80%	82%	Exceeded

N/A – Signifies data does not currently exist or targets were not established

*(Continued on next page)*

**TABLE 1.8** *Continued from previous page*

<b>PERFORMANCE MEASURES RESULTS SUMMARY</b> <i>(continued)</i>				
<b>GOAL 3: Facilitate Access to the Information Investors Need to Make Informed Investment Decisions</b>				
<b>OUTCOME 3.1: Investors have access to high-quality disclosure materials that are useful to investment decision making.</b>	<b>FY 2010 Actual</b>	<b>FY 2011 Target</b>	<b>FY 2011 Actual</b>	<b>FY 2011 Results</b>
<b>MEASURE 1:</b> Percentage of public companies and investment companies with disclosures reviewed each year				
Corporations	44%	33%	48%	Exceeded
Investment company portfolios	35%	33%	33%	Met
<b>MEASURE 2:</b> Time to issue initial comments on Securities Act filings	24.1 days	< 30 days	24.4 days	Met
<b>MEASURE 3:</b> Percentage of investment company disclosure reviews for which initial comments are completed within timeliness goals				
Initial registration statements	93%	85%	92%	Exceeded
Post-effective amendments	94%	90%	94%	Exceeded
Preliminary proxy statements	99%	99%	98%	Not Met
<b>MEASURE 4:</b> Point of sale "click-through rate"	N/A	N/A	N/A	N/A
<b>MEASURE 5:</b> Access to broker-dealer and investment adviser background checks				
BrokerCheck System	N/A	N/A	N/A	N/A
IAPD System	N/A	N/A	N/A	N/A
<b>MEASURE 6:</b> Investor demand for disclosures on municipal securities	N/A	N/A	N/A	N/A
<b>MEASURE 7:</b> Satisfaction index for disclosure process	N/A	N/A	N/A	N/A
<b>OUTCOME 3.2: Agency rulemaking and investor education programs are informed by an understanding of the wide range of investor needs.</b>	<b>FY 2010 Actual</b>	<b>FY 2011 Target</b>	<b>FY 2011 Actual</b>	<b>FY 2011 Results</b>
<b>MEASURE 8:</b> Number of investors reached, and number of in-person events with specifically targeted communities and organizations				
Number of investors reached (in millions)	17.8	16	14.8	Not Met
Number of in-person events	42	30	48	Exceeded
<b>MEASURE 9:</b> Number of investor educational initiatives organized and produced	9	10	11	Exceeded
<b>MEASURE 10:</b> Timeliness of responses to investor contacts				
Closed within 7 days	72%	80%	67%	Not Met
Closed within 30 days	93%	90%	92%	Exceeded
<b>MEASURE 11:</b> Percentage of rules impacting investors that are presented in alternate user-friendly formats	100%	100%	100%	Met
<b>MEASURE 12:</b> Customer satisfaction with usefulness of investor educational programs and materials	N/A	N/A	N/A	N/A

*N/A – Signifies data does not currently exist or targets were not established*

*(Continued on next page)*

TABLE 1.8 *Continued from previous page*

<b>PERFORMANCE MEASURES RESULTS SUMMARY</b> <i>(continued)</i>				
<b>GOAL 4: Enhance the Commission's Performance Through Effective Alignment and Management of Human, Information, and Financial Capital</b>				
<b>OUTCOME 4.1: The SEC maintains a work environment that attracts, engages, and retains a technically proficient and diverse workforce that can excel and meet the dynamic challenges of market oversight.</b>	<b>FY 2010 Actual</b>	<b>FY 2011 Target</b>	<b>FY 2011 Actual</b>	<b>FY 2011 Results</b>
<b>MEASURE 1:</b> Survey of employee engagement	58%	65%	61%	Not Met
<b>MEASURE 2:</b> Best Places to Work ranking	Ranked #24	Ranked #5	N/A	N/A
<b>MEASURE 3:</b> Turnover	5%	< 8%	6.4%	Met
<b>MEASURE 4:</b> Expanding staff expertise	N/A	N/A	9%	N/A
<b>MEASURE 5:</b> Size of competency gaps	N/A	10%	N/A	N/A
<b>MEASURE 6:</b> Number of diversity-related partnerships/alliances	2	5	10	Exceeded
<b>MEASURE 7:</b> Survey feedback on the quality of the SEC's performance management program	N/A	65%	53%	Not Met
<b>OUTCOME 4.2: The SEC retains a diverse team of world-class leaders who provide motivation and strategic direction to the SEC workforce.</b>	<b>FY 2010 Actual</b>	<b>FY 2011 Target</b>	<b>FY 2011 Actual</b>	<b>FY 2011 Results</b>
<b>MEASURE 8:</b> Quality of hire	N/A	75%	N/A	N/A
<b>MEASURE 9:</b> Leadership competency gaps	N/A	10%	N/A	N/A
<b>MEASURE 10:</b> Satisfaction with Leadership Development Program (5-point scale)	4.46	4.5	4.49	Not Met
<b>OUTCOME 4.3: Information within and available to the SEC becomes a Commission-wide shared resource, appropriately protected, that enables a collaborative and knowledge-based working environment.</b>	<b>FY 2010 Actual</b>	<b>FY 2011 Target</b>	<b>FY 2011 Actual</b>	<b>FY 2011 Results</b>
<b>MEASURE 11:</b> Percentage of SEC data sources accessible through a virtual data warehouse, and milestones achieved towards the creation of a robust information management program	N/A	N/A	N/A	N/A
<b>MEASURE 12:</b> Deployment of document management and workflow tools	Enforcement and Examination	Tips, Complaints and Referrals Commission-wide	Tips, Complaints and Referrals Commission-wide	Met
<b>MEASURE 13:</b> Time to process evidentiary material for enforcement investigations	N/A	N/A	N/A	N/A
<b>MEASURE 14:</b> System availability				
Systems availability	99.97%	99.3%	99.94%	Exceeded
Percentage fail over within 4 hours	N/A	100%	0%	Not Met
Systems virtualized	22%	25%	38%	Exceeded
<b>OUTCOME 4.4: Resource decisions and operations reflect sound financial and risk management principles.</b>	<b>FY 2010 Actual</b>	<b>FY 2011 Target</b>	<b>FY 2011 Actual</b>	<b>FY 2011 Results</b>
<b>MEASURE 15:</b> Milestones achieved towards establishment of a robust data management program	N/A	Administrative Data and Reporting Requirements Identified	Administrative Data and Reporting Requirements Identified	Met
<b>MEASURE 16:</b> Financial Systems Integration	N/A	17%	N/A	N/A
<b>MEASURE 17:</b> Financial Audit Results				
Unqualified opinion	Yes	Yes	Yes	Met
Material weaknesses	2	0	0	Met
Significant deficiency	0	0	4	Not Met

N/A – Signifies data does not currently exist or targets were not established

TABLE 1.9

<b>PERFORMANCE INDICATORS RESULTS SUMMARY</b>		
<b>GOAL 1: Foster and Enforce Compliance with the Federal Securities Laws</b>		
<b>OUTCOME 1.1: The SEC fosters compliance with the Federal securities laws.</b>	<b>FY 2010 Actual</b>	<b>FY 2011 Actual</b>
<b>INDICATOR 1:</b> Percentage of actions identified as "high impact" which have resulted in significant corrective industry reaction	N/A	N/A
<b>INDICATOR 2:</b> Annual increases or decreases in the number of CCOs attending CCO outreach programs	N/A	N/A
<b>OUTCOME 1.2: The SEC promptly detects violations of the Federal securities laws.</b>	<b>FY 2010 Actual</b>	<b>FY 2011 Actual</b>
<b>INDICATOR 3:</b> Percentage of exams that identify deficiencies, and the percentage that result in a "significant finding"		
Percentage identify deficiencies	72%	82%
Percentage that result in a "significant finding"	42%	42%
<b>INDICATOR 4:</b> Number of investigations or cause exams from tips:		
Number of investigations	303	349
Number of cause exams	N/A	N/A
<b>OUTCOME 1.3: The SEC prosecutes violations of Federal securities laws and holds violators accountable.</b>	<b>FY 2010 Actual</b>	<b>FY 2011 Actual</b>
<b>INDICATOR 5:</b> SEC investigations referred to SROs or other state, Federal, and foreign authorities for enforcement	492	586
<b>INDICATOR 6:</b> Percent of all enforcement investigations deemed "high impact"	3.26%	5.11%
<b>INDICATOR 7:</b> Percent of investigations that come from internally-generated referrals or prospects	21.9%	18.5%
<b>INDICATOR 8:</b> Criminal investigations relating to SEC investigations	139	134
<b>INDICATOR 9:</b> Disgorgement and penalties ordered and the amounts collected by the SEC:		
Ordered amounts (in millions)	\$2,846	\$2,806
Collected amounts (in millions)	\$1,775	\$1,281
<b>INDICATOR 10:</b> Requests from foreign authorities for SEC assistance and SEC requests for assistance from foreign authorities		
Number of requests from foreign authorities	457	492
Number of SEC requests	605	772
<b>GOAL 2: Establish an Effective Regulatory Environment</b>		
<b>OUTCOME 2.1: The SEC establishes and maintains a regulatory environment that promotes high-quality disclosure, financial reporting and governance, and that prevents abusive practices by registrants, financial intermediaries, and other market participants.</b>	<b>FY 2010 Actual</b>	<b>FY 2011 Actual</b>
<b>INDICATOR 1:</b> Average cost of capital in U.S. relative to the rest of the world	10.99%	10.67%
<b>OUTCOME 2.2: The U.S. capital markets operate in a fair, efficient, transparent and competitive manner, fostering capital formation and useful innovation.</b>	<b>FY 2010 Actual</b>	<b>FY 2011 Actual</b>
<b>INDICATOR 2:</b> Average quoted spread for exchange listed stocks on a monthly basis (in cents)	2.52	1.76
<b>INDICATOR 3:</b> Average effective spread for exchange listed stocks on a monthly basis (in cents)	2.65	1.72
<b>INDICATOR 4:</b> Speed of execution (in seconds)	1.77	1.02
<b>INDICATOR 5:</b> Average quoted size of exchange listed stocks on a monthly basis	687	606
<b>INDICATOR 6:</b> Average daily volatility of exchange listed stocks on a monthly basis	1.18%	1.26%
<b>OUTCOME 2.3: The SEC adopts and administers rules and regulations that enable market participants to understand clearly their obligations under the securities laws.</b>	<b>FY 2010 Actual</b>	<b>FY 2011 Actual</b>
<b>INDICATOR 7:</b> Percentage of SRO rule filings that are submitted for immediate effectiveness	69%	77%
<i>N/A – Signifies data does not currently exist for existing or newly added measures</i>		

## Management Assurances

The SEC is firmly committed to building and maintaining strong internal controls. Internal control is an integral component of effective agency management, providing reasonable assurance that the following objectives are being achieved: effectiveness and efficiency of operations, reliability of financial reporting, and compliance with laws and regulations. The Federal Managers' Financial Integrity Act of 1982 (FMFIA) provides the statutory basis for management's responsibility for and assessment of internal accounting and administrative controls. Such controls include program, operational, and administrative areas, as well as accounting and financial management. The FMFIA requires Federal agencies to establish controls that reasonably ensure obligations and costs are in compliance with applicable law; funds, property, and other assets are safeguarded against waste, loss, unauthorized use, or misappropriation; and revenues and expenditures are properly recorded and accounted for to maintain accountability over the assets. The FMFIA also requires agencies to annually assess and report on the internal controls that protect the integrity of Federal programs (FMFIA § 2) and whether financial management systems conform to related requirements (FMFIA § 4).

Guidance for implementing the FMFIA is provided through Office of Management and Budget (OMB) Circular A-123. In addition to requiring agencies to provide an assurance statement on the effectiveness of programmatic internal controls and financial system conformance, the Circular requires agencies to provide an assurance statement on the effectiveness of internal control over financial reporting.

In addition, Section 963 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act) describes the responsibility of SEC management to establish and maintain adequate internal controls and procedures for financial reporting. The Dodd-Frank Act requires an annual financial controls audit, an assessment of the effectiveness of internal control, and an attestation by the Chairman and Chief Financial Officer. Section 922 of the Dodd-Frank Act requires the SEC to submit audited financial statements of the Investor Protection Fund, to the Committee on Banking, Housing and Urban Affairs of the Senate and the Committee on Financial Services of the House of Representatives.

The following Assurance Statement is issued in accordance with the FMFIA, OMB Circular A-123 and Sections 922 and 963 of the Dodd-Frank Act.

### Annual Assurance Statement

**Assurance Statement Under FMFIA:** The management of the SEC 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. In accordance with OMB Circular A-123, the SEC conducted its annual assessment of the effectiveness of internal controls. Based on the results of the assessment for the period ending September 30, 2011, the SEC is able to provide an unqualified statement of assurance that internal controls and the financial systems, both for the agency as a whole and for the Investor Protection Fund, meet the objectives of the FMFIA. No material weaknesses were found in the design or operation of the internal controls for the fiscal year ended September 30, 2011.

**Assurance Statement On Internal Controls Over Financial Reporting:** In accordance with Appendix A of OMB Circular A-123, the SEC conducted its assessment of the effectiveness of internal control over financial reporting, which includes safeguarding of assets and compliance with applicable laws and regulations. Based on the results of the assessment, the SEC is able to provide reasonable assurance that internal controls over financial reporting, both for the agency as a whole and for the Investor Protection Fund, met the objectives of FMFIA and were operating effectively as of September 30, 2011, and that no material weaknesses were found in the design or operation of the controls.



**Mary Schapiro**

Chairman

November 14, 2011



**Kenneth A. Johnson**

Chief Financial Officer

November 14, 2011

## Management's Responsibility for Internal Control

FMFIA requires the head of the agency, based on the agency's internal evaluation, to provide an annual Statement of Assurance on the effectiveness of their management, administrative, and financial reporting controls. OMB Circular A-123, *Management's Responsibility for Internal Control*, implements the FMFIA and defines management's responsibility for internal control in Federal agencies.

FMFIA § 2 requires agencies to establish internal controls and financial systems that provide reasonable assurance that the following objectives are achieved:

- Effective and efficient operations,
- Compliance with applicable laws and regulations, and
- Reliability of financial reporting.

FMFIA § 4 requires that agencies annually evaluate and report on whether financial management systems conform to Government-wide requirements. The SEC evaluated its financial management systems for the fiscal year ending September 30, 2011, in accordance with the Federal Financial Management Improvement Act of 1996 (FFMIA) and OMB Circular A-127, *Financial Management Systems*, as applicable.

Appendix A of OMB Circular A-123 requires the agency head to provide a separate statement of assurance on the effectiveness of internal control over financial reporting (ICFR), in addition to the overall FMFIA assurance statement. The 2011 annual assurance statements for FMFIA and ICFR are provided on the preceding page. This report also provides a Summary of Financial Statement Audits and Management Assurances under the section entitled Other Accompanying Information, as required by OMB Circular A-136, *Financial Reporting Requirements*.

As part of the overall FMFIA assurance process, SEC management assessed internal control at the entity-level, as well as at the process, transaction, and application level. To assess the effectiveness of entity-level controls, SEC management used the Government Accountability Office's

(GAO) document, titled *Internal Control Management and Evaluation Tool* (GAO-01-1008G) to define entity-level control objectives. SEC management then identified changes to control activities from the prior year that addressed each control objective. Information on these entity-level control activities was gathered through meetings with relevant points of contact and feedback in the form of survey responses from SEC supervisors. Entity-level control activities were also evaluated based on risk and control documentation, as well as the assessments conducted by the divisions and offices for providing management assurances over the effectiveness of programmatic and operational controls and compliance with laws and regulations.

The effectiveness of process-level controls was assessed through detailed test procedures related to the agency's financial reporting objectives. As part of this effort, the agency performed a comprehensive risk assessment in which SEC management identified:

- Significant financial reports and materiality;
- Significant line items, accounts, disclosures, and laws and regulations;
- Major classes of transactions;
- Relevant assertions, risks of material misstatement and control objectives;
- Reporting and regulatory requirements; and
- Existing deficiencies and corrective action plans.

From the results of the risk assessment, SEC management updated documentation of the business processes and control activities designed to mitigate significant financial reporting and compliance risks. These control activities were tested for design and operating effectiveness. The agency also tested for operating effectiveness those control activities that were found deficient in prior years and remediated in FY 2011. The test results served as a basis for management's assessment of the effectiveness of internal control over financial reporting.

<sup>1</sup> A significant deficiency is a deficiency, or combination of deficiencies, in internal control that is less severe than a material weakness yet important enough to merit attention by those charged with governance.

<sup>2</sup> A material weakness is a deficiency, or combination of deficiencies, such that there is a reasonable possibility that a material misstatement of the financial statements or other significant financial reports, will not be prevented, detected, or corrected on a timely basis.

SEC management analyzed the internal control deficiencies, both individually and in the aggregate, to determine if a significant deficiency<sup>1</sup> or a material weakness<sup>2</sup> exists in the financial reporting processes. Significant factors considered for assessing each deficiency included the following:

- Nature of the control deficiency (e.g., design, operation);
- Internal control objectives and activities impacted;
- Potential impact on financial statement line items, accounts, and disclosures;
- The interaction of control deficiencies with other deficiencies; and
- The materiality of account balances impacted by the deficiency.

In addition, each division director and office head provided a statement of assurance identifying any internal control weaknesses or management challenges related to the effectiveness of the controls over programs and operations, and compliance with laws and regulations. These statements were based on information gathered from various sources including, among other things:

- Internal management reviews, self-assessments, and tests of internal controls;
- Management's personal knowledge gained from daily operations;
- Reports from the GAO and the SEC's Office of Inspector General (OIG);
- Reviews of financial management systems under OMB Circular A-127, Financial Management Systems;
- Annual performance plans and reports pursuant to the Federal Information Security Management Act (FISMA) and OMB Circular A-130, Management of Federal Information Resources;
- Annual reviews and reports pursuant to the Improper Payments Elimination and Recovery Act;
- Reports and other information from Congress or agencies such as OMB, the Office of Personnel Management (OPM), or the General Services Administration (GSA) reflecting the adequacy of internal controls; and

- Additional reviews relating to a division or office's operations, including those discussed in the Other Reviews section below.

Each year, the agency's Financial Management Oversight Committee advises the Chairman as to whether the SEC had any deficiencies in internal control or financial system design significant enough to be reported as a material weakness or non-conformance. This advice is based on the assurance statements from directors and office heads and other supplemental sources of information. Among other factors, the SEC considered the implications of Antideficiency Act violations in FY 2010 and previous years related to a GAO opinion on the SEC's leasing program, which is discussed in *Note 14.C. Other Budgetary Disclosures*.

## Other Reviews

GAO audited the SEC's financial statements. The objective of GAO's audit was to express an opinion on the financial statements and on internal control over financial reporting and to report on tests of compliance with selected laws and regulations.

The OIG conducted 14 audits and reviews during the fiscal year. The reviews covered 17 of the 35 assessable units (49 percent). Some components had multiple reviews.

## Status of Prior Year Internal Control over Financial Reporting Issues

The SEC's FY 2010 financial audit and ICFR assessment identified two material weaknesses in internal control over financial reporting, one in information systems and a second in financial reporting and accounting processes. The second material weakness resulted from the combination of five significant deficiencies.

Based on the agency's continued efforts to address prior year audit findings and ICFR weaknesses, the agency successfully remediated both material weaknesses. The issues disclosed in the FY 2010 PAR related to disgorgement and penalty transactions and required supplementary information were either fully remediated or reduced to control deficiencies as a result of the remedial actions that were focused on strengthening controls and improving management's monitoring and oversight. Although the agency has four significant deficiencies, in the areas of financial reporting, budgetary resources, filing

fees, and IT security, the agency made significant improvement in addressing these four deficiency areas. In addition, the agency continued in FY 2011 to perform a robust internal control assessment and improved its process to effectively manage, track, monitor and test key risks and controls.

Below is a summary of the agency's efforts to remediate the six areas that constituted the two material weaknesses in FY 2010.

**Information Systems.** In FY 2011, the SEC successfully remediated its material weakness in the area of information systems and reduced it to the level of a significant deficiency. The SEC undertook corrective actions in FY 2011 to address information technology and security control weaknesses which spanned across its general support system and key applications.

During FY 2011, the Office of Information Technology (OIT) updated patches across the agency's financial systems and improved backup processes to ensure the recovery of critical financial data. OIT also continued to aggressively work to resolve outstanding information security control deficiencies identified by management through its certifications and accreditations and by prior-year audits. The SEC improved its monitoring capability over system configuration changes, so that all changes to system requirements, design, and scripts are evaluated by a Configuration Control Board on the basis of cost, benefits, and risk to the agency. Future system upgrades are documented to show both the impact on security and evidence of approval by the Board. The agency also made notable progress with respect to user access controls and segregation of duties.

New and residual deficiencies were identified during the SEC's FY 2011 assessment including dated security risk management procedures, inconsistent continuous monitoring processes to support FISMA requirements, user account control gaps, and further improvements needed in the patch management process. These areas will be a priority for remediation in FY 2012.

**Disgorgement and Penalties.** The SEC successfully remediated this significant deficiency, through efforts to improve the controls and procedures that ensure that accounts receivables and payments related to disgorgements and penalties were recorded accurately and in the proper accounting period.

Some of the improved control activities implemented by the SEC were as follows:

- Instituting a more comprehensive monthly review of Court Link/Lexis Nexus for valid judgments/court orders against new and existing SEC civil cases for new receivables or subsequent transfer orders;
- Implementing procedures to age receivables and to record post-judgment interest;
- Establishing a new process for recording deposits in transit to ensure all checks received are recognized in the proper accounting period; and
- Implementing an automated interface between the SEC's current core financial system and the Bureau of Public Debt's FedInvest system to record purchases and redemptions for tracking investments at the detailed level held in the Disgorgement Deposit Fund account.

New and residual deficiencies were identified during the SEC's FY 2011 assessment, but these deficiencies, even when considered in aggregate, do not rise to the level of a significant deficiency.

**Required Supplementary Information.** In FY 2011, the SEC successfully resolved its previous significant deficiency regarding the required supplemental information, particularly with respect to the new Investor Protection Fund. The SEC prepared the required supplementary information during FY 2011, and formalized the process of performing a detailed review of OMB Circular A-136 *Financial Reporting Requirements* and other relevant guidance to ensure that such requirements are properly reflected in the agency's financial statements.

**Financial Reporting.** This process area continues to have a significant deficiency in FY 2011. Many of the agency's financial reporting processes are still manual in nature and reliant on spreadsheets and databases to both initiate transactions and perform key control functions.

During FY 2011, the SEC was able to reduce the number of manual processes by tracking investments at the detail level within the financial system and building an automated interface with the Bureau of Public Debt for handling investments. In addition, SEC reduced the number of manual journal vouchers by implementing the use of standard

vouchers for recurring types of journal vouchers. The agency implemented a remediation plan to control its user developed applications (UDAs), such as Microsoft Access databases and spreadsheets, based on risk.

While the SEC made significant improvement in this area, the agency still continues to have deficiencies related to financial reporting. Most notably, the agency's remediation related to UDAs went into effect late in the fiscal year, and thus for most of FY 2011, the UDAs were not subject to the newly required controls as appropriate to ensure that manual compensating controls are operating effectively. OFM plans to continue to assess its UDAs and to strengthen the controls associated with those UDAs.

**Budgetary Resources.** This process area continues to have a significant deficiency in FY 2011. The SEC continued its efforts to ensure the correct use of posting models and developed new policies and procedures related to posting obligations, funds reservations, and monitoring open obligations.

During FY 2011, the agency found continuing issues, specifically in the design and operation of controls to:

- Record obligations and adjustments to obligations accurately and on a timely basis, upon contract execution.
- Ensure completeness of recorded obligations between the core financial reporting and sub-ledger systems.
- Ensure that open obligations identified by the divisions and offices as no longer needed are timely de-obligated by the contracting officer per the closeout procedures contained in the Federal Acquisition Regulation.

The SEC will continue to refine its business processes in this area in FY 2012. Most notably, the agency's controls over budgetary resources will be significantly enhanced through integration of procurement and financial systems, which the agency aims to achieve as part of the migration to a Federal Shared Service Provider (FSSP).

**Filing Fees.** This process area continues to have a significant deficiency in FY 2011 related to timeliness of recording revenues and the backlog of inactive registrant accounts with balances. The agency moved on multiple fronts to remediate these deficiencies, such as eliminating a backlog of offering and verification reviews of fees, resolving thousands of registrant deposit accounts, and implementing a quarterly statistical

analysis to enhance the accuracy of financial reporting related to filing fees.

As of September 30, 2011, the control activities still need to be improved to routinely review, research, and monitor registrant deposit account activity to determine if amounts should be refunded or recognized as revenue. The processes for continuous monitoring and sustaining these efforts will be finalized and formalized in FY 2012.

The SEC will continue its efforts to resolve the backlog of inactive deposit accounts and maintain the timeliness of the review and verification of filing fees. In addition, the SEC will continue to develop and implement long term enhancements, such as business process redesign and enhancements to the systems supporting these processes. With these remediation efforts, the SEC intends to ensure that registrant filings and deposits are matched on a timely basis, revenues are recorded in the period earned, and there is no backlog of dormant registrant deposit accounts.

## Financial Management System Conformance

The FFMI A requires that each agency shall implement and maintain financial management systems that comply substantially with Federal financial management systems requirements, applicable Federal accounting standards, and the U.S. Standard General Ledger at the transaction level. The purpose of the FFMI A is to advance Federal financial management by ensuring that financial management systems provide accurate, reliable, and timely financial management information. Although the SEC is exempt from the requirement to determine substantial compliance with FFMI A, the agency assesses its financial management systems annually for conformance with the requirements of OMB Circular A-127 and other Federal financial system requirements.

The SEC's process for assessing its financial management systems is in compliance with the January 9, 2009 revision of OMB Circular A-127 and included the use of an FFMI A risk model that ranks risks from nominal to significant. Based on the results of the review, the SEC concluded that its risk rating is nominal. After reviewing the criteria in OMB Circular A-127 for agencies with nominal risk, the SEC determined its financial core and mixed systems are in substantial compliance with Section 803(a) of the FFMI A requirements. This decision was based on notable progress made in implementing corrective

actions in response to the material weakness in information systems noted in FY 2010.

### **Summary of Current Financial System and Future Strategies**

The SEC's current financial management system environment is characterized by a core financial system that has some gaps in functionality; silo applications providing key financial management functionality; external data marts with embedded business logic used for reporting; and processes that rely extensively on human capital for data entry, cleansing, and reconciliation. The SEC's core financial system, Momentum Version 6.1.5, is used to record all accounting transactions, maintain an agency-wide general ledger, produce financial reports, and generate external reports submitted periodically to Treasury and other Federal entities. The core financial system has automated interfaces with mixed systems such as the Budget Planning and Performance Management System for budget formulation and execution; the Central Contractor Registry for SEC vendor information; FedTraveler for travel orders and vouchers; Fee Momentum for the agency's filing fees; and the Department of the Interior's payroll systems. The agency's financial reporting and processes are dependent upon a number of Microsoft Access databases, such as those related to disgorgements and penalties receivables, financial reporting and analysis, payments to harmed investors, and accounts payable accruals.

During FY 2011, the agency began its migration to an OMB-designated FSSP to replace its core financial system. Through this initiative, the SEC seeks to automate some manual, non-integrated financial sub-processes and adopt standard business and technology practices. Accordingly, during FY 2011, the SEC signed two Inter-Agency Agreements (IAA) with the Enterprise Service Center of the U.S. Department of Transportation (DOT) for the Planning and Requirements Gathering and the Implementation Phases of this migration. The SEC has worked throughout FY 2011 with the DOT FSSP team to develop detailed requirements in order to cut over to the new system in FY 2012.

### **Federal Information Security Management Act (FISMA)**

FISMA requires Federal agencies to conduct annual assessments of their information security and privacy programs, to develop and implement remediation efforts for identified weaknesses and vulnerabilities, and to report compliance to OMB. The SEC's Office of the Inspector General (OIG), Chief Information Security Officer, and Privacy Officer are performing a joint review of the agency's compliance with FISMA requirements during 2011, and will submit the report to OMB on November 15, 2011, as required.

In FY 2011, OIT, in conjunction with system owners, completed assessment and authorization activities for 22 reportable systems, including annual assessments of systems such as the Momentum core financial system. As a result, the SEC has now assessed and authorized a total of 59 reportable systems in accordance with OMB policy and guidance from the National Institute of Standards and Technology (NIST). OIT also completed contingency testing on the majority of the SEC's authorized systems as part of several disaster recovery exercises.

OIT, in conjunction with system owners, completed 58 privacy reviews during FY 2011. The privacy reviews included Privacy Impact Assessments (PIA) on 14 required systems.

# PERFORMANCE SECTION



**T**he U.S. Securities and Exchange Commission's (SEC) performance data provides a foundation for both programmatic and organizational decision-making and is an essential part of the agency's strategic planning and performance measurement program. The SEC is committed to using performance management best practices to achieve critical strategic outcomes, and to promote greater accountability to our primary stakeholders, the American people.

At the SEC, strategic planning and performance management is a multi-phase process: setting strategic goals and priorities; identifying strategic outcomes and creating programs to achieve them; measuring and monitoring program activities; collecting data and tracking progress toward achievement of strategic goals; using performance information to influence program and resource allocation decision-making; and communicating results to stakeholders. These steps are designed to improve the management and performance of the SEC, with a focus on delivering results.

The Performance Section of this report contains, among other things, the SEC's fiscal year (FY) 2011 performance targets and results achieved against those targets. This section is intended to communicate the agency's progress in achieving strategic goals and outcomes, the tangible public benefits the SEC has produced this fiscal year, and the specific program accomplishments.

## A Reader's Guide to the SEC's Performance Information

---

This section provides performance information for each of the agency's four strategic goals in accordance with the SEC's Strategic Plan for FY 2010 – FY 2015:

- (1) Foster and enforce compliance with the Federal securities laws
- (2) Establish an effective regulatory environment
- (3) Facilitate access to the information investors need to make informed investment decisions
- (4) Enhance the Commission's performance through effective alignment and management of human, information and financial capital

Through various program initiatives, the SEC strives to achieve its mission by meeting performance targets. Throughout the year, the performance results are analyzed to determine the success of program activities.

Organized by planned outcomes within each strategic goal, this section discusses FY 2011 program achievements and progress toward achieving planned performance levels. Additionally, for each strategic goal, this section includes a brief narrative on the public benefit produced by the agency's programs and highlights major performance achievements for FY 2011. For each performance measure, this section presents the planned performance target, the actual performance level achieved, analysis of the performance results, the source of the performance data, and, when applicable, plans for improving performance.

Actual performance levels achieved for the prior four fiscal years also are presented. Not applicable (N/A) in the performance measures table indicates that performance data is not available. Performance indicators that do not include targets also are included in this section, providing useful information for understanding the SEC's activities. A discussion of program assessments and evaluations conducted in FY 2011 is provided at the end of this section.

The following outlines a brief description of each of the major components of the performance section:

**FY 2011 Performance Summary by Strategic Goal:** A brief summary of this year's performance achievements including cost data and an overall discussion of performance.

**Strategic Goal Summary:** Each strategic goal section opens by reviewing the purpose of the goal, followed by information identifying the resources allocated to achieving the goal.

**Public Benefit:** This narrative explains the value of the work done toward achieving the strategic goal, from gains within the agency to benefits to the public.

**Spotlight on Performance Achievements:** This narrative highlights major performance achievements for FY 2011.

**Strategic Outcome:** This section provides a description of the SEC's strategic outcome that gauges the agency's performance within each strategic goal.

**Performance Measures and Indicators:** Each strategic goal chapter includes a presentation of performance measures and performance indicators by outcome, comparing planned and actual performance levels for FY 2011. Four years of historical data is provided for performance measures and performance indicators where available. A plan for improving program performance is included for measures where non-achievement was significant.

## Verification and Validation of Performance Data

---

The SEC ensures that the performance data presented in the report is complete, reliable and accurate based upon the following assessment steps:

- (1) The agency develops performance measures through the agency's strategic planning process
- (2) The SEC's divisions and offices perform the following steps to ensure that data used in the calculation of performance measures is accurate and reliable:
  - i. Adequately documenting and explaining the sources of the underlying data elements, and the procedures used to gather the data
  - ii. Adequately documenting and explaining the procedures used to obtain assurance as to the accuracy and reliability of the data
  - iii. Adequately documenting the data definitions for reference
  - iv. Adequately documenting and explaining the measure calculations
- (3) The divisions and offices calculate and report the performance measures to the Office of Financial Management (OFM), and the measures are approved by division directors and office heads

## FY 2011 Performance Summary by Strategic Goal

---

In FY 2011, the SEC dedicated more than \$1,148 million to achieve its goals. Overall, the agency exceeded or met approximately 49 percent of its planned performance targets. See the Performance Highlights in the Management's Discussion & Analysis for more information.

In FY 2011, the SEC performed several activities in order to foster and enforce compliance with the Federal securities laws. Staff collaborated across organizational lines to provide information and resources to investment advisory and broker-dealer firms through events that the majority of industry participants found useful. As a result of increased training for examination staff and improved communication and planning of examinations, staff increased the percentage of non-sweep and non-cause examinations completed within targeted timeframes.

When violations of the Federal securities laws do occur, the SEC investigates and brings enforcement actions against regulated entities or persons, as well as other market participants. The SEC is committed to the timely collection of funds from securities laws violators to the victims of their wrongdoing, and is pleased to report that in FY 2011, the agency obtained payment or initiated collection activities within six months of the due date of a debt for over 90 percent of debts.

The agency devotes a large portion of its resources responding to no-action letters and interpretive and other requests from regulated entities, public companies, and other outside parties. By responding to these requests in a timely manner, the SEC enables market participants to understand clearly their obligations under the Federal securities laws, and in FY 2011, the SEC continued to meet or exceed targeted response rates to written requests.

While it is critically important that industry participants understand their obligations to comply with Federal securities laws, an educated investing public ultimately provides the best defense against fraud and costly mistakes. In FY 2011, the agency continued to focus on educating investors by reaching approximately 18 million investors through various communication methods and in-person events.

In order to support the SEC's program offices in carrying out the above initiatives and in fulfilling the agency's mission, SEC management continued to enhance performance by making sound investments in human capital and new technologies, and by employing strong financial management practices.

## Goal 1: Foster and Enforce Compliance with the Federal Securities Laws

The Commission seeks to detect problems in the securities markets, prevent and deter violations of Federal securities laws, and alert investors to possible wrongdoing. When violations occur, the SEC aims to take prompt action to halt the misconduct, sanction wrongdoers effectively, and return funds to harmed investors. In FY 2011, approximately \$622.9 million and 1,834 full-time equivalents (FTEs) were directed at achieving results in Goal 1, with the agency exceeding or meeting 7 of 15 planned performance targets.

CHART 2.1



CHART 2.2



**Public Benefit.** Fostering compliance with Federal securities laws is interwoven through all of the SEC’s programs and is central to fulfilling the critical mission of the agency. These critical investor protection functions contribute to investors’ confidence in our capital markets. Through disclosure reviews and examinations of broker-dealers, investment advisers, self-regulatory organizations (SROs) and other market participants, the SEC seeks both to detect violations of the securities laws and rules and to foster strong compliance and risk management practices within these firms and organizations.

In FY 2011, the SEC instituted extensive reforms of its national Enforcement and Examination programs to foster and enforce compliance with the Federal securities laws. These reforms included vastly expanding the SEC’s training programs, hiring staff with new skill sets, streamlining management, restructuring processes to ensure better sharing of information, leveraging the knowledge of third parties, revamping the way the SEC handles the hundreds of thousands of tips the agency receives annually, and improving risk-assessment techniques. These and several other significant efforts contribute to the agency’s objective of creating an enduring structure for improved protection of investors and markets.

**Spotlight on Performance Achievements.** While investigating and prosecuting violations of Federal securities laws are integral aspects of the Commission’s programs, working to detect and prevent violations of the securities laws are also key to protecting investors and enhancing market integrity. Efforts designed to promote investor awareness are the first line of defense against fraud.

The Chief Compliance Officer Outreach (CCOutreach) program continues to offer information and resources to investment advisory and broker-dealer firms, and the agency is pleased to report that in FY 2011 the vast majority of participants found the program to be useful (Goal 1, Measure 4). SEC staff collaborated across organizational lines as staff in the Office of Compliance Inspections and Examinations (OCIE), Division of Trading and Markets (TM), and Financial Industry Regulatory Authority (FINRA) worked together and utilized feedback from chief compliance officers (CCO), to ensure that outreach events covered topics of interest and relevance. Additionally, informal feedback received from CCOs that participated in online events also were positive, and OCIE plans to place particular emphasis on future online events to ensure that the content and delivery is as effective as possible.

Through examinations of regulated entities and other market participants, the SEC seeks to both detect violations and to foster strong compliance and risk management practices within these firms and organizations. In FY 2011, the agency implemented improved processes identified during a top-to-bottom review of the examination process. The review resulted in enhancements in training, examination planning, identification of and follow up regarding red flags, complaint evaluation, and third party verification procedures, and helped to mitigate structural issues that in the past impaired communication both among examination staff and across other SEC divisions. Furthermore in FY 2011, the SEC focused on enhancing the expertise of staff through targeted training in critical areas, and enabling staff to obtain certifications as Certified Fraud Examiners and Chartered Financial Analysts.

As a result of these and other targeted efforts, examination program staff completed more than 50 percent of non-sweep and non-cause examinations within 120 days (Goal 1, Measure 8). The program placed an increased emphasis in FY 2011 on completing examination reports and communicating findings in the most efficient and effective manner possible. Revised procedures relating to the monitoring and review of open examinations helped to ensure that the program was allocating resources to those examinations most in need. Furthermore, additional program improvements implemented during the year, such as those aimed at streamlining the documentation of exam findings, helped the program to achieve a high level of performance. Going forward, the staff will strive to complete all examinations within the 180 day timeframe outlined in the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd Frank Act).

Under the Sarbanes-Oxley Act of 2002, the SEC can use Fair Funds to redirect penalties collected from securities law violators to the victims of their wrongdoing. The SEC is committed to the timely collection and distribution of penalties and disgorgement funds and has developed a variety of measures for monitoring progress in this area. In FY 2011, debts were paid or collection activity was initiated within six months for over 90 percent of debts. Disgorgement and penalties processes are currently being streamlined and documented to ensure transparency, efficiency, and more extensive data management and reporting capabilities.

**OUTCOME 1.1: The SEC Fosters Compliance with the Federal Securities Laws.**

In FY 2011, the SEC dedicated approximately \$191.9 million to achieve this outcome.

**GOAL 1 MEASURE 1: Number of new investor education materials designed specifically to help investors protect themselves from fraud**

**DESCRIPTION:** Through its Office of Investor Education and Advocacy (OIEA), and often in conjunction with other organizations, the agency issues Investor Alerts and other forms of educational material that inform investors about new or emerging types of fraud.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013	
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target	
Number of education materials	Prior-year data not available				16	24	24	24	26

**Target:** Met – This measure was developed in FY 2010 during the strategic planning process and prior-year data is not available.

**Analysis:** During FY 2011, the SEC reached its goal of issuing 24 new investor education materials by identifying topics from enforcement actions, rulemaking initiatives, areas of investor interest, and emerging products. By alerting investors to possible areas of concern, these investor education materials help equip investors with the information they need to protect themselves from investment fraud.

**Responsible Division/Office:** Office of Investor Education and Advocacy

**Data Source:** [www.sec.gov](http://www.sec.gov) and [www.investor.gov](http://www.investor.gov)

**GOAL 1 MEASURE 2: Number of industry outreach and education programs targeted to areas identified as raising particular compliance risks**

**DESCRIPTION:** Targeted communication with industry participants on topics shaping the examination program is intended to enhance compliance practices and prevent violations before they occur. This measure identifies the number of major outreach efforts conducted, including the agency’s national and regional CCO outreach events, published Compliance Alerts, and other educational initiatives.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013	
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target	
Number of major outreach efforts	Prior-year data not available				6	10	5	12	12

**Target:** Not Met – This measure was developed in FY 2010 during the strategic planning process and prior-year data is not available.

**Analysis:** The SEC seeks to encourage a strong culture of compliance within organizations that fosters ethical behavior and decision-making. As part of its efforts to promote compliance within the industry, OCIE conducted two CCO outreach events, published one National Risk Alert and also published two public reports during FY 2011. In addition to these efforts, staff from throughout the program participated in a number of additional outreach efforts, including speaking at numerous industry conferences and related engagements, which are not reflected in the above numbers. The program will continue to expand and improve on these efforts during FY 2012 as these are critical elements in fostering and promoting compliance with Federal securities laws. The performance target was set at an approximate level, and the examinations program conducted these initiatives and events to the extent permissible within existing resources.

**Plan for Improving Program Performance:** The program will continue to expand and improve on these efforts during FY 2012 as these are critical elements in fostering and promoting compliance with Federal securities laws. Particular emphasis will be placed on publishing timely and relevant risk alerts and reports describing key observations of the exam program. Through these communications, we will seek to encourage and strengthen the effectiveness of registrants’ risk management and compliance programs by recognizing and appropriately addressing key risks.

**Responsible Division/Office:** Office of Compliance Inspections and Examinations

**Data Source:** Internal tracking, although the events noted above are referenced in the SEC’s website.

### GOAL 1 MEASURE 3: Percentage of firms receiving deficiency letters that take corrective action in response to all exam findings

**DESCRIPTION:** At the conclusion of examinations, the staff communicates identified deficiencies to registrants in the form of a deficiency letter. Registrants are then given a chance to respond to staff findings and often take action to remedy any problems and potential risks. Most often, registrants respond that they have corrected the deficiencies and implemented measures to prevent recurrence.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
Percentage	94%	93%	94%	90%	90%	93%	91%	92%

**Target:** Exceeded

**Analysis:** OCIE works to enforce and foster compliance with Federal securities laws through its examination program. During examinations in FY 2011, the staff identified a number of areas where firms appeared not to be in compliance with Federal securities laws. In response to deficiency letters that were sent to firms by the staff, the vast majority of registrants confirmed they are taking corrective action in response to the staff's findings. In order to achieve this level of high performance, the staff made concerted efforts during the year to improve dialogue and communication with firms, including at the most senior levels. These efforts have helped to ensure that there is a clear understanding of issues and concerns between the SEC and registrants. Overall, this measure continues to show that registrants are using examination results to improve operations and compliance with Federal securities laws.

**Responsible Division/Office:** Office of Compliance Inspections and Examinations

**Data Source:** Super Tracking and Reporting System (STARS)

### GOAL 1 MEASURE 4: Percentage of attendees at CCO Outreach that rated the program as "Useful" or "Extremely Useful" in their compliance efforts

**DESCRIPTION:** The CCO Outreach program is designed to educate, inform, and alert CCOs of pertinent information, including about effective compliance controls, that may assist them in administering compliance programs within registered firms. Improving compliance programs will reduce violative activity, resulting in increased protection for investors. At the conclusion of all CCO Outreach events, CCOs are given the opportunity to rate the usefulness of the information provided in assisting them in their compliance efforts.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
Percentage	97%	92%	84%	77%	80%	86%	80%	82%

**Target:** Exceeded

**Analysis:** During FY 2011, the staff devoted a considerable amount of time to the CCO Outreach program in order to make it as relevant and beneficial as possible for registered entities. The level represented above is reflective of the feedback received during our National Seminar focusing on broker-dealers. Staff from OCIE, the Division of Trading and Markets, and FINRA worked together, and utilized feedback from CCOs, to ensure that this event covered topics of interest and relevance to CCOs. It is important to note that feedback received from an on-line event was not included in the above results. The informal feedback from this event was positive and also noted a number of areas of improvement. While the SEC is pleased that the majority of attendees continue to find these sessions to be useful, the SEC will focus on the feedback provided by attendees and will strive to improve the program so that CCOs continue to learn about common deficiencies and areas of regulatory interest. Particular emphasis will be placed on any future on-line events to ensure that the content and delivery is as effective as possible.

**Responsible Division/Office:** Office of Compliance Inspections and Examinations

**Data Source:** Internal tracking

**GOAL 1 INDICATOR 1: Percentage of actions identified as “high impact” which have resulted in significant corrective industry reaction**

**DESCRIPTION:** The SEC discontinued this performance indicator in FY 2011. The indicator will be replaced with other metrics that will measure enforcement actions on both a qualitative and quantitative basis.

**GOAL 1 INDICATOR 2: Annual increases or decreases in the number of CCOs attending CCO outreach programs**

**DESCRIPTION:** While the raw number of CCOs in the industry may vary depending on factors outside of the SEC’s control, the Commission seeks to provide educational programs that are highly valued by attendees and their employers. Analyzing changes in participation levels will foster continued improvement in both program content and outreach efforts.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011
	Actual	Actual	Actual	Actual	Actual
Number of CCOs	Prior-year data not available			N/A	N/A
<b>Analysis:</b> This measure was developed in FY 2010 during the strategic planning process, and it is currently under review as part of the SEC’s Strategic Plan Addendum process (see MD&A page 6).					
<b>Responsible Division/Office:</b> Office of Compliance Inspections and Examinations					
<b>Data Source:</b> N/A					

**OUTCOME 1.2: The SEC promptly detects violations of the Federal securities laws.**

In FY 2011, the SEC dedicated approximately \$122.7 million to achieve this outcome.

**GOAL 1 MEASURE 5: Percentage of cause and special exams (sweeps) conducted as a result of risk assessment process that includes multi-divisional input**

**DESCRIPTION:** As SEC staff expands its use of risk-based methods and has more data available for risk analysis, staff anticipates that the percentage volume of exams driven by a more robust risk assessment process will increase.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
Percentage	Prior-year data not available				N/A	N/A	TBD	TBD
<b>Target:</b> N/A - This measure was developed in FY 2010 during the strategic planning process, and it is currently under review as part of the SEC’s Strategic Plan Addendum process (see MD&A page 6).								
<b>Analysis:</b> Overall, the SEC focuses its resources on those firms and activities presenting the most risk to investors. Firms with higher risk characteristics or profiles may be identified based on any number of factors, including input from other divisions and offices within the Commission. OCIE will utilize all input, from inside and outside the agency, to most appropriately allocate its resources. Examinations of high risk firms may be for cause, as part of a risk targeted examination sweep, or simply due to the presence of certain higher risk characteristics.								
<b>Responsible Division/Office:</b> Office of Compliance Inspections and Examinations								
<b>Data Source:</b> N/A								

**GOAL 1 MEASURE 6: Percentage of advisers deemed “high risk” examined during the year**

**DESCRIPTION:** To conduct oversight of investment advisers, the staff conducts a risk-based program of examinations. Certain advisers are identified as high risk at the beginning of every fiscal year, and then inspections are planned on a cyclical basis. The staff’s goal is to inspect high-risk advisers at least once every three years. Meeting this target will depend upon the SEC having sufficient resources to keep pace with growth in the industry and the need for examiners to check compliance with evolving regulatory requirements.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
Percentage	33%	33%	22%	N/A	N/A	N/A	TBD	TBD

**Target:** N/A - This measure was developed in FY 2010 during the strategic planning process, and it is currently under review as part of the SEC’s Strategic Plan Addendum process (see MD&A page 6).

**Analysis:** The SEC focuses its resources on those firms and activities presenting the most risk to investors. Firms with higher risk characteristics or profiles may be identified based on any number of factors and will be examined as quickly as possible.

**Responsible Division/Office:** Office of Compliance Inspections and Examinations

**Data Source:** N/A

**GOAL 1 MEASURE 7: Percentage of investment advisers, investment companies, and broker-dealers examined during the year**

**DESCRIPTION:** This measure indicates the number of registrants examined by the SEC or a SRO as a percentage of the total number of registrants. This measure includes all types of examinations: routine examinations, cause inspections to follow up on tips and complaints, limited-scope special inspections to probe emerging risk areas, and oversight examinations of broker-dealers to test compliance and the quality of examinations by the Financial Industry Regulatory Authority (FINRA).

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
Investment advisers	13%	14%	10%	9%	11%	8%	11%	13%
Investment companies	20%	23%	29%	10%	11%	13%	13%	15%
Broker-dealers (exams by SEC and SROs)	54%	57%	54%	44%	45%	42%	42%	44%

**Target:** Investment advisers – Not Met; Investment companies – Exceeded; Broker-dealers – Not Met

**Analysis:** Coverage of the industry helps the Commission in its efforts to both promptly detect violations of Federal securities laws and to promote compliance with such laws.

The staff spent considerable time and effort during the year on improving its risk assessment and surveillance capabilities to ensure that the program is spending its limited time and resources on those firms presenting the highest risk. Examinations of high risk firms often take significant time to complete and are frequently of large and complex entities. For example, the investment advisers examined in FY 2011 represent more than 30 percent of the overall assets under management of currently registered advisers.

The coverage percentage of investment advisers was approximate to FY 2010 levels, but was considerably lower than anticipated for several reasons. The staff had originally anticipated that the number of advisers registered with the Commission would decrease significantly during FY 2011, thereby increasing the program’s coverage levels. This expected decrease in the number of advisers did not occur during FY 2011. In addition, examination resources were reallocated during the last year to other efforts intended to improve the long-term performance of the program, including industry outreach initiatives and other program improvement efforts that were identified as part of the program’s broad, overarching self-assessment.

**Plan for Improving Program Performance:** During FY 2012, the staff will continue to implement improved processes and procedures that were identified as part of its self-assessment process. Over 30 significant improvement initiatives in the areas of strategy, structure, people, processes, and technology are underway. The agency expects that these improvements, which include further refinements to the exam program’s risk assessment processes, will lead to more effective coverage of registered entities.

**Responsible Division/Office:** Office of Compliance Inspections and Examinations

**Data Source:** Super Tracking and Reporting System (STARS) (IA, IC, and BD SEC data) and FINRA Databases (BD SRO Data)

**GOAL 1 MEASURE 8: Percentage of non-sweep and non-cause exams that are concluded within 120 days**

**DESCRIPTION:** The staff conducts examinations each year of investment advisers, investment company complexes, transfer agents, and broker-dealers. The staff strives to complete its examinations in the most efficient and effective manner. When possible, the staff attempts to conclude its examinations within 120 days of the end of any field work completed. However, some examinations require significantly more time so that potential violations are fully reviewed. To ensure that time pressure does not impair quality, the target for this benchmark should not be set too high.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
Percentage	Prior-year data not available			48%	50%	53%	55%	57%

**Target:** Exceeded – This measure was developed in FY 2010 during the strategic planning process, and prior-year data is not available.

**Analysis:** The staff's goal is to identify and communicate potential issues to firms to ensure that compliance problems and issues are corrected quickly. During FY 2011, the staff completed more than 50 percent of its non-sweep and non-cause examinations within 120 days. The program placed an increased emphasis in FY 2011 on completing examination reports and communicating findings in the most efficient and effective manner. Revised procedures relating to the monitoring and review of open examinations helped to ensure that the program was allocating resources to those examinations most in need. Furthermore, additional program improvements implemented during the year, such as those aimed at streamlining the documentation of exam findings, helped the program to achieve the level of performance reflected above. This is all despite more rigorous examination protocols that have been implemented in recent years. Going forward, the staff will strive to complete all examinations within the 180 day timeframe outlined in the Dodd-Frank Act. This measure will be updated to reflect this goal. Overall, this measure has helped the SEC to ensure that deficiencies are promptly detected and resolved by firms.

**Responsible Division/Office:** Office of Compliance Inspections and Examinations

**Data Source:** Super Tracking and Reporting System (STARS)

**GOAL 1 INDICATOR 3: Percentage of exams that identify deficiencies, and the percentage that result in a "significant finding"**

**DESCRIPTION:** Examiners find a wide range of deficiencies during examinations. Some of the deficiencies are more technical in nature, such as failing to include all information that is required to be in a record. However, other deficiencies may cause harm to customers or clients of a firm, have a high potential to cause harm, or reflect recidivist misconduct. The latter deficiencies are among those categorized as "significant." This measure identifies the percentage of exams by registrant category that identified deficiencies, and that resulted in significant deficiency findings.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011
	Actual	Actual	Actual	Actual	Actual
Percentage that identify deficiencies	Prior-year data not available			72%	82%
Percentage that result in a "significant finding"	Prior-year data not available			42%	42%

**Analysis:** In FY 2011, examiners continued to use risk assessment techniques to focus examinations on those areas most likely to reveal significant issues. Overall, the majority of examinations resulted in the identification of deficiencies, and more than 40 percent revealed significant findings. While it is difficult to predict these numbers in future years, they do reflect an effective risk-focused approach that is identifying issues in order to protect investors, prevent fraud and improve compliance.

**Responsible Division/Office:** Office of Compliance Inspections and Examinations

**Data Source:** Super Tracking and Reporting System (STARS)

**GOAL 1 INDICATOR 4: Number of investigations or cause exams from tips**

**DESCRIPTION:** Analysis of a tip can support the request for a cause exam or an enforcement investigation. This indicator would identify the volume of SEC investigations and cause exams that result from tips collected through outreach efforts.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011
	Actual	Actual	Actual	Actual	Actual
<b>Division of Enforcement</b>					
<b>Number of investigations</b>	Prior-year data not available			303	349
<b>Analysis:</b> Results of this indicator are based on investigations opened during the fiscal year and originating from a tip or complaint.					
<b>Responsible Division/Office:</b> Division of Enforcement					
<b>Data Source:</b> HUB case management and tracking system for the Division of Enforcement					
<b>Office of Compliance Inspections and Examinations</b>					
<b>Number of cause exams</b>	Prior-year data not available			N/A	N/A
<b>Analysis:</b> The data for this metric was not available for FY 2011; however, it will be tracked in future years. More broadly, the staff conducted more than 575 cause examinations of investment advisers, broker-dealers, investment company complexes, and transfer agents during FY 2011. Many of these examinations were conducted due to the receipt of critical tips received by the Commission.					
<b>Responsible Division/Office:</b> Office of Compliance Inspections and Examinations					
<b>Data Source:</b> N/A					

**OUTCOME 1.3: The SEC prosecutes violations of Federal securities laws and holds violators accountable.** In FY 2011, the SEC dedicated approximately \$309.1 million to achieve this outcome.

**GOAL 1 MEASURE 9: Percentage of enforcement actions successfully resolved**

**DESCRIPTION:** An action is considered “successfully resolved” if it results in a favorable outcome for the SEC, including through litigation, a settlement, or the issuance of a default judgment. In general, the SEC strives to successfully resolve as many actions as possible but, at the same time, aims to file large, difficult, or precedent-setting actions when appropriate, even if success is not assured. This measure does not include any actions in which the SEC awaits a final outcome. The measure is calculated on a per-defendant basis. Large actions may involve several defendants.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
<b>Percentage</b>	92%	92%	92%	92%	92%	93%	92%	92%
<b>Target:</b> Exceeded								
<b>Analysis:</b> The Division of Enforcement has implemented controls and strategies to resolve actions on a favorable basis. Additionally, the Division will not be reluctant to file precedent setting or complex matters that are programmatically important, even if success is not assured.								
<b>Responsible Division/Office:</b> Division of Enforcement								
<b>Data Source:</b> HUB case management and tracking system for the Division of Enforcement Database								

**GOAL 1 MEASURE 10: Percentage of first enforcement actions filed within two years**

**DESCRIPTION:** This measure identifies the percentage of first enforcement actions filed within two years of opening of a MUI (matter under inquiry). In conducting investigations, the enforcement program continually strives to balance the need for complete, effective, and fair investigations with the need to file enforcement actions in as timely a manner as possible.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
Percentage	54%	62%	70%	67%	70%	61%	65%	65%

**Target:** Not Met

**Analysis:** Filing enforcement actions in a timely manner is an important measure of the Division of Enforcement's effectiveness. Timely actions have an increased deterrent impact; conversely, unnecessarily delayed periods between conduct and sanctions can weaken deterrent effect and undermine the public's faith in the effectiveness of law enforcement. Timeliness of actions will be negatively impacted by cases that are complex and large, which can take extended time to develop successfully. In the last two years, the division has focused its efforts on pursuing such cases. For example, the Division has prioritized investigating and holding accountable firms and individuals who committed securities law violations linked to the financial crisis. Many of these cases involved complex financial products, market transactions and conduct that can be difficult to detect and take longer to investigate. In addition, the Division is focusing on emerging threats involving new trading technologies such as high-frequency and algorithmic trading, large volume trading, as well as systemic insider trading and manipulation schemes.

**Plan for Improving Program Performance:** Recognizing the challenges of bringing complex cases in a timely manner, the Division has streamlined its processes to enable the staff to bring cases more quickly. In addition, the Division has developed and implemented metrics designed to capture the nature and level of investigative activity, the number and timeliness of enforcement actions, as well as overall efficiency and performance. The Division will utilize these and other tools in evaluating and improving its efficiency and timeliness.

**Responsible Division/Office:** Division of Enforcement

**Data Source:** HUB case management and tracking system for the Division of Enforcement Database

**GOAL 1 MEASURE 11: Percentage of debts where either a payment has been made or a collection activity has been initiated within six months of the due date of the debt**

**DESCRIPTION:** The SEC can seek a wide range of remedies for failure to comply with the securities laws. These remedies include civil monetary penalties and disgorgement. When the remedies are imposed by the Commission or the Federal district court, payments must be made by a certain date. This measure identifies the percentage of debts where debtors have made payments or the SEC has initiated a collection activity within 180 days of the due date. Such collection activities include, among other things, demand letters, negotiation of payment plans, enforcing the payment of the debt through the courts, or other judicial remedies.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
Percentage	N/A	88%	90%	86%	90%	91%	92%	92%

**Target:** Exceeded

**Analysis:** During FY 2010, the agency's effort to collect and distribute disgorgement and penalties were studied for efficiency and effectiveness. Based on the findings of this study, a business process re-engineering effort was launched. The organizations supporting these functions have been reorganized into the Office of Collections and the Office of Distributions within the Division of Enforcement, and the Enforcement Audit and Data Integrity Branch within the Office of Financial Management. Disgorgement and penalties processes are currently being streamlined and documented to ensure transparency, efficiency, and more extensive data management and reporting capabilities. Requirements gathering is underway for system upgrades that will enhance accurate reporting on collections-related measures. The requisite data elements for reporting on performance measures are slated for development and inclusion in the existing case tracking system during FY 2012.

**Responsible Division/Office:** Division of Enforcement

**Data Source:** Case Activity Tracking System, Phoenix, relevant case files

**GOAL 1 MEASURE 12: Percentage of Fair Fund and disgorgement fund plans that distributed the final tranche of funds to injured investors within 24 months of the order appointing the fund administrator**

**DESCRIPTION:** In addition to other types of relief, the Commission may seek orders requiring parties to disgorge any money obtained through wrongdoing. The Commission also is empowered to seek civil penalties for violations of the securities laws. Where appropriate, the Commission has sought to return disgorged funds to harmed investors and, as a result of the Fair Funds provision of the Sarbanes-Oxley Act, to combine amounts paid as penalties with disgorged funds, or to create a Fair Fund from penalties only, to reduce losses to injured parties. After sufficient disgorgement and/or penalties have been collected to form a distribution fund, the Commission appoints, or, in civil actions, seeks the appointment of, a fund administrator to develop and subsequently implement an approved plan to distribute funds to injured investors. Using the claims-made process, the fund administrator identifies injured investors and determines amounts to be disbursed to eligible claimants. The distribution of funds to eligible claimants may be made in several tranches to return funds to investors more quickly, while efforts continue to locate any remaining investors through the claims-made process. This measure identifies the percentage of “claims-made” distribution plans that distributed the final tranche during the fiscal year and within 24 months of the order appointing the fund administrator. This reflects Commission-wide efforts to develop, approve, and implement plans to return funds to investors quickly, regardless of the monetary amount in the fund. Any funds not returned to investors are sent to the U.S. Treasury or to the SEC’s Investor Protection Fund.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
Percentage	Prior-year data not available				N/A	N/A	TBD	TBD

**Target:** N/A - This measure was developed in FY 2010 during the strategic planning process, and it is currently under review as part of the SEC’s Strategic Plan Addendum process (see MD&A page 6).

**Analysis:** During FY 2010, the agency’s efforts to collect and distribute disgorgement and penalties were studied for efficiency and effectiveness. Based on the findings of this study, a business process re-engineering effort was launched. The organizations supporting these functions have been reorganized into the Office of Collections and the Office of Distributions within the Division of Enforcement, and the Enforcement Audit and Data Integrity Branch within the Office of Financial Management. Disgorgement and penalties processes are currently being streamlined and documented to ensure transparency, efficiency, and more extensive data management and reporting capabilities. The Division of Enforcement is currently assessing options for reporting. Considerable work has been done toward system upgrades that will enable accurate reporting on distributions-related measures. The requisite data elements for reporting on performance measures are slated for development and inclusion in the existing case tracking system during FY 2012.

**Responsible Division/Office:** Division of Enforcement

**Data Source:** N/A

**GOAL 1 MEASURE 13: Percentage of Fair Fund and disgorgement fund plans approved by final order within the prior fiscal year which had a first tranche of funds distributed under those plans within 12 months of such approval date**

**DESCRIPTION:** In its enforcement actions, the Commission may seek to return funds to harmed investors through disgorgement of ill-gotten gains or through the Fair Funds provision of the Sarbanes-Oxley Act, as amended. This provision permits the Commission to combine amounts paid as penalties with disgorged funds, or to create a Fair Fund from penalties only, to reduce losses to injured parties. This measure identifies the percentage of distribution plans for which a first tranche was distributed to injured investors within 12 months of the plans' approval date. This reflects the Commission's efforts to return funds to investors quickly, regardless of the monetary amount in the fund. Any funds not returned to investors are sent to the U.S. Treasury or to the SEC's Investor Protection Fund.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
Percentage	Prior-year data not available				N/A	N/A	TBD	TBD

**Target:** N/A - This measure was developed in FY 2010 during the strategic planning process and it is currently under review as part of the SEC's Strategic Plan Addendum process (see MD&A page 6).

**Analysis:** During FY 2010, the agency's efforts to collect and distribute disgorgement and penalties were studied for efficiency and effectiveness. Based on the findings of this study, a business process re-engineering effort was launched. The organizations supporting these functions have been reorganized into the Office of Collections and the Office of Distributions within the Division of Enforcement, and the Enforcement Audit and Data Integrity Branch within the Office of Financial Management. Disgorgement and penalties processes are currently being streamlined and documented to ensure transparency, efficiency, and more extensive data management and reporting capabilities. The Division is currently assessing options for reporting. Considerable work has been done toward system upgrades that will enable accurate reporting on distributions-related measures. The requisite data elements for reporting on performance measures are slated for development and inclusion in the existing case tracking system during FY 2012.

**Responsible Division/Office:** Division of Enforcement

**Data Source:** N/A

**GOAL 1 INDICATOR 5: SEC investigations referred to SROs or other state, Federal, and foreign authorities for enforcement**

**DESCRIPTION:** The SEC works closely with other regulators and authorities so that violators of Federal securities laws are held accountable. In certain circumstances, a matter may be more appropriately handled by another entity or in another venue, and the agency will refer the investigation for further action. This measure identifies the number of investigations that are referred to others for action. This number includes investigations that SEC continues to pursue, as well as referrals more appropriately handled by other regulators or authorities.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011
	Actual	Actual	Actual	Actual	Actual
Number of investigations	Prior-year data not available			492	586

**Analysis:** In circumstances where an authority may have an interest in information obtained by the SEC, the SEC may grant the authority access to that information, pursuant to Section 24(c) of the Securities Exchange Act of 1934 and Rule 24c-1 thereunder. Results of this indicator are based on investigations in which requests for access to information were granted to authorities during the fiscal year.

**Responsible Division/Office:** Division of Enforcement

**Data Source:** HUB case management and tracking system for the Division of Enforcement Database

**GOAL 1 INDICATOR 6: Percent of all enforcement investigations deemed “high impact”**

**DESCRIPTION:** High impact or national priority investigations include those investigations which are significant for one or more of the following reasons: (1) The matter presents an opportunity to send a particularly strong and effective message of deterrence, including with respect to markets, products and transactions that are newly developing, or that are long established but by their nature present limited opportunities to detect wrongdoing and thus to deter misconduct. (2) The matter involves particularly egregious or extensive misconduct. (3) The matter involves potentially widespread and extensive harm to investors. (4) The matter involves misconduct by persons occupying positions of substantial authority or responsibility, or who owe fiduciary or other enhanced duties and obligations to a broad group of investors or others. (5) The matter involves potential wrongdoing as prohibited under newly-enacted legislation or regulatory rules. (6) The potential misconduct occurred in connection with products, markets, transactions or practices that pose particularly significant risks for investors or a systemically important sector of the market. (7) The matter involves a substantial number of potential victims and/or particularly vulnerable victims. (8) The matter involves products, markets, transactions or practices that the Enforcement Division has identified as priority areas (*i.e.*, conduct relating to the financial crisis; fraud in connection with mortgage-related securities; financial fraud involving public companies whose stock is widely held; misconduct by investment advisers; and matters involving priorities established by particular regional offices or the specialized units). (9) The matter provides an opportunity to pursue priority interests shared by other law enforcement agencies on a coordinated basis.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011
	Actual	Actual	Actual	Actual	Actual
Percentage	Prior-year data not available			3.26%	5.11%

**Analysis:** The Division of Enforcement conducts many enforcement actions each year that can be characterized as high impact. A matter can be deemed high impact for a variety of reasons, as outlined above. The best proxy for the most significant cases with the “highest” impact is the Division’s list of national priority investigations. In FY 2011, national priority investigations constituted 5.11 percent of the Commission’s active investigations. This figure was calculated by dividing the number of investigations designated as national priority at the end of FY 2011 by the total number of active, ongoing investigations. Active investigations generally include only investigations that are being actively pursued, and generally exclude matters in collections or distributions, matters that are solely in litigation or matters that are in the case closing process.

**Responsible Division/Office:** Division of Enforcement

**Data Source:** HUB case management and tracking system for the Division of Enforcement

**GOAL 1 INDICATOR 7: Percent of investigations that come from internally-generated referrals or prospects**

**DESCRIPTION:** Through enhanced risk assessment practices, the agency aims to improve its ability to identify internally-generated tips or prospects for investigations. Internal prospects could include issues identified during the course of SEC examinations, analysis of data, disclosure reviews, or other activities.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011
	Actual	Actual	Actual	Actual	Actual
Percentage	Prior-year data not available			21.9%	18.50%

**Analysis:** The results of this indicator are based on investigations opened during the fiscal year and originating from referrals within the SEC or other internal analysis.

**Responsible Division/Office:** Division of Enforcement

**Data Source:** HUB case management and tracking system for the Division of Enforcement Database

**GOAL 1 INDICATOR 8: Criminal investigations relating to SEC investigations**

**DESCRIPTION:** In some instances, investigations may reveal that both civil and criminal violations have occurred, and the agency will refer matters to criminal authorities so that those authorities may determine whether to conduct a criminal investigation.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011
	Actual	Actual	Actual	Actual	Actual
Number of criminal investigations	Prior-year data not available			139	134

**Analysis:** This indicator identifies the number of SEC investigations in which one or more related criminal actions was filed in the fiscal year.  
**Responsible Division/Office:** Division of Enforcement  
**Data Source:** HUB case management and tracking system for the Division of Enforcement Database

**GOAL 1 INDICATOR 9: Disgorgement and penalties ordered and the amounts collected by the SEC**

**DESCRIPTION:** In addition to other types of relief, the SEC may seek orders requiring parties to disgorge any money obtained through wrongdoing. The SEC is also empowered to seek civil penalties for violations of the securities laws. Where appropriate, the SEC has sought to return disgorged funds to harmed investors. Funds not returned to investors are sent to the Treasury. This indicator lists disgorgement and penalties ordered as a result of SEC cases and the amounts collected by the SEC. This indicator could increase or decrease based on various factors.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011
	Actual	Actual	Actual	Actual	Actual
Ordered amounts (in millions)	\$1,601	\$1,030	\$2,442	\$2,846	\$2,806
Collected amounts (in millions)	\$979	\$521	\$1,694	\$1,775	\$1,281

**Analysis:** Totals reported include amounts collected to date against the fiscal year ordered amounts. The indicator does not reflect amounts collected during the current fiscal year for prior fiscal year debts. Collected amounts also do not reflect payments received by the SEC against debts payable to courts, receivers, or others.  
**Responsible Division/Office:** Division of Enforcement and Office of Financial Management  
**Data Source:** Phoenix Report - "Total Amounts of Disgorgement, ITSA, Remedies Act Penalties and Undertakings Ordered and Paid".

**GOAL 1 INDICATOR 10: Requests from foreign authorities for SEC assistance and SEC requests for assistance from foreign authorities**

**DESCRIPTION:** Each year, the SEC makes hundreds of requests for enforcement assistance to foreign regulators, while responding to hundreds of such requests from other nations. To facilitate this type of assistance, and encourage other countries to enact laws necessary to allow regulators to cooperate with their foreign counterparts, the SEC has entered into the Multilateral Memorandum of Understanding, an information-sharing arrangement negotiated through the International Organization of Securities Commissions (IOSCO).

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011
	Actual	Actual	Actual	Actual	Actual
Number of requests from foreign authorities	454	414	408	457	492
Number of SEC requests	556	594	774	605	772

**Analysis:** In FY 2011, the SEC experienced growth in the number of requests to foreign authorities by 28 percent over FY 2010 levels, due to the Division of Enforcements' burgeoning need to obtain overseas documents and testimony for investigations and litigated matters. Requests from foreign authorities in FY 2011 increased 8 percent over FY 2010 levels because foreign authorities had an increased need to obtain evidence located in the United States for their investigations.  
**Responsible Division/Office:** Office of International Affairs  
**Data Source:** International Program Oversight Database and Business Object reports

## Goal 2: Establish an Effective Regulatory Environment

During FY 2011, the SEC pursued a vigorous investor-focused rulemaking agenda that will help protect investors and ensure that markets operate fairly. Under the recently enacted Dodd-Frank Act the agency began implementing a more effective regulatory structure focused on greater market transparency and accountability. In FY 2011, the agency dedicated approximately \$126.4 million and 494 FTEs toward achieving results in Goal 2, exceeding or meeting 10 of 16 planned performance targets.

CHART 2.3

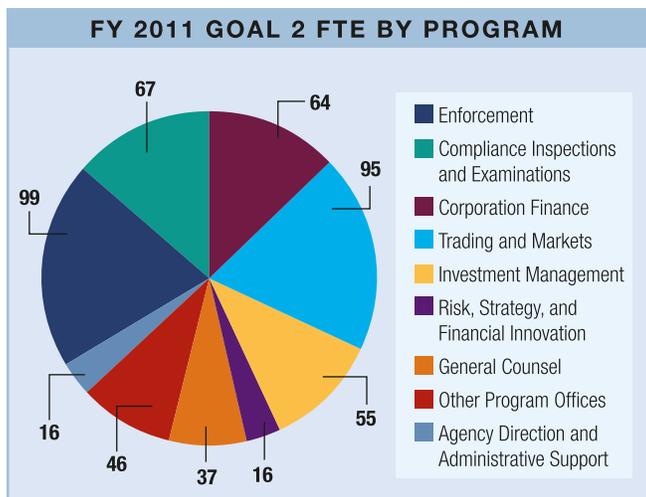
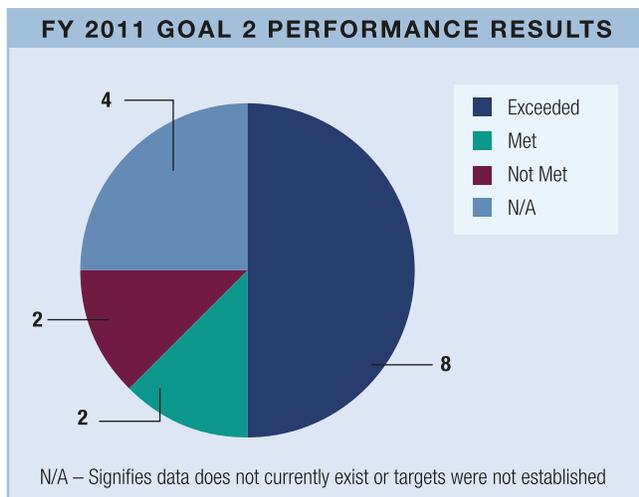


CHART 2.4



**Public Benefit.** The Commission’s responsibility is to put the Federal securities laws into action by establishing a regulatory environment that fulfills and sustains the agency’s mission. Most securities law and regulation flow from two central principles. First, all investors should have equal access to accurate, complete and timely information about the investments they buy, sell and hold. Second, investors should be able to rely upon market participants to conduct investors’ securities transactions efficiently and in the investors’ best interests.

The Commission has broad authority to shape the regulatory framework for the securities industry. In general, rulemaking and policies are designed to improve disclosure, facilitate the flow of important information to investors and the public, improve governance, promote high-quality accounting standards, enhance the accountability of financial intermediaries and other market participants, and strengthen the structure of the trading markets, among other goals. When properly crafted, these rules serve to further the agency’s mission and allow for accurate and reliable information to be made available to investors.

In addition to promulgating its rules and regulations, the SEC provides guidance on rules, responds to inquiries from individuals and companies about whether an activity undertaken in a specified manner would violate the securities laws, and issues individual orders granting relief from provisions of the securities laws when the specific facts indicate that doing so is consistent with the protection of investors. These orders can serve as a testing ground for useful innovation and may pave the way for rulemaking.

The Commission believes that its rules and regulations should be drafted to enable market participants to understand clearly their obligations under the Federal securities laws and to conduct their activities in compliance with law. Just as the securities laws require that disclosures be clear and precise, the Commission aims to promulgate rules that are clearly written, easily understood, and tailored toward specific ends. In addition, the agency recognizes that regular reviews of Commission regulations and its rulemaking processes are necessary to confirm that intended results are being achieved.

**Spotlight on Performance Achievements.** Rulemaking is one of the SEC’s primary functions and involves staff in virtually every program. In FY 2011, the Commission embarked on an aggressive rulemaking agenda intended to address problems exposed by the financial crisis while strengthening investor protection, market transparency, and accountability.

The SEC devotes a large share of resources responding to no-action letters, and interpretive and other requests from regulated entities, public companies, and other outside parties. The agency is committed to speeding the response to such requests where appropriate. In FY 2011, the Divisions of Trading and Markets (TM), Corporation Finance (CF), and Investment Management (IM) met or exceeded their response rate targets (Goal 2, Measure 7). In particular, TM achieved the Division’s highest rate of response since FY 2007, IM processed 100 percent of initial comments on no-action letters, interpretive requests and exemptive applications within set timeframes, and CF continued to surpass its targets to complete initial comments on no-action letters, interpretive requests and shareholder proposals.

The performance data for written inquiries reflects the agency’s dedication in achieving *Strategic Goal 2: Establish an Effective Regulatory Environment*. By responding to written inquiries in a timely manner, the divisions provide confirmation to outside parties that their activities comply with the Federal securities laws. Furthermore, responses to these inquiries generally promote an effective regulatory environment by clarifying the proper application of Federal securities laws.

The SEC also monitors the industry’s efforts to provide stable trading platforms, directly supporting Strategic Outcome 2.2: *The U.S. capital markets operate in a fair, efficient, transparent, and competitive manner, fostering capital formation and useful innovation*. The agency continued to assess the resiliency of market systems in FY 2011, reporting that 99 percent of transaction dollars were settled on time, continuing a trend of timely settlement (Goal 2, Measure 4). In order to maintain these performance levels, TM staff maintained regular supervisory contacts with personnel at relevant clearing agencies to ensure that operational and other issues that arose were promptly identified and addressed. Additionally, the Division expanded resources devoted to clearance and settlement matters over the past year to prepare for the increased focus outlined in the Dodd-Frank Act.

**OUTCOME 2.1: The SEC establishes and maintains a regulatory environment that promotes high-quality disclosure, financial reporting, and governance, and that prevents abusive practices by registrants, financial intermediaries, and other market participants.** In FY 2011, the SEC dedicated approximately \$52.3 million to achieve this outcome.

**GOAL 2 MEASURE 1: Survey on quality of disclosure**

**DESCRIPTION:** Under this metric, the SEC plans to conduct surveys of individual investors to elicit feedback on the quality of disclosures and the Commission’s disclosure requirements. The SEC would track whether the percentage of respondents answering positively improves over time.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
Percentage of positive response	Prior-year data not available				N/A	N/A	TBD	TBD
<p><b>Target:</b> N/A - This measure was developed in FY 2010 during the strategic planning process, and it is currently under review as part of the SEC’s Strategic Plan Addendum process (see MD&amp;A page 6).</p> <p><b>Analysis:</b> This performance measure identifies the usability of specific disclosure documents for the individual investor. Reportable results are not currently available, and OIEA is exploring options for providing data for this metric.</p> <p><b>Responsible Division/Office:</b> Office of Investor Education and Advocacy</p> <p><b>Data Source:</b> N/A</p>								

### GOAL 2 MEASURE 2: Number of consultations; joint events, reports, or initiatives; and joint examinations and other mutual supervisory efforts with SROs and other Federal, state, and non-U.S. regulators

**DESCRIPTION:** This metric gauges how much the SEC is coordinating with other financial regulatory agencies within a given fiscal year. Also, as securities markets around the world become increasingly integrated and globalized, it is essential that the SEC work frequently and effectively with its partner regulators both in the U.S. and abroad.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
Number	Prior-year data not available				N/A	N/A	TBD	TBD

**Target:** N/A - This measure was developed in FY 2010 during the strategic planning process, and it is currently under review as part of the SEC's Strategic Plan Addendum process (see MD&A page 6).

**Analysis:** The SEC will continue to coordinate efforts and consult with other financial regulatory agencies in future years when possible. The staff will leverage existing relationships and look to build additional alliances in order to ensure that regulation for registered entities is as effective as possible.

**Responsible Division/Office:** Several SEC offices

**Data Source:** N/A

### GOAL 2 MEASURE 3: Number of non-U.S. regulators trained

**DESCRIPTION:** This metric shows the reach of the SEC's technical assistance programs for regulators around the world. The SEC conducts these training sessions to assist countries in developing and maintaining robust protections for investors and promote cross-border enforcement and supervisory assistance.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
Number of non-U.S. regulators	Prior-year data not available			1,997	2,020	1,765	1,783	1,800

**Target:** Not Met – This measure was developed in FY 2010 during the strategic planning process and prior-year data is not available.

**Analysis:** The number of foreign regulators trained may vary from year to year and is impacted by the realignment of priorities due to resource limitations. Additionally, in FY 2011 foreign counterparts experienced limitations on their ability to host or attend training sessions.

**Plan for Improving Program Performance:** OIA will consider other methods of providing training that are less resource intensive and are focused on the most strategic deployment of SEC training expertise.

**Responsible Division/Office:** Office of International Affairs

**Data Source:** International Program Oversight Database and Business Object reports

### GOAL 2 INDICATOR 1: Average cost of capital in U.S. relative to the rest of the world

**DESCRIPTION:** Countries' cost of capital can vary according to their protections for investors, the strength of their disclosure regimes, and the presence of fair, orderly, and efficient markets, among other factors. Therefore, although this metric is affected by other economic factors, it can provide some indication of the quality of securities regulation in a given country.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011
	Actual	Actual	Actual	Actual	Actual
Average cost of capital	Prior-year data not available			10.99%	10.67%

**Analysis:** The United States ranks number seven out of 44 countries in terms of the cost of capital as estimated by the World Capital Asset Pricing Model. The lowest cost of capital is in Pakistan at 7.7 percent and the highest is Hungary at 18.35 percent. Ahead of the United States in descending order are Pakistan (7.7 percent), Jordan (8.16 percent), Chile (9.48 percent), Japan (9.63 percent), Malaysia (10.03 percent), and Switzerland (10.45 percent).

**Responsible Division/Office:** Division of Risk, Strategy, and Financial Innovation

**Data Source:** Morningstar International Cost of Capital Report (Annual)

**OUTCOME 2.2: The U.S. capital markets operate in a fair, efficient, transparent, and competitive manner, fostering capital formation and useful innovation.** In FY 2011, the SEC dedicated approximately \$48.0 million to achieve this outcome.

**GOAL 2 MEASURE 4: Percentage of transaction dollars settled on time each year**

**DESCRIPTION:** This metric measures the efficiency of the U.S. clearance and settlement system for equity securities.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
Percentage	N/A	99%	99%	99%	99%	99%	99%	99%

**Target:** Met

**Analysis:** The U.S. clearance and settlement system for equity securities continues to perform at a high rate of timely settlement. Staff from the Division of Trading and Markets maintains regular supervisory contacts with personnel at relevant clearing agencies to ensure operational and other issues that may arise are promptly identified and addressed. The Division expanded its resources devoted to clearance and settlement matters over the past year to prepare for the increased focus on the area contemplated by the Dodd-Frank Act.

**Responsible Division/Office:** Division of Trading and Markets

**Data Source:** National Securities Clearing Corporation

**GOAL 2 MEASURE 5: Average institutional transaction costs for exchange listed stocks on a monthly basis**

**DESCRIPTION:** This performance metric captures the actual cost of trading in large (institutional size) transactions.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
Average transaction costs	Prior-year data not available				N/A	N/A	TBD	TBD

**Target:** N/A - This measure was developed in FY 2010 during the strategic planning process, and it is currently under review as part of the SEC's Strategic Plan Addendum process (see MD&A page 6).

**Analysis:** This metric is subjective to a multitude of assumptions that are intrinsic to each institutional firm and as such, institutional transaction costs vary from firm to firm and trade by trade.

**Responsible Division/Office:** Division of Risk, Strategy, and Financial Innovation

**Data Source:** N/A

### GOAL 2 MEASURE 6: Percentage of market outages at SROs and electronic communications networks (ECNs) that are corrected within targeted timeframes

**DESCRIPTION:** Market outages reflect problems in the systems underlying the securities markets that could have an adverse affect on the markets' ability to function as required. The SEC assesses the reliability and resiliency of these systems to minimize the number and duration of outages. This metric gauges how quickly outages are resolved, so that market activity can resume.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
Within 2 hours	81%	84%	87%	74%	60%	88%	60%	60%
Within 4 hours	91%	96%	98%	85%	75%	94%	75%	75%
Within 24 hours	100%	100%	98%	100%	96%	100%	96%	96%

**Target:** Within 2 hours – Exceeded; Within 4 hours – Exceeded; Within 24 hours – Exceeded

**Analysis:** The SROs exceeded the planned performance targets because of enhancements to the SRO's systems incident handling procedures, and greater emphasis on 100 percent uptime during the trading day hours of operation.

The agency has continued to work with critical SROs on improving their continuity of operations, availability of critical production systems, and recovery time objectives. SROs have shown greater system availability and the ability to open even during disaster events, such as hurricanes, earthquakes and power outages.

**Responsible Division/Office:** Division of Trading and Markets

**Data Source:** ECN outage data is derived from SROs.

### GOAL 2 INDICATOR 2: Average quoted spread for exchange listed stocks on a monthly basis

**DESCRIPTION:** This indicator gauges the hypothetical cost of trading in small amounts at the quoted markets, based solely on published quotations.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011
	Actual	Actual	Actual	Actual	Actual
Average quoted spread	Prior-year data not available		1.70 cents	2.52 cents	1.76 cents

**Analysis:** The average quoted spread for FY 2011 is 1.76 cents indicating that the market is exhibiting normal conditions and suffered no large abnormal quoted spreads.

**Responsible Division/Office:** Division of Risk, Strategy, and Financial Innovation

**Data Source:** Thompson Transaction Analytics

### GOAL 2 INDICATOR 3: Average effective spread for exchange listed stocks on a monthly basis

**DESCRIPTION:** This indicator captures the cost of trading in small amounts based on actual trade prices and the quotes at the times of those trades.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011
	Actual	Actual	Actual	Actual	Actual
Average effective spread	Prior-year data not available		2.19 cents	2.65 cents	1.72 cents

**Analysis:** The average effective spread for FY 2011 is 1.72 cents, which is considerably lower than that seen in the previous two years. This is indicative of market and marketable limit orders receiving price improvement.

**Responsible Division/Office:** Division of Risk, Strategy, and Financial Innovation

**Data Source:** Thompson Transaction Analytics

**GOAL 2 INDICATOR 4: Speed of Execution**

**DESCRIPTION:** This indicator gauges how quickly transactions are executed in the U.S. securities markets.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011
	Actual	Actual	Actual	Actual	Actual
Speed of execution	Prior-year data not available		1.59 seconds	1.77 seconds	1.02 seconds

**Analysis:** The speed of execution for FY 2011 is 1.02 seconds, continuing a trend of faster execution speeds on retail orders. The speed of execution for FY 2010 was 1.77 seconds; however, there was a very large (abnormal) speed of execution in May 2010 of 10.1 seconds due to the flash crash.

**Responsible Division/Office:** Division of Risk, Strategy, and Financial Innovation

**Data Source:** Thompson Transaction Analytics

**GOAL 2 INDICATOR 5: Average quoted size of exchange listed stocks on a monthly basis**

**DESCRIPTION:** This indicator measures the amount of liquidity visible to the market at the displayed quotes.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011
	Actual	Actual	Actual	Actual	Actual
Average quoted size	Prior-year data not available		606 shares	687 shares	606 shares

**Analysis:** Average quoted size of exchange listed stocks on a monthly basis has decreased in 2011 commensurate with a decrease in the average quoted spread for exchange listed stocks compared to the prior year.

**Responsible Division/Office:** Division of Risk, Strategy, and Financial Innovation

**Data Source:** Thompson Transaction Analytics

**GOAL 2 INDICATOR 6: Average daily volatility of exchange listed stocks on a monthly basis**

**DESCRIPTION:** This statistic gauges short term price changes, which are an indicator of the risk of holding stock.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011
	Actual	Actual	Actual	Actual	Actual
Average daily volatility in the S&P 500	Prior-year data not available	1.60%	2.69%	1.18%	1.26%

**Analysis:** The average daily volatility for exchange listed stocks was 1.26 percent for FY 2011, which equates to an annualized volatility equal to 20.05 percent. Market volatility is impacted by a myriad of factors so it is difficult to ascertain with certainty why changes (particularly small changes) in volatility occur.

**Responsible Division/Office:** Division of Risk, Strategy, and Financial Innovation

**Data Source:** Bloomberg

**OUTCOME 2.3: The SEC adopts and administers rules and regulations that enable market participants to understand clearly their obligations under the securities laws.** In FY 2011, the SEC dedicated approximately \$26.1 million to achieve this outcome.

**GOAL 2 MEASURE 7: Length of time to respond to written requests for no-action letters (NAL), exemptive applications, and written interpretive requests**

**DESCRIPTION:** The SEC staff responds to requests for guidance from individuals and companies about specific provisions of the Federal securities laws. These queries can ask for proper interpretations of the securities laws or regulations, or for assurances that no enforcement action will be taken in certain circumstances. The staff also reviews applications for exemptions from the securities laws. Written responses to such requests for guidance, when provided, generally are publicly available, as are applications and related notices and orders, when issued. This measure gauges whether the Divisions of Trading and Markets, Investment Management, and Corporation Finance are issuing initial comments on these requests on a timely basis.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
<b>Trading and Markets: No-action letters, exemptive applications, and written interpretive requests (combined figure)</b>								
Percentage	91%	63%	70%	91%	85%	98.5%	85%	85%
<b>Target:</b> Exceeded								
<b>Analysis:</b> For FY 2011, the Division of Trading and Markets exceeded expectations for timely responses to written requests. The Division responded to written inquiries within the required timeframes 98.5 percent of the time. Responses to these inquiries generally promote an effective regulatory environment by clarifying ambiguity, which permit private entities to more efficiently use their compliance resources.								
The Division's Office of Chief Counsel (OCC) maintains an electronic log for tracking all correspondence received, including the actions taken by the staff and the requestor (with a field for a date of the action). This feature of the electronic log, as well as monthly reporting generated from the log, permit OCC to track written inquiries and reply to them in a timely manner.								
<b>Responsible Division/Office:</b> Division of Trading and Markets								
<b>Data Source:</b> TM Office of Chief Counsel Electronic Log								
<b>Investment Management</b>								
No-action letters and interpretive requests	91%	98%	100%	100%	75%	100%	90%	90%
Exemptive applications	N/A	81%	95%	100%	80%	100%	80%	80%
<b>Target:</b> No action letters and interpretive requests – Exceeded; Exemptive applications – Exceeded								
<b>Analysis:</b> For the third year in a row, IM processed 100 percent of initial comments on no-action letters within three weeks, surpassing the agency's target. While the target of 75 percent within three weeks was reasonable and appropriate when first established (given prior data and trends), more recent trends suggest that it can be increased. Given recent trends for FY 2012, the Division is going to change the target to 90 percent within three weeks.								
<b>Responsible Division/Office:</b> Division of Investment Management								
<b>Data Source:</b> OCC Letter Log, OICR and OIP Applications Tracking Systems								
<b>Corporation Finance</b>								
No-action letters and interpretive requests	66%	66%	85%	97%	90%	97%	90%	90%
Shareholder proposals	100%	100%	100%	100%	100%	100%	100%	100%
<b>Target:</b> No action letters and interpretive requests – Exceeded; Shareholder proposals – Met								
<b>Analysis:</b> CF surpassed its FY 2011 target to complete 90 percent of initial comments on no-action letters within 30 days. The completion rate of 97 percent is consistent with the previous year's performance. This improvement can be attributed to two main factors. First, a new system was developed in FY 2010, which focused on improving tracking of no-action letters. Second, the Division implemented a series of new processes focused on resolving aged requests in a timely fashion.								
<b>Responsible Division/Office:</b> Division of Corporation Finance								
<b>Data Source:</b> Division No-Action Letter database and Division Shareholder Proposal database								

**GOAL 2 MEASURE 8: Survey on whether SEC rules and regulations are clearly understandable**

**DESCRIPTION:** The SEC aims to promote a regulatory environment in which market participants clearly understand their obligations. Through this metric, the SEC intends to survey market participants to determine whether they believe the Commission’s regulatory requirements are clear.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
Percentage	Prior-year data not available				N/A	N/A	TBD	TBD

**Target:** N/A - This measure was developed in FY 2010 during the strategic planning process, and it is currently under review as part of the SEC’s Strategic Plan Addendum process (see MD&A page 6).

**Analysis:** There are no methods or procedures in place to capture data for this measure. TM will review the measure and determine a timeframe for establishing a methodology during FY 2012.

**Responsible Division/Office:** Division of Trading and Markets

**Data Source:** N/A

**GOAL 2 MEASURE 9: Time to complete SEC review of SRO rules that are subject to SEC approval**

**DESCRIPTION:** The SEC reviews SRO rule proposals for consistency with the Exchange Act standards of investor protection, fair and orderly operation of the markets and market structure, as well as other statutory requirements. This metric gauges how long it takes the SEC to approve a filing after publication of notice of the proposal for comment.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
Within 35 days	Prior-year data not available			73%	40%	0%	0%	0%
Within 45 days	Prior-year data not available			99%	80%	82%	80%	80%

**Target:** Within 35 days – Not Met; Within 45 days – Exceeded – This measure was developed in FY 2010 during the strategic planning process and prior-year data is not available.

**Analysis:** The SRO rule filing process supports the SEC’s outcome of adopting and administering rules and regulations that enable market participants to understand clearly their obligations under the securities laws. During FY 2011, although the SEC did not meet the 35-day standard on any of the SRO rule filings, it did meet the Dodd-Frank Act’s 45-day standard, exceeding the 80 percent target. The SEC exceeded this target despite a 13 percent increase in rule filings over the previous fiscal years. It is important to note that for the thirty seven (37) filings which exceeded the 45 day standard, all but one filing was approved within an additional longer statutory timeframe within which the SEC may act.

**Plan for Improving Program Performance:** Of the 220 SRO rule filings approved in FY 2011, 10 were covered by the pre-Dodd-Frank standard of 35 days from the date of publication of notice in the Federal Register and final approval. However, none of the 10 rule changes met the 35-day standard. These rule filings were complex and presented novel issues or were contrary to the Commission policy. The SEC expects to be able to meet the post-Dodd-Frank Act standard of reviewing SRO rule filings within 45 days.

**Responsible Division/Office:** Division of Trading and Markets

**Data Source:** SRO Rule Tracking System (SRTS). Information was extracted from the SRTS data tables into an Excel file. The information was then analyzed to determine the applicable population of filings. Simple formulas were used to calculate the time from filing after publication of notice to approval of filing.

**GOAL 2 INDICATOR 7: Percentage of SRO rule filings that are submitted for immediate effectiveness**

**DESCRIPTION:** This metric gauges the proportion of SRO rule proposals that can be submitted for immediate effectiveness, without Commission approval.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011
	Actual	Actual	Actual	Actual	Actual
Percentage	Prior-year data not available			69%	77%

**Analysis:** This indicator gauges the percentage of rule filings submitted by SROs for immediate effectiveness. Rule proposals can be submitted for immediate effectiveness for certain types of filings, including non-controversial changes, rules relating to fee filings, or so called “copy-cat” rule filings related to proposed rule changes other than trading rules. Rule proposals not submitted for immediate effectiveness require Commission review and approval or disapproval.

**Responsible Division/Office:** Division of Trading and Markets

**Data Source:** SRO Rule Tracking System (SRTS).

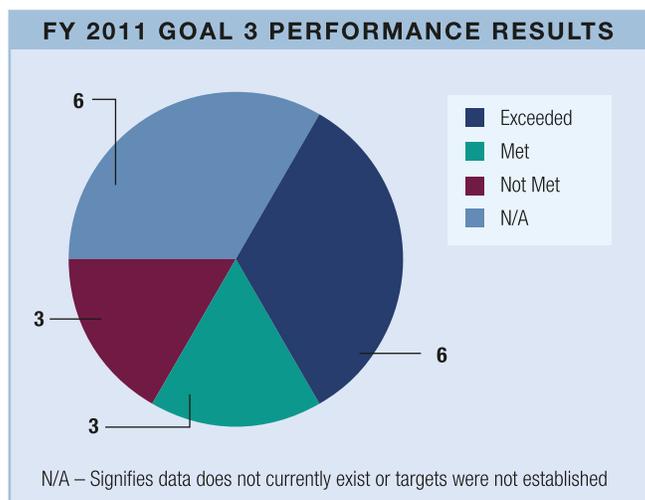
### Goal 3: Facilitate Access to the Information Investors Need to Make Informed Investment Decisions

The SEC promotes informed investment decisions through two main approaches. The first is to require that investors have accurate, adequate, and timely public access to disclosure materials that are easily understood and analyzed. Secondly, the SEC implements a variety of investor education initiatives, aimed at giving investors a better understanding of the operations of the nation’s securities markets. In FY 2011, the agency dedicated approximately \$185.9 million and 640 FTEs toward achieving results in Goal 3, exceeding or meeting 9 of 18 planned performance targets.

CHART 2.5



CHART 2.6



**Public Benefit.** The Federal securities laws require that corporations, investment companies, and other entities provide investors with timely and meaningful information about, among other things, their operations and finances. Because an educated and informed investor ultimately provides the best defense against fraud and costly mistakes, these laws place great emphasis on providing the investing public with meaningful information.

As part of its disclosure program, the SEC requires entities to disclose financial and non-financial information to the public, providing a common pool of knowledge for all investors to use to judge for themselves if a security is a good investment. Similarly, SEC rules require that investors have access to certain information about the financial intermediaries that they rely upon for investment advice and other services. SEC staff review the filings that corporations, investment companies, and other entities submit to assess whether the disclosures appear adequate and accurate.

In FY 2011, the SEC’s investor education program worked on its own and collaboratively with other regulators and educational organizations to provide investors with information they need to evaluate current and potential investments, while also providing agency staff with critical insight about emerging trends and factors that shaped investor decision making. Staff collected investor-focused data from a variety of sources and used it to track trends in the securities industry and to identify, among other things, problematic brokers, firms, and sales practices. This information helped to shape the agency’s overall approach to risk assessment, focused internal resources, and shaped initiatives of other SEC divisions and offices.

**Spotlight on Performance Achievements.** In FY 2011, as part of their disclosure programs, CF and IM continued to meet the requirements of the Sarbanes-Oxley Act (Goal 3, Measure 1). This volume of disclosure review helped deter fraud and assured that investors had access to relevant information about emerging issues. In addition, the agency continued to focus on educating investors about products commonly marketed to them and provided educational programs and materials to help investors detect and avoid potential scams. The Office of Investor Education and Advocacy (OIEA) reached close to 18 million investors through various communication methods, and reached more investors and participated in more in-person events in FY 2011 than in prior years (Goal 3, Measure 8).

**OUTCOME 3.1: Investors have access to high-quality disclosure materials that are useful to investment decision making.** In FY 2011, the agency dedicated approximately \$142.6 million to achieving this outcome.

**GOAL 3 MEASURE 1: Percentage of public companies and investment companies with disclosures reviewed each year**

**DESCRIPTION:** The Sarbanes-Oxley Act requires that the SEC review the disclosures of all companies and investment company portfolios reporting under the Exchange Act at least once every three years. These reviews help improve the information available to investors and may uncover possible violations of the securities laws.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
<b>Division of Corporation Finance</b>								
Corporations	36%	39%	40%	44%	33%	48%	33%	33%
<b>Target:</b> Exceeded								
<b>Analysis:</b> The SEC exceeded its planned level of review of corporations in FY 2011. This review level is expected to deter fraud in public securities transactions and should help investors receive accurate material information about the companies they invest in.								
<b>Responsible Division/Office:</b> Division of Corporation Finance								
<b>Data Source:</b> Electronic, Data Gathering, Analysis, and Retrieval (EDGAR)/Filing Activity Tracking System								
<b>Division of Investment Management</b>								
Investment company portfolios	38%	36%	35%	35%	33%	33%	33%	33%
<b>Target:</b> Met								
<b>Analysis:</b> IM met its planned review level for FY 2011. Each year, the staff sets a target number for the requirement, under Section 408 of the Sarbanes-Oxley Act of 2002, that the Commission review disclosures made by certain public issuers, including issuers' financial statements, no less frequently than once every three years. The targeted number of reviews is dictated by the number of investment companies that were not reviewed in the prior two fiscal years.								
<b>Responsible Division/Office:</b> Division of Investment Management								
<b>Data Source:</b> Microsoft Office Suite Tools								

**GOAL 3 MEASURE 2: Time to issue initial comments on Securities Act filings**

**DESCRIPTION:** The target of 30 days or less has become a *de facto* industry standard for the maximum time to receive initial comments.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
Days	25.5 days	25.2 days	25.3 days	24.1 days	<30 days	24.4 days	<30 days	<30 days

**Target:** Met

**Analysis:** During FY 2011, the SEC issued initial comments on Securities Act filings within an average of 24.4 days of filing. The Division of Corporation Finance's timely review allows companies seeking to raise capital and allows them to build offering schedules around the *de facto* standard.

**Responsible Division/Office:** Division of Corporation Finance

**Data Source:** Electronic, Data Gathering, Analysis, and Retrieval (EDGAR)

**GOAL 3 MEASURE 3: Percentage of investment company disclosure reviews for which initial comments are completed within timeliness goals**

**DESCRIPTION:** For initial registration statements, the SEC's goal is to comment within 30 days after they are filed (60 days for registration statements of insurance product separate accounts). The SEC also aims to comment on post-effective amendments within 45 days and preliminary proxy statements within 10 days after they are filed.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
Initial registration statements	87%	95%	95%	93%	85%	92%	85%	85%
Post-effective amendments	95%	97%	97%	94%	90%	94%	90%	90%
Preliminary proxy statements	99%	99%	99%	99%	99%	98%	99%	99%

**Target:** Initial registration statements – Exceeded; Post-effective amendments – Exceeded; Preliminary proxy statements – Not Met

**Analysis:** The staff strives to review all significant disclosures by registrants, including initial registration statements and post-effective amendments with material changes, including changes due to new disclosure requirements. The staff may limit the scope of a review, through selective review procedures, to a review of only the disclosure in a filing that has not been previously reviewed. The staff generally does not set a target for the number of filings that are reviewed in a fiscal year because the staff does not dictate the number of filings that registrants make. Instead, other factors, such as registrant business decisions or the implementation of new disclosure requirements, typically drive whether investment companies make filings and the type of filings that they make. During periods of increased reviewable filings, the staff is able to handle the increased workload largely through the use of selective review procedures. The staff sets targets for the timeliness of reviews.

**Plan for Improving Program Performance:** For FY 2011, the Division of Investment Management continued its goal of providing comments on proxy statements within 10 days of filing at least 99 percent of the time. The Division missed its 10-day goal for only seven out of 294 filings – due largely to the short period in which to provide comments and the ambitious goal of 99 percent. Also, the responsible office experienced substantial staff changes.

**Responsible Division/Office:** Division of Investment Management

**Data Source:** Electronic, Data Gathering, Analysis, and Retrieval (EDGAR)

**GOAL 3 MEASURE 4: Point of Sale “click-through rate”**

**DESCRIPTION:** The point of sale initiative relies on a layered approach that combines point of sale disclosure and Internet-based disclosure. This measure would determine how often investors click on broker-dealers’ websites to obtain information about broker-dealer compensation and related conflicts of interest.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
“Click-through rate”	Prior-year data not available				N/A	N/A	TBD	TBD

**Target:** N/A - This measure was developed in FY 2010 during the strategic planning process, and it is currently under review as part of the SEC’s Strategic Plan Addendum process (see MD&A page 6).

**Analysis:** Processes and procedures used to collect this information are currently under review, and the agency will work to finalize its methodology during FY 2012.

**Responsible Division/Office:** Division of Trading and Markets

**Data Source:** N/A

**GOAL 3 MEASURE 5: Access to broker-dealer and investment adviser background checks**

**DESCRIPTION:** Greater availability of professional background information of broker-dealers and their employees through the BrokerCheck system will provide investors with the ability to make better-informed decisions. Investors also have the ability to check the backgrounds of investment advisory firms through the SEC’s Investment Adviser Public Disclosure (IAPD) system. This measure would gauge the demand for disclosure information about broker-dealers and their employees through the BrokerCheck website and about investment advisers through the IAPD.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
BrokerCheck System	Prior-year data not available				N/A	N/A	TBD	TBD

**Target:** N/A - This measure was developed in FY 2010 during the strategic planning process, and it is currently under review as part of the SEC’s Strategic Plan Addendum process (see MD&A page 6).

**Analysis:** There are no methods or procedures in place to capture data for this measure. Management will review the measure and determine a timeframe for establishing a methodology during FY 2012.

**Responsible Division/Office:** Division of Trading and Markets

**Data Source:** N/A

IAPD System	Prior-year data not available				N/A	N/A	TBD	TBD
-------------	-------------------------------	--	--	--	-----	-----	-----	-----

**Target:** N/A - This measure was developed in FY 2010 during the strategic planning process, and it is currently under review as part of the SEC’s Strategic Plan Addendum process (see MD&A page 6).

**Analysis:** The agency is currently working with FINRA to enhance the Investment Adviser Public Disclosure System (IAPD) system (through a study conducted under Section 919B of the Dodd-Frank Act) which is expected to change how site usage is monitored. Also, in anticipation of this performance measure being included in future SEC reports, the SEC has asked FINRA to consolidate IAPD’s usage measurements to equate to those that are or in the future will be used by BrokerCheck. In addition, IAPD usage statistics received in the past year have fluctuated some, given other changes to IAPD such as the inclusion of information regarding state registered investment adviser representatives (the site is a shared site between SEC and the states). Therefore, the SEC does not yet have reliable and comparable information that would be useful to the public.

**Responsible Division/Office:** Division of Investment Management

**Data Source:** FINRA

**GOAL 3 MEASURE 6: Investor demand for disclosures on municipal securities**

**DESCRIPTION:** Greater availability of market-sensitive information through the Municipal Securities Rulemaking Board's Electronic Municipal Market Access (EMMA) website will provide investors with the ability to make better-informed investment decisions and assist market participants in fulfilling their disclosure obligations. This measure gauges the demand for disclosure information about municipal securities through the EMMA website.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
Website hits	Prior-year data not available				N/A	N/A	TBD	TBD

**Target:** N/A - This measure was developed in FY 2010 during the strategic planning process, and it is currently under review as part of the SEC's Strategic Plan Addendum process (see MD&A page 6).

**Analysis:** There are no methods or procedures in place to capture data for this measure. Management will review the measure and determine a timeframe for establishing a methodology during FY 2012.

**Responsible Division/Office:** Division of Trading and Markets

**Data Source:** N/A

**GOAL 3 MEASURE 7: Satisfaction index for disclosure process**

**DESCRIPTION:** The agency will conduct survey research or focus groups to identify the level of satisfaction with disclosure requirements.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
Satisfaction index	Prior-year data not available				N/A	N/A	TBD	TBD

**Target:** N/A - This measure was developed in FY 2010 during the strategic planning process, and it is currently under review as part of the SEC's Strategic Plan Addendum process (see MD&A page 6).

**Analysis:** The targets measure the usability of specific disclosure documents for the individual investor. Reportable results are not currently available. OIEA is exploring options for providing data for this metric.

**Responsible Division/Office:** Office of Investor Education and Advocacy

**Data Source:** N/A

**OUTCOME 3.2: Agency rulemaking and investor education programs are informed by an understanding of the wide range of investor needs.** In FY 2011, the agency dedicated approximately \$43.3 million to achieving this outcome.

**GOAL 3 MEASURE 8: Number of investors reached, and number of in-person events with specifically targeted communities and organizations**

**DESCRIPTION:** The agency has developed an extensive collection of free information to help investors understand the basics of investing; the risks and rewards of various products and strategies; the importance of diversification; and ways to find information about brokers, advisers, and companies. Much of this information is posted on the SEC's Investor Information Web page, a key tool for informing and educating the investing public. In addition, the Office of Investor Education and Advocacy publishes hard-copy educational brochures and conducts in-person events. This measure seeks to determine the total number of investors reached by the SEC, and assess the effectiveness of outreach efforts conducted by OIEA and the regional offices targeted to specific investor groups (for example, seniors, military, or other affinity groups). The measure also captures the use of various channels to reach investors, such as the SEC webpage, investor.gov, social networking sites, outreach programs, or public appearances.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
Number of investors reached (in millions)	Prior-year data not available			17.8	16	14.8	15	15
Number of in-person events	Prior-year data not available			42	30	48	35	50

**Target:** Number of Investors Reached (in millions) – Not Met; Number of In-Person Events – Exceeded

**Analysis:** OIEA reached more investors and participated in more in-person events this year than in FY 2010, as outreach gains from more active partnerships exceeded outreach declines related to its direct mail partnership with the IRS. In FY 2012, OIEA will continue to examine new ways to offset the expected continuing decline in its direct mail partnership with the IRS, a result of fewer taxpayers receiving paper refund checks. OIEA uses these measures to ensure that it continues to explore and identify cost-effective outreach initiatives, while maintaining a consistent level of participation at in-person events, which help inform OIEA's investor education program.

**Responsible Division/Office:** Office of Investor Education and Advocacy

**Data Source:** Microsoft Office Suite Tools

**GOAL 3 MEASURE 9: Number of investor educational initiatives organized and produced**

**DESCRIPTION:** In partnership with other organizations, the agency will develop a number of educational campaigns intended to customize content and maximize its reach to various investor communities. Through the use of primary and secondary research including tracking emerging investor concerns and complaints, the agency will continue to assess how to best target its efforts to the investing public. This measure identifies the number of major investor initiatives undertaken.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
<b>Number of initiatives</b>	Prior-year data not available			9	10	11	11	11

**Target:** Exceeded

**Analysis:** OIEA exceeded its target for educational campaigns in FY 2011 by, among other efforts, providing investor education resources to British Petroleum payout recipients and helping Deaf investors avoid affinity fraud. OIEA continues to work on numerous ongoing initiatives and projects that address a variety of objectives, from developing new products for teachers and students to serving the unique needs of seniors and Spanish-speaking investors. This measure helps ensure that OIEA strives to develop new ways to educate investors and continues to help individuals in various target audiences.

**Responsible Division/Office:** Office of Investor Education and Advocacy

**Data Source:** Microsoft Office Suite Tools

**GOAL 3 MEASURE 10: Timeliness of responses to investor contacts**

**DESCRIPTION:** OIEA serves the tens of thousands investors each year who contact the SEC with investment-related complaints and questions. The staff aims to close out as many new investor assistance matters within seven and 30 business days.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
<b>Closed within 7 days</b>								
<b>Total</b>	82%	78%	70%	72%	80%	67%	70%	70%
<b>Closed within 30 days</b>								
<b>Total</b>	94%	88%	90%	93%	90%	92%	90%	90%

**Target:** 7 Days – Not Met; 30 days – Exceeded

**Analysis:** While the complexity of questions and complaints varies, OIEA uses these measures to ensure that individuals contacting OIEA receive high quality responses within a reasonable amount of time.

**Plan for Improving Program Performance:** OIEA did not meet its seven business day target due to reductions in staff as a result of attrition and detail assignments, and a higher percentage of substantive contacts due to adjustments to OIEA's voice response system. OIEA has adjusted its seven business day target for fiscal years 2012 and 2013 to reflect the new work flow demands and higher percentage of substantive contacts. OIEA remains focused on improving its response rates and maintaining the accuracy and clarity of the responses.

**Responsible Division/Office:** Office of Investor Education and Advocacy

**Data Source:** Internal log using IRIS data

**GOAL 3 MEASURE 11: Percentage of rules impacting investors that are presented in alternate user-friendly formats**

**DESCRIPTION:** The agency intends to publish explanations of Commission actions in easily understandable language, to encourage investor participation and comments on issues materially affecting them. The Office of Investor Education and Advocacy also will track emerging concerns and trends and then work with the rulemaking divisions and other offices on possible regulatory responses. The SEC also may use surveys or questionnaires to collect input from investors to assist in assessing their views on Commission actions.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
Percentage	Prior-year data not available			100%	100%	100%	100%	100%

**Target:** Met

**Analysis:** During FY 2011, OIEA provided input to the SEC's Divisions of Investment Management, Trading and Markets, and Corporation Finance on a variety of rulemaking projects, including initiatives required by the Dodd-Frank Act. In addition, OIEA continued to issue investor bulletins that provide concise summaries of Commission rules, including a bulletin on "say on pay" and golden parachute votes. The SEC uses this measure to ensure that the perspectives of individual investors are considered in the Commission's rulemaking efforts.

**Responsible Division/Office:** Office of Investor Education and Advocacy

**Data Source:** Internal Log

**GOAL 3 MEASURE 12: Customer satisfaction with usefulness of investor educational programs and materials**

**DESCRIPTION:** Through the use of focus groups and surveys, the agency will assess the usefulness of educational material provided to investors across a variety of channels based upon ease of use, appropriateness, and other factors.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
Satisfaction index	Prior-year data not available				N/A	N/A	TBD	TBD

**Target:** N/A - This measure was developed in FY 2010 during the strategic planning process, and it is currently under review as part of the SEC's Strategic Plan Addendum process (see MD&A page 6).

**Analysis:** While OIEA receives direct feedback from some investors regarding its investor assistance function through a customer satisfaction survey, inadequate data exists to benchmark performance targets for this measure. Currently, OIEA is exploring other options for establishing a performance target for this measure.

**Responsible Division/Office:** Office of Investor Education and Advocacy

**Data Source:** N/A

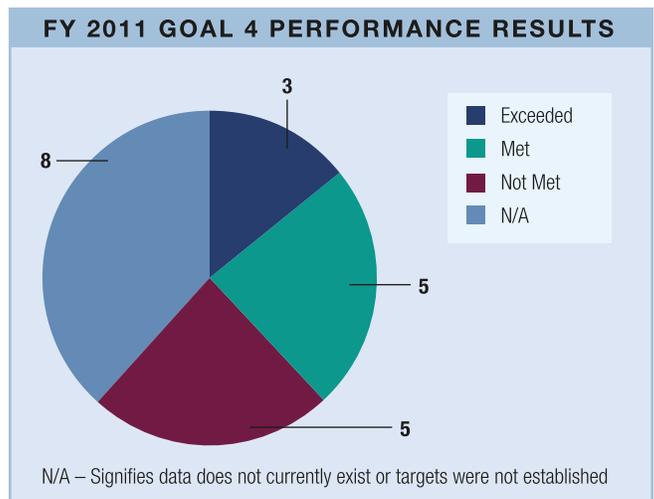
## Goal 4: Enhance the Commission’s Performance Through Effective Alignment and Management of Human, Information, and Financial Capital

The investing public and the securities markets are best served by an efficient, effective, and agile SEC. In FY 2011, the SEC continued to take steps to become a more effective regulator of the U.S. financial markets by making sound investments in human capital and new technologies, and enhancing internal controls. The agency directed approximately \$212.9 million and 848 FTEs toward Goal 4 in FY 2011, exceeding or meeting eight of 21 planned performance targets.

CHART 2.7



CHART 2.8



**Public Benefit.** Given the immense size of the securities markets the SEC regulates, the agency’s success in fulfilling its mission is highly dependent upon its ability to continually direct its resources towards the most productive uses for investors and the public. The SEC also is extremely mindful of its responsibility to maximize the impact of public funds.

In FY 2011, the agency focused on recruiting and retaining high-performing staff, and continually updating the expertise of SEC employees so they are abreast of the latest developments in the industry. Additionally, the SEC created organizational structures and work processes that were aimed at increasing organizational efficiency and effectiveness. The agency’s information technology environment was enhanced to provide employees better tools to view, analyze, and act upon the enormous volume of financial data and other information relevant to oversight of the securities markets. Furthermore, the SEC continued to further strengthen internal controls.

**Spotlight on Performance Achievements.** The SEC’s employees are its most vital strategic resource. The agency is committed to being an employer of choice by consistently attracting, hiring, developing, and retaining a high-quality, diverse, and results-oriented workforce. In FY 2011, the SEC tracked the performance of new measures to gauge the agency’s progress in recruiting and retaining staff, and increasing staff training and development so that each employee achieved and maintained the highest level of performance.

Compared with FY 2010, the SEC in FY 2011 developed five times more diversity-related partnerships or alliances with professional associations and educational organizations, aimed towards providing opportunities to educate students about the agency’s work and recruit career professionals from diverse backgrounds (Goal 4, Measure 6). The Office of Equal Employment Opportunity was responsible for this achievement. Beginning in FY 2012, the responsibility for the agency’s performance in this area will transfer to the new Office of Minority and Women Inclusion.

Additionally in FY 2011, the Office of Human Resources (OHR) made significant progress in improving the quality of the agency's performance management program, such as conducting a thorough evaluation of the existing system, facilitating mandatory face-to-face training for all SEC managers, providing substantial online training for employees, increasing communication about the program among staff, and implementing a robust calibration process to improve consistency and fairness (Goal 4, Measure 7).

Information technology plays a crucial role in the mission of the SEC as well. The increasing size and complexity of the U.S. securities markets require that the SEC leverage technology to continuously improve its productivity, as well as identify and address the most significant threats to investors. In FY 2011, the SEC continued to focus on developing a robust data integration and management program, aimed at modernizing tools for enforcement case management, examination management, rulemaking, the agency's processes for handling disgorgement and penalties, and management of Commission actions (Goal 4, Measure 12). In FY 2011, six projects were identified to implement workflow and document management across the agency to further enhance current application functionality and increase staff efficiency, and in March 2011, the Tips, Complaints and Referrals (TCR) Intake system was released for use by SEC staff.

Given the SEC's role in overseeing the securities markets, it is important that the agency maintain strong internal controls and sound financial management practices over its own operations. In FY 2011, the agency worked to further strengthen internal controls and improve accounting processes and succeeded in eliminating two material weaknesses in internal controls over financial reporting (Goal 4, Measure 17).

**OUTCOME 4.1: The SEC maintains a work environment that attracts, engages, and retains a technically proficient and diverse workforce that can excel and meet the dynamic challenges of market oversight.**

In FY 2011, the SEC dedicated approximately \$57.2 million to achieve this outcome.

**GOAL 4 MEASURE 1: Survey of employee engagement**

**DESCRIPTION:** The SEC strives to maintain a culture in which employees demonstrate a strong personal, positive connection with the organization and its mission and strategic goals. This connection, which can be called "employee engagement," can result in higher-quality work, willingness to lead or participate in special projects, sharing job knowledge with others, mentoring other staff, or other positive contributions to the agency and its work. This index will be drawn from annual survey results and will track the agency's success in improving employee engagement.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
Annual index score	Prior-year data not available			58%	65%	61%	65%	65%

**Target:** Not Met

**Analysis:** The SEC has made progress toward its goal of increasing employee engagement, as reflected in the results of the 2011 Employee Viewpoint Survey. In FY 2011, management began to execute action plans developed in FY 2010 to address specific areas of improvement to the extent possible given workload and budget constraints.

**Plan for Improving Program Performance:** In FY 2012, OHR will facilitate additional focus groups with divisions and offices to design solutions needed to continue improving employee engagement.

**Responsible Division/Office:** Office of Human Resources

**Data Source:** Internal Survey

**GOAL 4 MEASURE 2: Best Places to Work ranking**

**DESCRIPTION:** This annual ranking of Federal Government agencies will be used to determine the SEC's overall success in improving our organizational climate.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
Ranking number	Ranked #3	Ranked #3	Ranked #11	Ranked #24	Ranked #5	N/A	Ranked #20	Ranked #15

**Target:** N/A

**Analysis:** The employee viewpoint survey results have been released for the FY 2011 period. However, the Partnership for Public Service has not published the Best Places to Work rankings yet.

**Responsible Division/Office:** Office of Human Resources

**Data Source:** Partnership for Public Service "Best Places to Work" Agency Rankings

**GOAL 4 MEASURE 3: Turnover**

**DESCRIPTION:** The SEC strives to maintain an organizational climate in which high-performing employees wish to remain. Although turnover can fluctuate based on a variety of factors, including the health of the economy and the number of outside job opportunities available for SEC staff, the agency aims to keep its turnover rate relatively low, below 8 percent per year.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
Percent turnover	8.8%	6.2%	3.7%	5%	<8%	6.4%	<8%	<8%

**Target:** Met

**Analysis:** The SEC has continued to exceed its target for annual turnover. The increase over FY 2010 turnover was affected by an offering of Voluntary Early Retirement Authority (VERA), which comprised approximately one-third of separations in FY 2011.

**Responsible Division/Office:** Office of Human Resources

**Data Source:** The National Business Center at Department of Interior (DOI)

**GOAL 4 MEASURE 4: Expanding staff expertise**

**DESCRIPTION:** Internal training and hiring programs are designed to help the agency recruit and develop its staff so that key skills, industry knowledge, and expertise are maintained. In particular, there is a need to hire more economists, trading specialists, and other experts with knowledge of the marketplace and both investment and trading practices. Annual agency training goals and hiring practices are focused on ensuring staff have the necessary capabilities to address trends in the industry. This measure tracks whether certain areas requiring significant training are being addressed. For example, the agency will monitor the percentage of staff that has received or maintained significant relevant training in fraud detection as measured by achieving the status of a Certified Fraud Examiner, Chartered Financial Analyst, Series 7, or other relevant industry designations.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
Percent of staff with industry designations	Prior-year data not available			N/A	N/A	9%	15%	20%

**Target:** N/A - This measure was developed in FY 2010 during the strategic planning process; FY 2011 targets were not established.

**Analysis:** The College of Securities and Investor Protection (CSIP), established in FY 2011 within OHR's SEC University, delivered 89 learning events in FY 2011, covering such topics as Forensic Accounting, Detecting Financial Fraud, Clearing and Settlement, Complex Insider Trading Investigations, Financial Modeling, Quantitative High Frequency Trading, and Risk Assessment. Over 6,700 SEC staff members attended the programs, an average of 1.8 programs per SEC employee as some employees attended more than one program. In addition, SEC staff members were able to attend over 4,300 external short programs in securities and regulation (an average of 1.1 programs per SEC employee).

**Responsible Division/Office:** Office of Human Resources

**Data Source:** Association of Certified Fraud Examiners, Chartered Financial Analyst Institute

**GOAL 4 MEASURE 5: Size of competency gaps**

**DESCRIPTION:** Key competencies will be rated as part of the SEC's performance management process. Once the SEC has implemented a technology system to support the performance management program, the agency will assess its baseline competency gaps annually and work to bring them down over time.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
Percentage reduction for the size of competency gaps	Prior-year data not available			N/A	10%	N/A	10%	10%

**Target:** N/A - This measure was developed in FY 2010 during the strategic planning process and is currently under review.

**Analysis:** The SEC plans to implement a Performance Management Information System (PMIS) to automate its performance management process. The methodology for assessing competency gaps will be defined as part of the PMIS when implemented.

**Responsible Division/Office:** Office of Human Resources

**Data Source:** N/A

**GOAL 4 MEASURE 6: Number of diversity-related partnerships/alliances**

**DESCRIPTION:** Increased numbers of diversity-related partnerships or alliances with professional associations and educational organizations provide opportunities to educate students about the SEC’s work and recruit career professionals from all segments of society. The SEC will track the number of partnerships and/or alliances with diverse professional associations and educational organizations.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
Number of part-nerships/alliances	Prior-year data not available			2	5	10	12	15

**Target:** Exceeded

**Analysis:** The number reflected for each fiscal year will be all active partnerships/alliances established in prior years (beginning with FY 2010) plus new partnerships/alliances established during the reporting year. This performance measure will transfer to the new Office of Minority and Women Inclusion (OMWI) effective FY 2012. OMWI provided targets for FY 2012 and FY 2013.

**Responsible Division/Office:** Office of Equal Employment Opportunity

**Data Source:** Office of Equal Employment Opportunity Internal Records

**GOAL 4 MEASURE 7: Survey feedback on the quality of the SEC’s performance management program**

**DESCRIPTION:** The SEC will construct an index from survey results to determine the extent to which managers and other employees find the performance management program valuable, credible, transparent, and fair.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
Percentage of positive survey responses	Prior-year data not available			N/A	65%	53%	65%	65%

**Target:** Not Met

**Analysis:** The SEC implemented a pilot performance management system in the Division of Enforcement and the Office of Compliance Inspections and Examinations in late FY 2010. The results of the survey, therefore, reflect the pilot and the previous system that was in place until early FY 2011. OHR and others conducted several evaluations of the pilot, which led to some key changes, and the new system was implemented Commission-wide on November 1, 2011.

**Plan for Improving Program Performance:** Since the survey was administered to employees, OHR has taken many steps to improve the performance of the system and the perceptions of employees. These steps include:

- 1) A thorough evaluation of the system;
- 2) Mandatory face-to-face training for all managers in the Commission;
- 3) Substantial on-line training for employees;
- 4) Increased communication; and
- 5) A robust calibration process to improve consistency and fairness.

The above listed steps are expected to improve SEC employee perceptions of the system. OHR expects to institute changes to the system based on experience gained from the 2011 effort.

**Responsible Division/Office:** Office of Human Resources

**Data Source:** 2011 Employee Viewpoint Survey results to questions related to Performance Management

**OUTCOME 4.2: The SEC retains a diverse team of world-class leaders who provide motivation and strategic direction to the SEC workforce.** In FY 2011, the agency dedicated approximately \$37.7 million to achieving this outcome.

#### GOAL 4 MEASURE 8: Quality of hire

**DESCRIPTION:** Data related to each new hire will be gathered from either the immediate supervisor or the selecting official, as appropriate. Data will be gathered three months after entry on board. This early assessment will not only inform the agency's selection system, but will provide an opportunity to address quickly any developmental needs or performance issues.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
Percentage of hires rated at least four on a five-point scale	Prior-year data not available			N/A	75%	N/A	TBD	TBD

**Target:** N/A - This measure was developed in FY 2010 during the strategic planning process and is currently under review.

**Analysis:** In FY 2011, the OHR worked with divisions and offices to enhance their selection systems to increase the quality of candidate assessment and selection. OHR plans to implement an SEC-wide on-boarding program, in which managers will be polled to assess the quality of hires to further inform selection systems and needed developmental opportunities.

**Responsible Division/Office:** Office of Human Resources

**Data Source:** N/A

#### GOAL 4 MEASURE 9: Leadership Competency Gaps

**DESCRIPTION:** A 360-degree feedback survey will be conducted across all leadership ranks. This will provide an SEC-wide score on each competency measured in the survey. The gap will be determined by subtracting the obtained scores from expected proficiency levels on key competencies. Progress will be determined by comparing this baseline to scores obtained from subsequent administrations of the survey.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
Average percentage of gaps reduced in each survey	Prior-year data not available			N/A	10%	N/A	TBD	TBD

**Target:** N/A - This measure was developed in FY 2010 during the strategic planning process and is currently under review.

**Analysis:** OHR has continued to implement a 360-degree feedback tool to assist in establishing baseline competency levels based on SEC's leadership competency model. To date, 145 SEC managers have completed 360-degree assessments within the Successful Leaders Program. Plans are in place to launch an agency-wide 360-degree assessment through a staged roll out, in which Senior Officers and SK-17's will participate in Phase I. Once a baseline is established and development opportunities are offered, reassessments will be conducted to measure gap closures.

**Responsible Division/Office:** Office of Human Resources

**Data Source:** N/A

**GOAL 4 MEASURE 10: Satisfaction with Leadership Development Program**

**DESCRIPTION:** After each major developmental event participants will complete a survey of items related to key training outcomes. Responses to these items will be compiled to create a composite score.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
Average score on a five-point scale	Prior-year data not available			4.46	4.5	4.49	4.5	4.5

**Target:** Not Met

**Analysis:** In FY 2011, the SEC University continued implementation of the Successful Leaders Program and established a new framework for a ladder of courses and electives to promote leadership development at all levels of the Commission. In addition to the core Successful Leaders Program modules (Core I, Core II, Crucial Conversations, Coaching Tools and Strategic Leadership), the College of Leadership Development launched electives for non supervisory employees on communication skills, emotional intelligence and team leader skills. An additional elective on coaching tools was provided for management staff. In FY 2011, 538 SEC employees enrolled in leadership programs. Additional output measures were added to the post-event survey to capture “behavior change”, “job impact” along with “value” of the program to participants.

**Plan for Improving Program Performance:** The SEC made progress toward meeting the target of 4.5. The College of Leadership Development will continue to monitor the satisfaction of offerings and make adjustments to its curriculum to meet the needs and expectation of its learners.

**Responsible Division/Office:** Office of Human Resources

**Data Source:** Successful Leaders Program Evaluations

**OUTCOME 4.3: Information within and available to the SEC becomes a Commission wide shared resource, appropriately protected, that enables a collaborative and knowledge-based working environment.** In FY 2011, the agency dedicated approximately \$29.7 million to achieving this outcome.

**GOAL 4 MEASURE 11: Percentage of SEC data sources accessible through a virtual data warehouse, and milestones achieved towards the creation of a robust information management program**

**DESCRIPTION:** The SEC intends to reform its information management processes, so that data can be more easily accessed, shared, and analyzed across the organization. This metric will display the percentage of SEC data sources accessible for search and analysis through a virtual data warehouse. In addition, the SEC will track its success in achieving relevant milestones over the course of this multi-year effort. These milestones include establishing a formal information management program in 2010, completing an information catalog by 2011, providing capabilities to support analysis of information by 2012, and developing a capability that allows integration of business operations data for management, reporting and analysis by 2013.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
Percentage	Prior-year data not available			N/A	N/A	N/A	TBD	TBD

**Target:** N/A - This measure was developed in FY 2010 during the strategic planning process, and it is currently under review as part of the SEC’s Strategic Plan Addendum process (see MD&A page 6).

**Analysis:** The high-level Data Governance Program completed Phase I in April 2011. This phase addressed the collection of metadata and the development of a SharePoint website repository of information (metadata) that will serve as a data catalog, and includes all Data Governance schedules and activities. Site content includes the ‘as-is’ state for OIT; the incorporation of artifacts for business rules; data security; policies, procedures and standards; roles, tools and technologies; data categories; datasets; and reference data. Phase II of the program commenced in May 2011. This phase established a business-level task force and stakeholders and continues the process of metadata collection to capture a picture of the current state for the SEC.

**Responsible Division/Office:** Office of Information Technology

**Data Source:** N/A

**GOAL 4 MEASURE 12: Deployment of document management and workflow tools**

**DESCRIPTION:** This metric will present the SEC's success in applying document management and workflow tools to the Commission's mission critical business functions. Over time, the SEC aims to deploy these tools for enforcement case management, the agency's processes for handling disgorgement and penalties, examination management, management of Commission actions, and rulemaking.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
Business functions served	Prior-year data not available			Enforcement & Examination	Tips, Complaints and Referrals Commission-wide	Tips, Complaints and Referrals Commission-wide	OCIE-National Exam Program	TBD

**Target:** Met

**Analysis:** Efforts are well under way to implement document management and workflow tools within SEC applications. The business areas that will benefit from enhancing document management and workflow are management of tips, complaints and referrals; enforcement case management; disgorgement and penalties management; examination management; management of Commission actions; filing of administrative proceedings; records management; and rulemaking. To date, six projects have been identified to implement workflow and document management in the Commission. Several projects have implemented Phase 1 and are working on deploying Phases 2 and 3 in the upcoming months to include additional SEC offices, further enhance current application functionality, and increase staff efficiency. In March 2011, the Tips, Complaints and Referrals (TCR) Intake system was released to the entire Commission. While plans exist to expand workflow and document management to all the divisions in the Commission in order to extend the range of solutions and to integrate these facilities into most of the management applications, the SEC's budget situation will impact the ability of the Commission to deploy additional workflow and document management capabilities in FY 2012 and FY 2013.

**Responsible Division/Office:** Office of Information Technology

**Data Source:** Data sources will be available in FY 2012

**GOAL 4 MEASURE 13: Time to process evidentiary material for enforcement investigations**

**DESCRIPTION:** The SEC aims to improve its ability to process evidentiary material gathered during the course of its enforcement investigations, and enhance the agency's document storage, organization, and analytical capabilities. This metric will gauge whether these efforts succeed in reducing the time required to process evidentiary material, so it can be analyzed by enforcement staff.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
Number of days	Prior-year data not available			N/A	N/A	N/A	TBD	TBD

**Target:** N/A

**Analysis:** An Electronic Discovery 2.0 software solution was selected and a new contract was awarded. This multi-year project is currently in the initial pilot of the software. The Evidence Tracking System program will be developed in FY 2012 and will support the Electronic Discovery Program's central processing unit. This measure is designed to capture the time to process evidentiary material for enforcement investigations. During the FY 2011 reporting period, the SEC tracked milestones against this measure however the measure will not be considered reportable until data becomes available. Therefore, the measure target is N/A.

**Responsible Division/Office:** Office of Information Technology

**Data Source:** Data sources will be available in FY 2012

**GOAL 4 MEASURE 14: System availability**

**DESCRIPTION:** The SEC aims to enhance its computing infrastructure to eliminate down time if systems at one site fail, among other objectives. This metric will capture the percentage of systems and applications that can fail over within 4 hours. In addition, the SEC will track the percentage of its systems that have been virtualized, further reducing down time and increasing their accessibility from alternative locations.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
Systems availability	Prior-year data not available			99.97%	99.3%	99.94%	99%	99%
Percentage fail over within 4 hours	Prior-year data not available			N/A	100%	0%	100%	100%
Systems virtualized	Prior-year data not available			22%	25%	38%	40%	45%

**Target:** Systems Availability – Exceeded; Percentage Fail Over Within 4 Hours – Not Met, Systems Virtualized – Exceeded

**Analysis:** System Availability is composed and measured by the following criteria: Systems are monitored on a real time basis by the OIT Network Operations Center (NOC) with automated network monitoring tools; the IT Business Continuity Team (ITBC) maintains a list of critical systems and applications that can be failed over to an alternate data center site in the event of a failure at the primary site; and the total percentage of systems virtualized will be measured as new servers are deployed based on current hardware replacement schedules.

**Plan for Improving Program Performance:** OIT did not meet the FY 2011 target to have 100 percent of mission critical applications able to fail over to the alternate site within 4 hours. Currently, OIT can fail over all critical systems to alternate site within 8 hours. OIT is continuing to target reducing the failover time to 4 hours by FY 2014. A new baseline for the fail over of the sub-systems will be established and OIT will improve this metric until it achieves the target of 100 percent by 2014.

**Responsible Division/Office:** Office of Information Technology

**Data Source:** OIT NOC- automated network monitoring tools

**OUTCOME 4.4: Resource decisions and operations reflect sound financial and risk management principles.** In FY 2011, the agency dedicated approximately \$88.3 million to achieving this outcome.

The SEC is placing great emphasis on bolstering its processes and systems in its budgeting, accounting, and internal control functions and continues to focus on delivering complete, concise, and meaningful information on its financial and operating performance.

**GOAL 4 MEASURE 15: Milestones achieved towards establishment of a robust data management program**

**DESCRIPTION:** A business process improvement effort will be initiated to identify enhancements needed to create a robust data management program over the next five years. This metric will gauge the agency's success in establishing an integrated enterprise data management, reporting, and analysis capability for mission and back office data.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
Milestone achieved	Prior-year data not available			N/A	Administrative data and reporting requirements identified	Administrative data and reporting requirements identified	Application Deployment FY 2012 Q2	TBD

**Target:** Met

**Analysis:** The SEC decided in the first quarter of 2011 to migrate the agency's financial system to one of the Federal Shared Service Providers. Milestones are being reevaluated based on the new project's plan.

**Responsible Division/Office:** Office of Information Technology

**Data Source:** Data sources will be available in FY 2012

**GOAL 4 MEASURE 16: Financial systems integration**

**DESCRIPTION:** As part of the SEC's effort to integrate its financial systems, the agency will measure the percentage of secondary systems that are fully interfaced with the core financial system, in compliance with applicable standards.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
Percentage	Prior-year data not available			N/A	17%	N/A	TBD	TBD

**Target:** N/A - This measure was developed in FY 2010 during the strategic planning process and is currently under review as part of the SEC's Strategic Plan Addendum Process (see MD&A page 6)

**Analysis:** The SEC decided in the first quarter of 2011 to migrate the agency's financial system to one of the Federal Shared Service Providers. Figures will not be available for this performance measure until the full scope of the system migration is completed.

**Responsible Division/Office:** Office of Information Technology

**Data Source:** Data sources will be available in FY 2012

**GOAL 4 MEASURE 17: Financial audit results**

**DESCRIPTION:** Under the Accountability of Taxpayer Dollars Act of 2002, the agency is required to meet all proprietary and budgetary accounting guidelines for Federal agencies and to undergo annual audits. The SEC’s audits are conducted by the Government Accountability Office.

Fiscal Year	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011		FY 2012	FY 2013
	Actual	Actual	Actual	Actual	Target	Actual	Target	Target
Unqualified opinion	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Material weaknesses	1	0	1	2	0	0	0	0
Significant deficiency	3	3	6	0	0	4	0	0

**Target:** Unqualified opinion – yes; Material weaknesses – 0; Significant deficiency – 4

**Analysis:** As discussed in this report, for FY 2011, the Government Accountability Office found that the SEC had successfully remediated the two material weaknesses from FY 2010. GAO did find that the SEC has four significant deficiencies remaining: in information security, financial reporting and accounting processes, budgetary resources, and registrant deposits.

**Plan for Improving Program Performance:** In FY 2012, the SEC will work to make its internal controls stronger and more sustainable by shifting to a new financial system offered by a Federal Shared Service Provider. At the same time, the SEC also will work to further strengthen its information security, reduce the backlog of dormant registrant deposit accounts, tighten controls over budgetary resources, and finish implementing controls over spreadsheets and databases used in financial reporting.

**Responsible Division/Office:** Office of Financial Management

**Data Source:** GAO FY 2011 SEC Financial Audit Report

## Program Assessments and Evaluations

Internal and external evaluations play a significant role in monitoring and improving SEC program performance. Through objective measurement and analysis, agency managers determine the extent to which programs are achieving mission objectives and direct SEC resources accordingly.

### Office of Inspector General Audits, Reviews, and Investigative Reports

The Office of the Inspector General (OIG) is an independent office within the SEC that conducts audits of programs and operations of the Commission and investigations into allegations of misconduct by staff or contractors. The mission of the OIG is to detect waste, fraud, and abuse, and to promote integrity, economy, efficiency, and effectiveness in the agency's programs and operations. During FY 2011, the OIG issued 14 audit and evaluation reports, 24 investigative reports and 18 inquiry memorandum reports. The table below shows descriptions of the audit and evaluation reports, as well as descriptions of eight investigative reports that are available on the OIG's website.

**TABLE 2.1**

Office of Audits	
Issued Reports	Examples of Findings
Assessment of the Office of Investor Education and Advocacy's Functions ( <i>Report No. 498</i> )	(1) OIEA's review procedures have lengthened the response time for priority inquiries (2) OIEA staff need additional training opportunities and sufficient time to attend training
Review of Alternative Work Arrangements, Overtime Compensation, and COOP-Related Activities at the SEC ( <i>Report No. 491</i> )	(1) A number of SEC employees are working unauthorized work schedules, and SEC policy on alternative work schedules is poorly documented and communicated (2) The SEC lacks clear guidance on overtime compensation and uncompensated services
Assessment of SEC's Continuous Monitoring Program ( <i>Report No. 497</i> )	(1) OIT is not fully enforcing the requirements of its implementing instruction for user account identification and authentication (2) OIT's helpdesk password and PIN reset verification procedures need improvement
Audit of SEC's Employee Recognition Program and Recruitment, Relocation, and Retention Incentives ( <i>Report No. 492</i> )	(1) OHR did not fully address OPM recommendations pertaining to SEC award practices (2) OHR's policy for its award program is outdated and not readily accessible
Review of SEC Contracts for Inclusion of Language Addressing Privacy Act Requirements ( <i>Report No. 496</i> )	(1) OAS's contracts contain appropriate language addressing Privacy Act Requirements (2) Strengthening the language in SEC contracts pertaining to privacy and information might help ensure vendor compliance with contractual and Privacy Act provisions
Oversight of and Compliance with Conditions and Representations Related to Exemptive Orders and No-Action Letters ( <i>Report No. 482</i> )	(1) The SEC's Divisions that issue Exemptive Orders and No-Action Letters do not have a coordinated process for ensuring adherence to the conditions and representations contained therein (2) Data on compliance with the conditions and representations in Exemptive Orders and No-Action Letters are not effectively captured, tracked, and analyzed
Establishment of the Office of Minority and Women Inclusion	(1) The SEC has not established its Office of Minority and Women Inclusion, as required by section 342(1)(A) of the Dodd-Frank Act, because it had concluded it cannot use appropriated funds for this purpose without first obtaining Congressional approval
Report of Review of Economic Analyses Performed by the Securities and Exchange Commission in Connection with Dodd-Frank Act Rulemakings	(1) The SEC formed teams with sufficient expertise to conduct a comprehensive and thoughtful review of the economic analyses of the six proposed releases examined (2) The OIG identified two areas of potential deficiencies in the SEC's cost benefit analysis for which additional review will be conducted
The SEC's Implementation of and Compliance with Homeland Security Presidential Directive 12 ( <i>Report No. 481</i> )	(1) The SEC has not issued PIV credentials to all employees and contractors and lags behind other federal agencies in implementing HSPD-12 (2) The SEC does not have the authority to determine eligibility of a person for access to classified information
SEC's Oversight of the Securities Investor Protection Corporation's Activities ( <i>Report No. 495</i> )	(1) TM and OGC do not maintain adequate written procedures and policies for oversight of SIPC (2) TM and OCIE do not inspect SIPC's activities in a systematic fashion
OCIE Regional Offices' Referrals to Enforcement ( <i>Report No. 493</i> )	(1) In response to the OIG survey issued to OCIE staff, most examiners expressed satisfaction with action taken by Enforcement (2) Because some examination-related referrals are provided informally, some information may not be captured

(Continued on next page)

**TABLE 2.1** *Continued from previous page*

<b>Office of Audits (continued)</b>	
<b>Issued Reports</b>	<b>Examples of Findings</b>
Audit of the SEC Budget Execution Cycle (Report No. 488)	(1) By alternating between two separate appropriations, the SEC may have violated the Purpose Statute and, as a consequence, the Antideficiency Act (2) The SEC inactivated Momentum budgetary controls to facilitate processing payroll transactions, which could lead to a violation of the Antideficiency Act
2010 Annual FISMA Executive Summary Report (Report No. 489)	(1) Exceptions to federal desktop core configuration deviations are not fully documented (2) Accounts are not properly terminated when users no longer require access
Review of Select Time-and-Materials and Labor-Hour Contracts (Report No. 487)	(1) Documented evidence for the acceptance of deliverables is needed (2) OA did not ensure the assignment of a qualified administrator for the XBRL contract
<b>Office of Investigations</b>	
<b>Investigative Reports</b>	<b>Examples of Findings</b>
Investigation of Conflict of Interest Arising from Former General Counsel's Participation in Madoff-Related Matters (OIG-560)	(1) The OIG found that Becker, along with his two brothers, inherited an interest in a Madoff account owned by his mother's estate after she died in 2004 (2) The OIG investigation found that after Becker rejoined the SEC as General Counsel and Senior Policy Director in February 2009, he participated personally and substantially in matters in which he had a personal financial interest by virtue of his inheritance of the proceeds of his mother's estate's Madoff account, and that the matters on which he advised could have directly impacted his financial position
Excessive Payment of Living Expenses in Contravention of OPM Guidance for a Headquarters Senior Official (OIG-561)	(1) The OIG found that the SEC's arrangement with Hu was contrary to OPM guidance and the SEC practice based on that guidance regarding IPA agreements (2) The SEC's former Executive Director was primarily responsible for the unprecedented offer to pay Hu's living expenses during the term of his IPA agreement with the SEC
Allegations of Enforcement Staff Misconduct in Insider Trading Investigation (OIG-511)	(1) The OIG concluded that there was insufficient evidence to substantiate claims that the SEC enforcement staff engaged in misconduct in conducting their investigation into Mr. Cuban's sale of his mamma.com stock shares (2) The OIG investigation also did not find sufficient evidence to substantiate Mr. Cuban's claim that an earlier enforcement investigation into Mamma.com stock was closed as a <i>quid pro quo</i> for the investigation relating to Mr. Cuban
Improper Actions Relating to the Leasing of Office Space (OIG-553)	(1) The OIG investigation found that based upon estimates of increased funding to meet the requirements of the Dodd-Frank Act, the SEC OAS conducted a deeply flawed and unsound analysis to justify the need for the SEC to lease 900,000 square feet of space at the Constitution Center facility in Washington, D.C. (2) The OIG investigation found that OAS prepared a faulty Justification and Approval to support entering into the Constitution Center lease without competition after the contract to lease the facility had already been signed and then backdated the Justification and Approval
Investigation of Abuse of Compensatory Time for Travel by a Headquarters Manager and Ineffective Supervision by Management (OIG-538)	(1) The OIG found that the HQ Manager overcharged the U.S. Government 63.5 hours of compensatory time for travel during an 18-month period costing taxpayers \$5,274.74 (2) The OIG found that the HQ Manager does not work his regularly scheduled hours, frequently leaving the office 30-50 minutes early without taking leave
Improprieties in the Selection of Information Technology and the Award of a Sole-Source Contract (OIG-523)	(1) The OIG investigation found that the Cloverleaf acquisition violated several provisions of the Competition and Contracting Act (CCA) and the Federal Acquisition Regulation (FAR) (2) The OIG found that the Cloverleaf acquisition was not reviewed and approved as part of a process to promote competition as required by statute, another violation of the CCA and the FAR

### Office of Investigations *(continued)*

Investigation Concerning the Role of Political Appointees in the SEC's Response to Requests Pursuant to the Freedom of Information Act and From Members of Congress ( <i>OIG-543</i> )	<p>(1) The OIG investigation did not find evidence that political appointees at the SEC have played an improper role in the review of or response to FOIA requests for SEC records</p> <p>(2) The OIG investigation found that the SEC's responses to requests by members of Congress for OIG reports are subject to review and approval by the Agency's five Commissioners, who are political appointees, and that, because of the Agency's effort to provide the same response to FOIA requesters as that provided to members of Congress requesting and OIG report, the Commission's review process of requests by members of Congress for OIG reports affects the responses to FOIA requests for these same OIG reports</p>
Investigation of the Failure of the SEC's Los Angeles Regional Office to Uncover Fraud in Westridge Capital Management Notwithstanding Investment Adviser Examination Conducted in 2005 and Inappropriate Conduct on the Part of Senior Los Angeles Official ( <i>OIG-533</i> )	<p>(1) The OIG investigation found that in 2005, the SEC's LARO missed a significant opportunity to uncover a Ponzi scheme and failed to conduct a competent and thorough examination of the investment adviser, Westridge Capital Management, and did not take the necessary steps to ensure that a follow-up examination of the broker-dealer, WG Trading, was conducted</p> <p>(2) The OIG further found that in 2009, when an examination team conducted a joint examination of Westridge and WG Trading, which it acknowledged were both operating in the "exact same fashion" in 2009 as in 2005, and the 2009 examination team followed up on the same "red flags" identified in 2005, the fraud was quickly and easily discovered</p>

## Government Accountability Office

The U.S. Government Accountability Office (GAO) conducts numerous studies or investigations related to the SEC’s programs every year. During FY 2011, GAO issued 10 reports on major rules promulgated by the SEC. In addition to reports on agency rules, GAO also conducted an annual audit of the SEC’s financial statements and internal controls over financial reporting. The table below shows descriptions of these reports as found on GAO’s website.

**TABLE 2.2**

GAO Reports on SEC Major Rules		
Report Title	Significant Findings	Report Number
Reporting of Security-Based Swap Transaction Data	GAO reviewed the Securities and Exchange Commission’s (Commission) new rule on the reporting of security-based swap transaction data. GAO found that (1) the interim final temporary rule requires specified counterparties to pre-enactment security-based swap transactions to report certain information relating to pre-enactment security-based swaps to a registered security-based swap data repository or to the Commission by the compliance date established in the security-based swap reporting rules required under sections 3C(e) and 13A(a) of the Securities Exchange Act of 1934 (“Exchange Act”), or within 60 days after a registered security-based swap data repository commences operations to receive and maintain data concerning such security-based swaps, whichever occurs first and report information relating to pre-enactment security-based swaps to the Commission upon request; and (2) Commission complied with applicable requirements in promulgating the rule.	GAO-11-173R
Risk Management Controls for Brokers or Dealers With Market Access	GAO reviewed the Securities and Exchange Commission’s (Commission) new rule on risk management controls for brokers or dealers with market access. GAO found that (1) the final rule will require brokers or dealers trading securities directly on an exchange or on an alternative trading system (ATS) to establish, document, and maintain a system of risk management controls and supervisory procedures; and (2) the Commission complied with the applicable requirements.	GAO-11-221R
Regulation SHO	GAO reviewed the Securities and Exchange Commission’s (Commission) new rule on the Regulation SHO. GAO found that (1) the final rule extends for a limited period of time the compliance date for the amendments to Rule 201 and Rule 200(g) of Regulation SHO from November 10, 2010, to February 28, 2011; and (2) Commission complied with the applicable requirements in promulgating the rule.	GAO-11-212R
Disclosure for Asset-Backed Securities Required by Section 943 of the Dodd-Frank Wall Street Reform and Consumer Protection Act	GAO reviewed the Securities and Exchange Commission’s (Commission) new rule on disclosure for asset-backed securities required by Section 943 of the Dodd-Frank Wall Street Reform and Consumer Protection Act. GAO found that (1) this final rule requires securitizers of asset-backed securities to disclose fulfilled and unfulfilled repurchase requests; and (2) the Commission complied with the applicable requirements in promulgating the rule.	GAO-11-353R
Issuer Review of Assets in Offerings of Asset-Backed Securities	GAO reviewed the Securities and Exchange Commission’s (SEC) new rule on issuer review of assets in offerings of asset-backed securities. GAO found that (1) the final rule implements section 945 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010. The rule requires any issuer registering the offer and sale of an asset-backed security (ABS) to perform a review of assets underlying the ABS. The rule also requires the issuer of an ABS to disclose the nature of its review and the findings and conclusions of the issuer’s review of the assets; and (2) SEC complied with applicable requirements in promulgating the rule.	GAO-11-341R
Shareholder Approval of Executive Compensation and Golden Parachute Compensation	GAO reviewed the Securities and Exchange Commission’s (Commission) new rule on shareholder approval of executive compensation and golden parachute compensation. GAO found that (1) the final rule implements section 951 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010. Section 951 requires companies to conduct a separate shareholder advisory vote to approve the compensation of executives; and (2) the Commission complied with the applicable requirements in promulgating the rule.	GAO-11-362R

*(Continued on next page)*

TABLE 2.2 *Continued from previous page*

GAO Reports on SEC Major Rules (continued)		
Report Title	Significant Findings	Report Number
Securities Whistleblower Incentives and Protections	GAO reviewed the Securities and Exchange Commission's (Commission) new rule on securities whistleblower incentives and protections. GAO found that (1) the final rule implements section 922 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010. Section 922 directs the Commission to pay awards, subject to certain limitations and conditions, to whistleblowers who voluntarily provide the Commission with original information about a violation of the securities laws that leads to the successful enforcement of an action brought by the Commission that results in monetary sanctions exceeding \$1,000,000; and (2) the Commission complied with the applicable requirements in promulgating the rule.	GAO-11-764R
Rules Implementing Amendments to the Investment Advisers Act of 1940	GAO reviewed the Securities and Exchange Commission's (Commission) new rule implementing the amendments to the Investment Advisers Act of 1940. GAO found that (1) the final rule and rule amendments are adopted under the Investment Advisers Act of 1940 to implement provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act; and (2) the Commission complied with applicable requirements in promulgating the rule.	GAO-11-862R
Family Offices	GAO reviewed the Securities and Exchange Commission's (SEC) new rule on family offices. GAO found that (1) the Investment Advisers Act of 1940 imposes certain registration and other regulatory requirements on investment advisers. The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 excluded family offices from the definition of investment advisers. This final rule defines family offices for the purposes of that exclusion; and (2) SEC complied with applicable requirements in promulgating the rule.	GAO-11-816R
Large Trader Reporting	GAO reviewed the Securities and Exchange Commission's (Commission), new rule on large trader reporting. GAO found that (1) the final rule is meant to both identify and obtain trading information on market participants that conduct a substantial amount of trading activity, as measured by volume or market value, in the U.S. securities markets; and (2) the Commission complied with the applicable requirements in promulgating the rule.	GAO-11-912R

GAO's annual report to Congress on high-risk areas, completed since 1990, serves to bring focus to specific areas needing extra attention. In its 2009 report, GAO identified the need to modernize the outdated U.S. financial regulatory system as a high-risk area. The Financial Regulatory System remained on the GAO high-risk list during FY 2011. The SEC will continue to coordinate with other federal departments and agencies to address this high-risk challenge. Information on the Financial Regulatory System high-risk list challenge, including relevant GAO reports, can be found at: [http://www.gao.gov/highrisk/risks/efficiency-effectiveness/modernizing\\_financial\\_system.php](http://www.gao.gov/highrisk/risks/efficiency-effectiveness/modernizing_financial_system.php). Additional GAO reports and recommendations are available at: <http://www.gao.gov>.

## Internal Performance Measurement Assessments

In FY 2011, the SEC worked to improve processes and internal controls around the collection, reporting, and assessment of performance measurement data. Specifically, the agency implemented additional data validation and verification techniques for all such data.



# FINANCIAL SECTION



**T**his section of the Performance and Accountability Report contains the U.S. Securities and Exchange Commission's (SEC) financial statements, required supplementary information, financial statements for the Investor Protection Fund, and the related Independent Auditor's Report. Information presented here satisfies the financial reporting requirements of the Office of Management and Budget (OMB) Circular A-136, *Financial Reporting Requirements*, Accountability of Tax Dollars Act of 2002, and Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act).

The SEC prepares these statements in conformity with U.S. Generally Accepted Accounting Principles (GAAP) for the Federal Government and OMB Circular A-136, *Financial Reporting Requirements*.

The first portion of this section contains the Government Accountability Office's (GAO) audit opinion, followed by the SEC's response. Then, the section shows the principal financial statements for the SEC as a whole. The statements provide a comparison of Fiscal Year (FY) 2011 and FY 2010 information. The SEC prepares the following required financial statements

- Balance Sheet – presents, as of a specific time, amounts of future economic benefits owned or managed by the reporting entity exclusive of items subject to stewardship reporting (assets), amounts owed by the entity (liabilities), and amounts which comprise the difference (net position).
- Statement of Net Cost – presents the gross cost incurred by the reporting entity less any exchange revenue earned from its activities. The SEC also prepares a Statement of Net Cost by program to provide cost information at the program level.
- Statement of Changes in Net Position – reports the change in net position during the reporting period. Net position is affected by changes to Cumulative Results of Operations.
- Statement of Budgetary Resources – provides information about how budgetary resources were made available as well as their status at the end of the year.
- Statement of Custodial Activity – reports collection of non-exchange revenue for the Treasury General Fund. The SEC, as the collecting entity, does not recognize these collections as revenue. Rather, the agency accounts for sources and disposition of the collections as custodial activities on this statement.

The SEC does not have stewardship over resources or responsibilities for which supplementary stewardship reporting would be required.

Budgetary information aggregated for purposes of the Statement of Budgetary Resources is disaggregated for each of the SEC's major budget accounts and is presented as Required Supplementary Information.

The accompanying *Notes to the Financial Statements* provide a description of significant accounting policies as well as detailed information on select statement lines.

The second portion of this section contains stand alone, comparative financial statements and accompanying notes for the Investor Protection Fund as required by the Dodd-Frank Act. These statements include the Balance Sheet, Statement of Net Cost, Statement of Changes in Net Position, and Statement of Budgetary Resources.

## Message from the Chief Financial Officer



I am delighted to join Chairman Schapiro in presenting the SEC's Performance and Accountability Report (PAR) for fiscal year (FY) 2011. We hope you find the PAR a useful summary of the SEC's use of resources, operating performance, financial stewardship, and internal control.

I am extremely pleased to report that the SEC has successfully remediated the two material weaknesses identified in 2010 related to information systems and financial reporting and accounting processes. This was a top priority of the SEC, and I am gratified that the agency staff's hard work and dedication to building a strong internal control environment have yielded such significant results.

In FY 2011, the SEC significantly enhanced its technology security, thereby reducing the first material weakness in information systems down to a significant deficiency. The agency achieved this important milestone through efforts such as remediating self-identified security deficiencies, updating security patches on SEC systems, and strengthening user access controls. The SEC eliminated the second material weakness by resolving two of the five underlying significant deficiencies, in disgorgements and penalties and in required supplementary information, and making significant progress on the other three areas, related to financial reporting, budgetary

resources, and filing fees. The agency did so through efforts such as:

- Tightening controls over the recording of subsequent orders, post-judgment interest, and deposits in transit related to disgorgements and penalties;
- Eliminating a backlog of offering and verification reviews of fees paid on registrant filings, and significantly reducing the backlog of inactive registrant accounts;
- Redesigning and implementing controls over the spreadsheets and databases used by the agency for material financial reporting-related transactions and key operational management decisions, based on risk;
- Bolstering the processes related to the use of miscellaneous obligating documents; and
- Strengthening our process for de-obligating funds from completed contracts, and ensuring that appropriate accounting adjustments are recognized.

At the same time, the agency has been engaged in a multi-year effort to migrate its core financial system to a Federal Shared Service Provider (FSSP) model, engaging with the Department of Transportation's Enterprise Services Center (ESC). The ESC has successfully served multiple Federal agencies, including various components of the Department of Transportation, the Government Accountability Office, and the Commodity Futures Trading Commission. Through this initiative, the SEC will

realize improvements in system functionality, automate some manual processes, and further enhance financial management and reporting.

In FY 2012, the SEC will continue working to ensure a successful transition to the FSSP, and the agency is on track to cut over to the new system and associated new processes in that year. In addition, the SEC plans further progress on tightening information security, resolving the backlog of inactive registrant deposit accounts, bolstering the processes related to deobligations of previously executed contracts, and implementing controls over spreadsheets and databases related to financial reporting.

I am proud of the tremendous strides the SEC has made over the past year. Yet our work is certainly not complete. We will continue investing the time and resources necessary to remediate our remaining deficiencies and build even stronger, more sustainable controls. That is what the public has every right to expect from their government.

Sincerely,



**Kenneth A. Johnson**  
Chief Financial Officer  
November 15, 2011

## Report of Independent Auditors



United States Government Accountability Office  
Washington, D.C. 20548

November 15, 2011

The Honorable Mary Schapiro  
Chairman  
United States Securities and Exchange Commission

Dear Ms. Schapiro:

The accompanying report presents the results of our audits of the financial statements of the United States Securities and Exchange Commission (SEC) and its Investor Protection Fund (IPF)<sup>1</sup> as of and for the fiscal years ended September 30, 2011, and 2010. The Accountability of Tax Dollars Act of 2002 requires that SEC prepare and submit audited financial statements to Congress and the Office of Management and Budget. The Securities Exchange Act of 1934, as amended in 2010 by the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act), requires SEC to prepare and submit a complete set of audited financial statements for IPF to Congress.<sup>2</sup> We agreed, under our audit authority, to audit SEC's and IPF's financial statements. Section 963 of the Dodd-Frank Act further requires that (1) SEC submit a report to Congress describing management's responsibility for internal control over financial reporting and assessing the effectiveness of such internal control during the fiscal year; (2) the SEC Chairman and Chief Financial Officer attest to SEC's report; and (3) GAO submit a report to Congress evaluating the effectiveness of SEC's internal control over financial reporting and assessing, attesting to, and reporting on SEC management's internal control assessment.<sup>3</sup> Accordingly, this report also responds to our requirement under the Dodd-Frank Act.

This report contains our (1) unqualified opinions on SEC's and IPF's fiscal years 2011 and 2010 financial statements; (2) opinion that, although internal controls could be improved, SEC maintained, in all material

<sup>1</sup>IPF was established in 2010 by section 922 of the Dodd-Frank Wall Street Reform and Consumer Protection Act to fund the activities of SEC's whistleblower award program and the SEC Office of Inspector General suggestion program. IPF is a separate fund within SEC and its financial statements present a segment of SEC financial activity. Accordingly, IPF's financial transactions are also included in SEC's financial statements.

<sup>2</sup> Section 21F(g)(5) of the Securities Exchange Act of 1934, 15 U.S.C. § 78u-6(g)(5).

<sup>3</sup> Dodd-Frank Act, Pub. L. No. 111-203, § 963, 124 Stat. 1376, 1910 (July 21, 2010)(codified at 15 U.S.C. § 78d-8).

---

respects, effective internal control over financial reporting for both the agency as a whole and IPF as of September 30, 2011;<sup>4</sup> and (3) conclusion that our tests of SEC's compliance with selected provisions of laws and regulations disclosed no instances of noncompliance for either the agency as a whole or IPF for fiscal year 2011.

---

We are sending copies of this report to the Chairmen and Ranking Members of the Senate Committee on Banking, Housing, and Urban Affairs; the Senate Committee on Homeland Security and Governmental Affairs; the House Committee on Financial Services; and the House Committee on Oversight and Government Reform. We are also sending copies to the Secretary of the Treasury, the Director of the Office of Management and Budget, and other interested parties. In addition, this report will be available at no charge on the GAO website at <http://www.gao.gov>.

If you have questions about this report, or if I can be of further assistance, please contact me at (202) 512-9406 or [dalkinj@gao.gov](mailto:dalkinj@gao.gov). Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. GAO staff who made key contributions to this report are listed in appendix II.

Sincerely yours,



James R. Dalkin  
Director  
Financial Management and Assurance

---

<sup>4</sup> Section 963(b) of the Dodd-Frank Act also requires, effective for fiscal year 2011, GAO to assess the effectiveness of SEC's internal control over financial reporting and SEC's assessment of the same. Our audit satisfies these requirements. See 15 U.S.C. § 78d-8(b), which codifies this requirement.



United States Government Accountability Office  
Washington, D.C. 20548

To the Chairman of the United States Securities and Exchange Commission

We agreed, under our audit authority, to audit the financial statements of the United States Securities and Exchange Commission (SEC) and the financial statements of SEC's Investor Protection Fund (IPF). The Securities Exchange Act of 1934, as amended in 2010 by the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act), requires that SEC provide separate audited financial statements for IPF to Congress.<sup>1</sup> Since IPF is a fund within SEC, its financial transactions are also included in SEC's overall financial statements. In accordance with the Dodd-Frank Act,<sup>2</sup> we are required to assess the effectiveness of SEC's internal control over financial reporting, evaluate SEC's assessment of such effectiveness, and attest to SEC's assessment of its internal control over financial reporting.

In our audits of SEC's financial statements and IPF's financial statements for fiscal years 2011 and 2010, we found

- the financial statements are presented fairly, in all material respects, in conformity with U.S. generally accepted accounting principles;
- although internal controls could be improved, SEC maintained, in all material respects, effective internal control over financial reporting for both the agency as a whole and IPF as of September 30, 2011; and
- no reportable noncompliance in fiscal year 2011 with provisions of laws and regulations we tested.

The following sections discuss in more detail (1) these conclusions; (2) our conclusions on Management's Discussion and Analysis and required supplementary and other accompanying information; (3) our audit objectives, scope, and methodology; and (4) SEC's comments on a draft of this report.

<sup>1</sup> Section 21F(g)(5) of the Securities Exchange Act of 1934, 15 U.S.C. § 78u-6(g)(5).

<sup>2</sup> Dodd-Frank Act, Pub. L. No. 111-203, § 963, 124 Stat. 1376, 1910 (July 21, 2010)(codified at 15 U.S.C. § 78d-8).

---



---

## Opinion on SEC's Financial Statements

The financial statements, including the accompanying notes, present fairly, in all material respects, in conformity with U.S. generally accepted accounting principles, SEC's assets, liabilities, and net position as of September 30, 2011 and 2010, and its net costs, changes in net position, budgetary resources, and custodial activity for the fiscal years then ended.

---

## Opinion on IPF's Financial Statements

The financial statements, including the accompanying notes, present fairly, in all material respects, in conformity with U.S. generally accepted accounting principles, IPF's assets, liabilities, and net position as of September 30, 2011 and 2010, and its net costs, changes in net position, and budgetary resources for the fiscal years then ended.

---

## Opinion on Internal Control

Although certain internal controls could be improved, SEC maintained, in all material respects, effective internal control over financial reporting as of September 30, 2011, that provided reasonable assurance that misstatements, losses, or noncompliance material in relation to the agency's and IPF's financial statements would be prevented or detected and corrected on a timely basis. Our opinion is based on criteria established under 31 U.S.C. § 3512 (c), (d), commonly known as the Federal Managers' Financial Integrity Act of 1982 (FMFIA). As discussed below, our fiscal year 2011 audit identified significant deficiencies in SEC's internal control over financial reporting.<sup>3</sup> These significant deficiencies pertain to SEC's financial reporting, but not that of IPF because of the nature of IPF's financial transactions during fiscal year 2011. Our opinion on SEC's internal control is consistent with SEC's assertion that its internal controls over financial reporting, both for the agency as a whole and for IPF, were operating effectively as of September 30, 2011, and that no material weaknesses were found in the design or operation of the

---

<sup>3</sup> A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

---

controls.<sup>4</sup> SEC management's assertion is included in its Management's Discussion and Analysis included in this report.

In our 2010 audit report,<sup>5</sup> we concluded that SEC did not maintain effective internal control over financial reporting as of September 30, 2010, because of material weaknesses<sup>6</sup> in SEC's internal control over (1) information systems and (2) financial reporting and accounting processes. Based on SEC's efforts to address the deficiencies we previously found in its controls over information systems, and the improvements we found in this area during our fiscal year 2011 audit, we concluded that the remaining deficiencies in information systems no longer constitute a material weakness. However, these remaining deficiencies in controls over information systems could adversely affect SEC's information security and its financial reporting relevant to these information systems. Therefore, we considered SEC's controls over information security to be a significant deficiency in fiscal year 2011. This significant deficiency is discussed in more detail later in this report.

During fiscal year 2011, SEC also made progress in addressing the five areas of internal control deficiencies that collectively comprised the material weakness over financial reporting and accounting processes in fiscal year 2010. Specifically, SEC sufficiently addressed the deficiencies regarding SEC's internal controls related to accounting for disgorgement

---

<sup>4</sup> Dodd-Frank Act, Pub. L. No. 111-203, § 963, 124 Stat. 1376, 1910 (July 21, 2010)(codified at 15 U.S.C. § 78d-8), requires that (1) SEC submit a report to Congress describing management's responsibility for internal control over financial reporting and assessing the effectiveness of such internal control during the fiscal year, (2) the SEC Chairman and Chief Financial Officer attest to SEC's report, and (3) GAO submit a report to Congress evaluating the effectiveness of SEC management's internal control over financial reporting and management's assessment of such control and attesting to the internal control assessment made by SEC. SEC conducted an evaluation of its internal control over financial reporting in accordance with the Office of Management and Budget's Circular No. A-123, *Management's Responsibility for Internal Control*, based on criteria established under FMFIA.

<sup>5</sup> GAO, *Financial Audit: Securities and Exchange Commission's Financial Statements for Fiscal Years 2010 and 2009*, GAO-11-202 (Washington, D.C.: Nov. 15, 2010).

<sup>6</sup>A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented or detected and corrected on a timely basis. A deficiency in internal control 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 and correct, misstatements on a timely basis.

---

and penalties<sup>7</sup> and reporting required supplementary information such that we no longer consider these two areas to be control deficiencies as of September 30, 2011. SEC also addressed some of the issues comprising deficiencies in its financial reporting and accounting processes, budgetary resources, and registrant deposit and filing fee transactions that were also part of the material weakness in internal control over financial reporting in fiscal year 2010. However, our work in fiscal year 2011 showed continuing deficiencies in the design and/or implementation of effective internal control for each of these three areas that were significant to SEC's financial reporting as of September 30, 2011. Therefore, while they no longer collectively represent a material weakness, we considered each of these remaining continuing deficiencies to represent a significant deficiency in internal control in fiscal year 2011. These three significant deficiencies are discussed later in this report.

For all significant errors and issues that were identified, SEC made necessary adjustments to the financial statements, the notes accompanying the financial statements, and other required supplementary information, as appropriate, and was therefore able to prepare financial statements that were fairly presented in all material respects for fiscal years 2011 and 2010. Although the significant deficiencies in internal control did not materially affect SEC's fiscal year 2011 financial statements, misstatements may occur in other financial information reported by SEC and not be prevented or detected because of these significant deficiencies.

The four significant deficiencies as of September 30, 2011, although not considered to be material weaknesses, are important enough to merit the attention of those charged with governance of SEC. We will be reporting additional details concerning these four significant deficiencies separately to SEC management, along with recommendations for corrective actions. We also identified other deficiencies in SEC's system of internal control that we do not consider to be material weaknesses or significant deficiencies. We have communicated these matters to SEC management informally and, as appropriate, will be reporting them separately to SEC at a later date.

---

<sup>7</sup>A disgorgement is the repayment of illegally gained profits (or avoided losses) for distribution to harmed investors whenever feasible. A penalty is a monetary payment from a violator of securities law that SEC obtains pursuant to statutory authority. A penalty is fundamentally a punitive measure, although penalties occasionally can be used to compensate harmed investors.

---



---

## Compliance with Laws and Regulations

Our tests of SEC's compliance with selected provisions of laws and regulations for the agency as a whole and IPF for fiscal year 2011 disclosed no instances of noncompliance that would be reportable under U.S. generally accepted government auditing standards. The objective of our audit was not to provide an opinion on overall compliance with laws and regulations. Accordingly, we do not express such an opinion.

As disclosed in note 14C to SEC's financial statements, a GAO legal decision,<sup>8</sup> issued on October 3, 2011, concluded that SEC did not properly record its obligation when it entered into a 10-year lease by failing to record its total liability under the lease at the date when the lease was signed. Specifically, GAO concluded that SEC did not have the authority to record an obligation for an amount less than the government's full liability under the lease and was therefore in violation of the recording statute.<sup>9</sup> SEC made adjustments to its budget accounts in order to properly record any lease agreements it entered into during fiscal year 2011. SEC also made an adjustment to its budget accounts in fiscal year 2011 to obligate \$778 million for the full amount of its lease obligations it entered into during fiscal years 1990 through 2010. However, since SEC lacked sufficient budgetary authority to cover the \$778 million in lease obligations, it incurred violations of the Antideficiency Act for fiscal years 1990 through 2010, the years in which these obligations were incurred.

---

## Consistency of Other Information

SEC's Management's Discussion and Analysis, required supplementary information, and other accompanying information contain a wide range of information, some of which is not directly related to the financial statements. We did not audit and we do not express an opinion on this information. However, we compared this information for consistency with the financial statements and discussed the methods of measurement and presentation with SEC officials. On the basis of this limited work, we found no material inconsistencies with the financial statements, U.S. generally

---

<sup>8</sup>B-322160, Oct. 3, 2011 (*Securities and Exchange Commission—Recording of Obligation for Multiple-Year Contract*).

<sup>9</sup>Pursuant to the recording statute, 31 U.S.C. § 1501(a)(1), an agency is required to record the full amount of its contractual obligation against funds available at the time a contract is executed, and any authorization to record an obligation for an amount less than the full amount of the government's contractual obligation must be explicit.

---

accepted accounting principles, or Office of Management and Budget Circular No. A-136, *Financial Reporting Requirements*.

---

## Objectives, Scope, and Methodology

SEC management is responsible for (1) preparing the financial statements of the agency and IPF in conformity with U.S. generally accepted accounting principles; (2) establishing and maintaining effective internal control over financial reporting for both the agency as a whole and IPF, and evaluating its effectiveness; and (3) complying with laws and regulations applicable to both the agency and IPF. SEC management evaluated the effectiveness of internal control over financial reporting as of September 30, 2011, based on the criteria established under FMFIA. Under the Dodd-Frank Act, SEC is also responsible for attesting to the effectiveness of its internal control during the fiscal year.<sup>10</sup>

We are responsible for planning and performing the audits of SEC and IPF to obtain reasonable assurance and provide our opinion about whether (1) the financial statements are presented fairly, in all material respects, in conformity with U.S. generally accepted accounting principles and (2) SEC management maintained, in all material respects, effective internal control over financial reporting for the agency as a whole and IPF as of September 30, 2011. We are also responsible for (1) testing compliance with selected provisions of laws and regulations that have a direct and material effect on the financial statements of SEC and IPF and (2) performing limited procedures with respect to certain other information accompanying the financial statements. Further, under the Dodd-Frank Act, we are responsible for evaluating SEC's assessment of its internal control over financial reporting.<sup>11</sup>

In order to fulfill these responsibilities, we

- examined, on a test basis, evidence supporting the amounts and disclosures in the financial statements;
- assessed the accounting principles used and significant estimates made by SEC management;

---

<sup>10</sup> Dodd-Frank Act, Pub. L. No. 111-203, § 963, 124 Stat. 1376, 1910 (July 21, 2010)(*codified at* 15 U.S.C. § 78d-8).

<sup>11</sup> 15 U.S.C. § 78d-8(b)(1).

- 
- 
- evaluated the overall presentation of the financial statements;
  - obtained an understanding of SEC's and IPF's operations, including SEC's internal control over financial reporting for both the agency as a whole and IPF;
  - considered SEC's process for evaluating and reporting on internal control over financial reporting based on criteria established under FMFIA;
  - assessed the risk that a material misstatement exists in the financial statements and the risk that a material weakness exists in internal control over financial reporting;
  - evaluated the design and operating effectiveness of internal control over financial reporting based on the assessed risk;
  - tested relevant internal control over financial reporting;
  - evaluated SEC's assessment of its internal control over financial reporting;
  - tested compliance with selected provisions of the following laws and regulations: the Securities Exchange Act of 1934, as amended; the Securities Act of 1933, as amended; the Antideficiency Act; laws governing the pay and allowance system for SEC employees; the Debt Collection Improvement Act; the Prompt Payment Act; the Federal Employees' Retirement System Act of 1986; Full-Year Continuing Appropriations Act, 2011, which incorporates, by reference, certain provisions of the Financial Services and General Government Appropriations Act, 2010; and the Dodd-Frank Wall Street Reform and Consumer Protection Act; and
  - performed such other procedures as we considered necessary in the circumstances.

An entity's internal control over financial reporting is a process effected by those charged with governance, management, and other personnel, the objectives of which are to provide reasonable assurance that (1) transactions are properly recorded, processed, and summarized to permit the preparation of financial statements in accordance with U.S. generally accepted accounting principles, and assets are safeguarded against loss

---

from unauthorized acquisition, use, or disposition and (2) transactions are executed in accordance with the laws governing the use of budget authority and other laws and regulations that could have a direct and material effect on the financial statements.

We did not evaluate all internal control relevant to operating objectives as broadly established under FMFIA, such as controls relevant to preparing statistical reports and ensuring efficient operations. We limited our internal control testing to testing controls over financial reporting that are significant to SEC's and IPF's financial statements. Our internal control testing was for the purpose of expressing an opinion on the effectiveness of internal control over financial reporting and may not be sufficient for other purposes. Consequently, our audit may not identify all deficiencies in internal control over financial reporting that are less severe than a material weakness. Because of inherent limitations, internal control may not prevent or detect and correct misstatements caused by error or fraud, losses, or noncompliance. We also caution that projecting any evaluation of effectiveness to future periods is subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

We did not test compliance with all laws and regulations applicable to SEC or IPF. We limited our tests of compliance to selected provisions of laws and regulations that have a direct and material effect on SEC's and IPF's financial statements for the fiscal year ended September 30, 2011. We caution that other deficiencies in internal control may exist and not be detected by our tests and that our testing may not be sufficient for other purposes.

We performed our audit in accordance with U.S. generally accepted government auditing standards. We believe our audit provides a reasonable basis for our opinions and other conclusions.

---

## Significant Deficiency over Information Security

In our previous year's audit of SEC, we reported a material weakness in internal control over information systems because of pervasive deficiencies in the design and operation of SEC's information security and other system controls that spanned across its general support system and all key applications that supported financial reporting.<sup>12</sup> During fiscal year 2011, SEC made progress in addressing several of the control deficiencies that comprised this material weakness and thereby strengthened its overall security program. Notable among these efforts were the security

---

access control improvements and updates SEC made to its core general ledger system, reducing the system's vulnerability to unauthorized access, viruses, attacks, and other threats. SEC also implemented a security monitoring program over its core general ledger system to better identify and address segregation of incompatible duties and an entitywide system security program for its general support system to identify and address security risks. Further, SEC improved its capacity to effectively carry out information security controls through its increased investments in hiring information security staff. However, because SEC's remediation efforts focused primarily on its general ledger system and general support system, we continued to find information security design and implementation deficiencies similar to those found in our previous audit as well as new deficiencies concerning other key financial systems and databases that support financial reporting. These deficiencies decrease assurance regarding the reliability of the data processed by these key financial systems and increase the risk that unauthorized individuals could gain access to critical hardware or software and intentionally or inadvertently access, alter, or delete sensitive data or computer programs. Consequently, the combination of the continuing and new information security deficiencies existing as of September 30, 2011, considered collectively, represent a significant deficiency in SEC's internal control over information security.

Specifically, our fiscal year 2011 testing found that SEC did not perform necessary or adequate information security system updates on its financial system that processes significant amounts of filing fee revenue or its database that houses disgorgement and penalty financial data, thus exposing SEC to information security vulnerabilities in these areas. We also found that for some of its key financial applications, SEC did not always set sufficiently restrictive security-related parameters and users' rights and privileges, effectively secure remote connections, or effectively manage guest user accounts and open ports to prevent unauthorized access to its internal network. SEC also did not always ensure proper security oversight and monitoring of system connections for its information systems that were connected to external systems to ensure the existence of proper security requirements pertaining to these external systems. In addition, SEC did not always adequately protect or secure the confidentiality and integrity of sensitive data transmitted across its internal networks. Further, SEC did not appropriately manage its password

---

<sup>12</sup> GAO-11-202.

---

accounts or set system password protections for some of its key financial applications in accordance with its policy, resulting in weak passwords and excessive log-in attempts being allowed before a user's account is suspended.

Additionally, we found that while SEC implemented sufficient security monitoring and auditing tools over its core general ledger system in fiscal year 2011, it did not do so systemically for all of its key system applications that support financial reporting and consequently, it does not yet have comprehensive oversight of, and information concerning, the security risks to financial reporting. Information security risks are further amplified because SEC did not always implement vulnerability and compliance scans on network devices required under its information security program. Until SEC consistently implements all key elements of its information security program systemically across all its financial systems and applications that support financial reporting, there is increased risk that the information that is processed, stored, and transmitted on its systems remain vulnerable, and management will not have sufficient assurance that financial information and financial assets are adequately safeguarded from inadvertent or deliberate misuse, fraudulent use, improper disclosure, or destruction.

---

## Significant Deficiency over Financial Reporting and Accounting Processes

As we have reported in prior audits, SEC's general ledger system and certain software applications and configurations are not designed to provide the accurate, complete, and timely transaction-level data needed to accumulate and readily report reliable financial information. Instead, the initiation and recording of significant transactions is accomplished through the use of spreadsheets, databases, manual workarounds, and data handling that rely on significant analysis, reconciliation, and review to calculate amounts for the general ledger posting of transactions. These compensating manual processes are resource intensive and prone to error, and coupled with the significant amount of data involved, increase the risk of materially misstated account balances in the general ledger. To address some of the risks in its financial reporting and accounting processes, in fiscal year 2011 SEC implemented a reconciliation control procedure to provide some assurance that the data in its financial reporting tool database that is used to produce its monthly trial balances and financial statements are consistent with the source data in the general ledger. SEC also made enhancements this year to its financial reporting tool that assisted SEC in researching and reviewing financial activity, such as the development of record counts to facilitate comparison of data and

systematic timestamps to ensure the appropriate file is being used. In addition, SEC drafted a policy to strengthen and formalize application and security controls over its spreadsheets and databases (referred to by SEC as user developed applications); however, this policy did not become effective until September 30, 2011. Consequently, SEC operated throughout the fiscal year without adequate controls over some of its user developed applications. Despite SEC's actions to improve controls in this area, errors and deficiencies we found during this year's audit demonstrate that SEC remains at risk of not properly controlling user developed applications and manual financial reporting and accounting processes. Therefore, collectively, these continuing deficiencies represent a significant deficiency in internal control over SEC's financial reporting and accounting processes for fiscal year 2011.

For example, during this year's audit, we found errors in SEC's year-end calculation of its allowance for loss on the disgorgement and penalties receivable because of a spreadsheet formula error that was not discovered by SEC's review process. We also found that SEC made errors in its lease calculations because it used incorrect lease term and rate assumptions and because of spreadsheet formula errors that were also not detected. In addition, we noted that a spreadsheet error resulted in incorrect amounts for SEC's legal liability and lease liability disclosed in the notes to SEC's interim financial statements. SEC made the necessary adjustments to address these errors so that related balances were properly stated at year-end. However, these and other errors we found point to a lack of effective review procedures, which are even more critical given SEC's heavy dependence on spreadsheets and error-prone manual data entry for its financial reporting and accounting processes.

## Significant Deficiency over Budgetary Resources

For fiscal year 2011, SEC incurred approximately \$2 billion in new obligations,<sup>13</sup> which represent legal liabilities against funds available to SEC to pay for goods and services ordered, and deobligated approximately \$39 million for prior year obligations that were either canceled or for which the dollar amount of the obligation was decreased. During this fiscal year, SEC addressed some of the control deficiencies

<sup>13</sup> In fiscal year 2011, SEC also recorded \$778 million in additional obligations to recognize its full lease obligations pursuant to a GAO legal decision—B-322160, Oct. 3, 2011—concerning SEC's multi-year leasing authority. Refer to note 14 (Status of Budgetary Resources) to the financial statements for a further discussion of this issue.

---

that we have reported on in the past in this area. A noteworthy action that SEC implemented this year to compensate for a control issue concerning the timeliness of recording deobligations was the implementation of an accounting procedure for estimating an accrual for downward adjustments to obligations in situations where an obligation is no longer valid but has not yet been closed out. This accrual adjustment accounted for \$14.5 million of the total \$39 million in deobligations for fiscal year 2011. SEC also improved procedures this year for deobligating travel obligations and for recording miscellaneous obligations. However, consistent with our findings from our audits of SEC over the past 5 years, this year's audit continued to find general ledger system configuration deficiencies and continuing deficiencies in recording of obligations, monitoring open obligations, and deobligating obligations that were no longer valid. Collectively, these continuing deficiencies represent a significant deficiency in internal control over budgetary resources for fiscal year 2011.

Specifically, because of general ledger system configuration deficiencies that limit SEC from properly posting undelivered order and offsetting collection transactions,<sup>14</sup> SEC recorded \$38 million in manual correcting entries to accurately reflect related account balances on the Statement of Budgetary Resources for fiscal year 2011. Our testing of new obligations during the year also continued to find obligations that were either not supported by sufficient documentation or documentation showing that they were approved by an authorized individual, or were no longer required and therefore should have been deobligated. The errors we found indicated a likely \$12.7 million misstatement in SEC's obligation balance at June 30, 2011. In addition, our fiscal year 2011 testing showed a continuing deficiency in SEC's control over monitoring and reviewing its open obligations to ensure that they remain valid and that adjustments are made properly and timely. Of the 45 recorded deobligations we tested, we found that 28 were not deobligated timely. For example, our work found that SEC's contract close-out process took from 3 months to more than 3 years to complete from the end of the period of performance or completion of the contract. This is largely because SEC does not have a control in place to monitor its contracts in a timely manner, and therefore, needs to carry out time-consuming reconciliation procedures with its vendors before it can

---

<sup>14</sup>Undelivered orders represent obligations incurred for goods or services that have been ordered but not yet received. Offsetting collections are amounts that SEC receives from businesslike transactions with the public (e.g., fees for filing registration statements), which SEC is authorized to credit to its appropriations account for future obligations.

properly adjust an obligation or deobligate an obligation for contracts that were completed or whose period of performance had ended. Deobligating resources timely can be important to an agency to free up resources that may be made available for incurring new obligations or used to provide resources to fund increases to existing obligations.

SEC's new accrual procedure for downward adjustments to open obligations has resulted in more accurate financial reporting of budgetary activity on the Statement of Budgetary Resources for fiscal year 2011. However, the continuing ineffective processes and related documentation deficiencies that caused the errors in budgetary transactions increase SEC's risk of future misstatements being recorded in its general ledger and reported on its Statement of Budgetary Resources.

### Significant Deficiency over Registrant Deposits and Filing Fees

SEC is partially funded through the collection of securities registration, tender offer, merger, and other fees (filing fees) from registrants. SEC records the filing fees it collects as revenue. If registrants submit amounts to SEC in excess of the actual fee payment due for a specific filing, SEC records the excess amounts collected in a registrant deposit liability account until earned by SEC from a future filing. Pursuant to a revised SEC policy, SEC is to return to the account holder any funds held in any filing fee account in which there has not been any deposit, withdrawal or other adjustment activity for more than 3 years.<sup>15</sup> We have reported deficiencies in controls over SEC's registrant deposits since fiscal year 2009 and have made recommendations to improve controls over filing fee transactions. This year we noted that SEC made improvements in verifying current filing fee transactions more timely. However, our audit this year found continuing deficiencies in SEC's controls over registrant deposits and filing fees that collectively represent a significant deficiency for fiscal year 2011.

Specifically, SEC has not effectively addressed previously reported deficiencies in its process to enable timely recognition of filing fee revenue. For example, SEC still has not completed its review of dormant registrant

<sup>15</sup>In May 2011, for efficiency reasons and to better harmonize with similar rules pertaining to registrant activity, SEC approved an amendment to its account clearing procedures to extend the period in which SEC should hold a registrant's funds in a dormant account from 180 days to 3 years. See SEC regulation at 17 C.F.R. § 202.3a(e) (Return of Funds from Inactive Accounts); see also 76 Fed. Reg. 28,888 (May 19, 2011).

deposit accounts, which consisted of 2,042 accounts totaling over \$12 million as of September 30, 2011, to determine if any of these amounts should be refunded or recognized as revenue. Because of this continuing control deficiency, SEC is not always recognizing filing fee revenue in the correct accounting period and its registrant deposit liability of \$46 million as of September 30, 2011, could be misstated and not be corrected in a timely manner. For example, as of September 30, 2011, SEC identified \$2.3 million in the liability account that should have been recognized as revenue. The change in SEC's policy this year for extending the time period from 180 days to 3 years before initiating a return of funds explains the majority of the reduction in the balance of dormant accounts from \$25.7 million at September 30, 2010, to \$12.5 million at September 30, 2011. However, SEC has made limited progress in researching and determining the proper accounting treatment for the remaining backlog of dormant accounts. SEC has taken some short-term actions to compensate for its lack of timely review. For example, in the fourth quarter of fiscal year 2011, SEC implemented a new procedure to statistically analyze the inactive deposit accounts in order to estimate the amount of unrecognized revenue. This procedure resulted in an estimate of about \$7 million in unrecognized revenue pertaining to the dormant accounts. Contributing to SEC's deficiencies in this area is that SEC has yet to finalize and implement a formal process for ongoing monitoring of filing fee transactions.

## Agency Comments

In commenting on a draft of this report, SEC's Chairman expressed her pleasure that GAO found that SEC has successfully remediated the two material weaknesses identified in 2010, and attributes this success to its new leadership team of the Chief Operating Officer, Chief Financial Officer, Chief Information Officer, and Chief Accounting Officer. She stated that SEC will continue working to ensure that its controls infrastructure is strong and sustainable over the long term. The Chairman also commented that SEC will realize improvements in system functionality, automate some manual processes, and further enhance financial management and reporting upon completion in fiscal year 2012 of a migration of its core financial system to a federal government shared service provider. The Chairman added that SEC plans further progress on tightening information security, resolving the backlog of inactive registrant deposit accounts, bolstering controls over budgetary resources, and completing implementation of its new program governing the use of spreadsheets and databases related to financial reporting.

---

The complete text of SEC's comments is reprinted in its entirety in appendix I.

Sincerely yours,



James R. Dalkin  
Director  
Financial Management and Assurance

November 14, 2011

## Management's Response to Audit Opinion



THE CHAIRMAN

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

November 10, 2011

Mr. James R. Dalkin  
Director  
Financial Management and Assurance  
United States Government Accountability Office  
441 G Street, N.W.  
Washington, DC 20548

Dear Mr. Dalkin:

Thank you for the opportunity to review and comment on the audit report of the Government Accountability Office (GAO). I am pleased that the GAO's FY 2011 audit found that the SEC's financial statements and notes were presented fairly, in all material respects, and in conformity with U.S. generally accepted accounting principles.

Furthermore, I am delighted the GAO found that the SEC has successfully remediated the two material weaknesses identified in 2010. Under the newly-completed leadership team of the Chief Operating Officer, Chief Financial Officer, Chief Information Officer, and Chief Accounting Officer, the SEC has treated this remediation effort as a top priority, and GAO's opinion confirms the significant progress the agency has made in strengthening its internal controls.

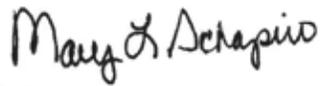
Although I am gratified by this achievement, the SEC's efforts in this area will not cease. The SEC will continue working to ensure that our controls infrastructure is strong and sustainable over the long term. In this regard, the agency has been engaged in a multi-year effort to migrate its core financial system to the Federal Shared Service Provider (FSSP) at the Department of Transportation's Enterprise Services Center (ESC). Through this initiative, the SEC will realize improvements in system functionality, automate some manual processes, and further enhance financial management and reporting. The SEC plans to complete the migration in FY 2012.

In addition, in FY 2012 the SEC will continue remediation related to the remaining deficiency areas identified in your report. The SEC plans further progress on tightening information security, resolving the backlog of inactive registrant deposit accounts, bolstering controls over budgetary resources, and completing implementation of our new program governing the use of spreadsheets and databases related to financial reporting. We welcome GAO's feedback on these initiatives throughout the process.

Mr. James R. Dalkin  
Page 2

I very much appreciate the professional manner in which you and your team conducted the audit for FY 2011. I look forward to continuing our productive dialogue in the coming months on the financial system migration and the SEC's efforts to address the areas noted in your report. If you have any questions, please feel free to contact me.

Sincerely,

A handwritten signature in black ink that reads "Mary L. Schapiro". The signature is written in a cursive, flowing style.

Mary L. Schapiro  
Chairman

## **SEC FINANCIAL STATEMENTS**

---

Financial Statements	124
Notes to the Financial Statements	129
Required Supplementary Information (Unaudited)	155

## Financial Statements

U.S. SECURITIES AND EXCHANGE COMMISSION

### Balance Sheet

As of September 30, 2011 and 2010

(DOLLARS IN THOUSANDS)

	FY 2011	FY 2010
<b>ASSETS (Notes 2 and 11):</b>		
Intragovernmental:		
Fund Balance with Treasury (Note 3)	\$ 6,995,610	\$ 6,989,367
Investments, Net (Note 5)	1,202,525	924,823
Accounts Receivable (Note 6)	20	–
Advances and Prepayments	7,172	2,198
Total Intragovernmental	8,205,327	7,916,388
Cash and Other Monetary Assets (Note 4)	–	2,815
Accounts Receivable, Net (Note 6)	214,026	161,143
Advances and Prepayments	3,656	2,381
Property and Equipment, Net (Note 7)	93,939	79,712
<b>Total Assets</b>	<b>\$ 8,516,948</b>	<b>\$ 8,162,439</b>
<b>LIABILITIES (Notes 8 and 11):</b>		
Intragovernmental:		
Accounts Payable	\$ 8,049	\$ 5,185
Employee Benefits	2,877	6,088
Unfunded FECA and Unemployment Liability	1,770	1,719
Custodial Liability	51,745	42,380
Liability for Non-Entity Assets	134	4
Total Intragovernmental	64,575	55,376
Accounts Payable	52,768	46,260
Accrued Payroll and Benefits	18,395	31,649
Accrued Leave	45,472	45,629
Registrant Deposits	46,622	44,729
Actuarial FECA Liability	7,805	7,576
Liability for Disgorgement and Penalties (Note 16)	862,976	1,021,466
Other Accrued Liabilities (Note 8)	7,212	29,270
<b>Total Liabilities</b>	<b>1,105,825</b>	<b>1,281,955</b>
Commitments and Contingencies (Note 10)		
<b>NET POSITION (Note 11):</b>		
Unexpended Appropriations – Other Funds	735	1,749
Cumulative Results of Operations – Earmarked Funds	7,409,186	6,878,132
Cumulative Results of Operations – Other Funds	1,202	603
<b>Total Net Position</b>	<b>\$ 7,411,123</b>	<b>\$ 6,880,484</b>
<b>Total Liabilities and Net Position</b>	<b>\$ 8,516,948</b>	<b>\$ 8,162,439</b>

The accompanying notes are an integral part of these financial statements.

U.S. SECURITIES AND EXCHANGE COMMISSION

**Statement of Net Cost***For the years ended September 30, 2011 and 2010*

<i>(DOLLARS IN THOUSANDS)</i>	<b>FY 2011</b>	<b>FY 2010</b>
<b>PROGRAM COSTS (Note 12):</b>		
Enforcement	\$ 391,183	\$ 355,451
Compliance Inspections and Examinations	239,435	229,389
Corporation Finance	131,660	131,166
Trading and Markets	62,176	54,107
Investment Management	47,240	47,873
Risk, Strategy and Financial Innovation	20,080	18,143
General Counsel	41,357	39,780
Other Program Offices	45,122	48,603
Agency Direction and Administrative Support	163,357	128,531
Inspector General	6,528	5,380
<b>Total Program Costs</b>	1,148,138	1,058,423
Less: Earned Revenue Not Attributed to Programs (Note 12)	1,643,730	1,382,856
<b>Net (Income) Cost from Operations (Note 15)</b>	\$ (495,592)	\$ (324,433)

*The accompanying notes are an integral part of these financial statements.*

U.S. SECURITIES AND EXCHANGE COMMISSION

**Statement of Changes in Net Position***For the years ended September 30, 2011 and 2010*

<i>(DOLLARS IN THOUSANDS)</i>	FY 2011		
	Earmarked Funds	All Other Funds	Consolidated Total
<b>CUMULATIVE RESULTS OF OPERATIONS:</b>			
Beginning Balances	\$ 6,878,132	\$ 603	\$ 6,878,735
<b>Budgetary Financing Sources:</b>			
Appropriations Used	—	1,014	1,014
Non-Exchange Revenue	990	—	990
<b>Other Financing Sources:</b>			
Imputed Financing (Note 13)	34,380	—	34,380
Other	—	(323)	(323)
Total Financing Sources	35,370	691	36,061
Net Income (Cost) from Operations	495,684	(92)	495,592
Net Change	531,054	599	531,653
Cumulative Results of Operations (Note 11)	7,409,186	1,202	7,410,388
<b>UNEXPENDED APPROPRIATIONS:</b>			
Beginning Balances	—	1,749	1,749
<b>Budgetary Financing Sources:</b>			
Appropriations Used	—	(1,014)	(1,014)
Total Unexpended Appropriations	—	735	735
<b>Net Position, End of Period</b>	<b>\$ 7,409,186</b>	<b>\$ 1,937</b>	<b>\$ 7,411,123</b>

<i>(DOLLARS IN THOUSANDS)</i>	FY 2010		
	Earmarked Funds	All Other Funds	Consolidated Total
<b>CUMULATIVE RESULTS OF OPERATIONS:</b>			
Beginning Balances	\$ 6,058,225	\$ —	\$ 6,058,225
<b>Budgetary Financing Sources:</b>			
Appropriations Used	—	8,111	8,111
Non-Exchange Revenue	451,910	—	451,910
<b>Other Financing Sources:</b>			
Imputed Financing (Note 13)	36,216	—	36,216
Other	—	(160)	(160)
Total Financing Sources	488,126	7,951	496,077
Net Income (Cost) from Operations	331,781	(7,348)	324,433
Net Change	819,907	603	820,510
Cumulative Results of Operations (Note 11)	6,878,132	603	6,878,735
<b>UNEXPENDED APPROPRIATIONS:</b>			
Beginning Balances	—	9,860	9,860
<b>Budgetary Financing Sources:</b>			
Appropriations Used	—	(8,111)	(8,111)
Total Unexpended Appropriations	—	1,749	1,749
<b>Net Position, End of Period</b>	<b>\$ 6,878,132</b>	<b>\$ 2,352</b>	<b>\$ 6,880,484</b>

*The accompanying notes are an integral part of these financial statements.*

U.S. SECURITIES AND EXCHANGE COMMISSION

**Statement of Budgetary Resources***For the years ended September 30, 2011 and 2010*

<i>(DOLLARS IN THOUSANDS)</i>	<b>FY 2011</b>	<b>FY 2010</b>
<b>BUDGETARY RESOURCES:</b>		
Unobligated Balance, Brought Forward, October 1	\$ 489,349	\$ 26,765
Recoveries of Prior Year Unpaid Obligations	38,945	18,753
Budget Authority:		
Appropriation	(847)	451,910
Spending Authority from Offsetting Collections:		
Earned:		
Collected	1,598,067	1,443,347
Change in Receivables from Federal Sources	20	(188)
Change in Unfilled Customer Orders:		
Advance Received	-	(157)
Without Advance from Federal Sources	2	(98)
Subtotal	1,597,242	1,894,814
Temporarily not Available Pursuant to Public Law	(412,005)	(347,694)
<b>Total Budgetary Resources</b>	<b>\$ 1,713,531</b>	<b>\$ 1,592,638</b>
<b>STATUS OF BUDGETARY RESOURCES:</b>		
Obligations Incurred:		
Direct (Note 14)	\$ 1,215,144	\$ 1,103,007
Direct, Change in Legal Interpretation for Lease Obligations (Note 14)	777,928	-
Reimbursable (Note 14)	388	282
Subtotal	1,993,460	1,103,289
Unobligated Balance:		
Apportioned	459,248	17,213
Unobligated Balance Not Available	(739,177)	472,136
<b>Total Status of Budgetary Resources</b>	<b>\$ 1,713,531</b>	<b>\$ 1,592,638</b>
<b>CHANGE IN OBLIGATED BALANCE:</b>		
Obligated Balance, Net:		
Unpaid Obligations, Brought Forward, October 1	\$ 317,772	\$ 236,399
Uncollected Customer Payments from Federal Sources, Brought Forward, October 1	(25)	(311)
Total Unpaid Obligated Balance, Net, Beginning of Fiscal Year	317,747	236,088
Obligations Incurred Net	1,993,460	1,103,289
Gross Outlays	(1,161,653)	(1,003,163)
Recoveries of Prior Year Unpaid Obligations, Actual	(38,945)	(18,753)
Change in Uncollected Customer Payments from Federal Sources	(22)	286
Total, Unpaid Obligated Balance, Net, End of Period (Note 10)	\$ 1,110,587	\$ 317,747
Obligated Balance, Net, End of Period:		
Unpaid Obligations	1,110,634	317,772
Uncollected Customer Payments from Federal Sources	(47)	(25)
Total, Unpaid Obligated Balance, Net, End of Period (Note 10)	\$ 1,110,587	\$ 317,747
<b>NET OUTLAYS:</b>		
Net Outlays:		
Gross Outlays	\$ 1,161,653	\$ 1,003,163
Offsetting Collections	(1,598,067)	(1,443,190)
Distributed Offsetting Receipts	660	194
Net Outlays/(Collections)	\$ (435,754)	\$ (439,833)

*The accompanying notes are an integral part of these financial statements.*

U.S. SECURITIES AND EXCHANGE COMMISSION

**Statement of Custodial Activity***For the years ended September 30, 2011 and 2010**(DOLLARS IN THOUSANDS)*

	FY 2011	FY 2010
<b>REVENUE ACTIVITY:</b>		
Sources of Cash Collections:		
Disgorgement and Penalties	\$ 413,413	\$ 1,116,632
Other	8,109	1
Total Cash Collections	421,522	1,116,633
Accrual Adjustments	9,365	42,380
<b>Total Custodial Revenue</b>	<b>430,887</b>	<b>1,159,013</b>
<b>DISPOSITION OF COLLECTIONS:</b>		
Amounts Transferred to:		
Department of the Treasury	421,522	664,723
Investor Protection Fund	—	451,910
Amounts Yet to be Transferred	9,365	42,380
<b>Total Disposition of Collections</b>	<b>430,887</b>	<b>1,159,013</b>
<b>NET CUSTODIAL ACTIVITY</b>	<b>\$ —</b>	<b>\$ —</b>

*The accompanying notes are an integral part of these financial statements.*

## Notes to the Financial Statements

U.S. SECURITIES AND EXCHANGE COMMISSION

As of September 30, 2011 and 2010

### NOTE 1. Summary of Significant Accounting Policies

#### A. Reporting Entity

The Securities and Exchange Commission (SEC) is an independent agency of the U.S. Government established pursuant to the Securities Exchange Act of 1934 (Exchange Act), charged with regulating this country's capital markets. The SEC's mission is to protect investors; maintain fair, orderly, and efficient securities markets; and facilitate capital formation. The SEC works with Congress, other executive branch agencies, Self Regulatory Organizations (SROs) (e.g., securities exchanges and the Financial Industry Regulatory Authority (FINRA)), accounting and auditing standards setters, state securities regulators, law enforcement officials, and many other organizations in support of the agency's mission.

The agency's programs protect investors and promote the public interest by fostering and enforcing compliance with the Federal securities laws; establishing an effective regulatory environment; facilitating access to the information investors need to make informed investment decisions; and enhancing the SEC's performance through effective alignment and management of human, information, and financial capital.

The SEC consists of five presidentially-appointed Commissioners, with staggered five-year terms. The SEC is organized into five Divisions and multiple offices. The five divisions are the Division of Corporation Finance; the Division of Trading and Markets; the Division of Investment Management; the Division of Enforcement; and the Division of Risk, Strategy, and Financial Innovation. The offices include the Office of Administrative Law Judges, the Office of Compliance Inspections and Examinations, the Office of the Chief Accountant, Office of Investor Education and Advocacy and various supporting services.

The SEC reporting entity includes the Investor Protection Fund (See Note 1.T. *Investor Protection Fund*). As discussed in Note 10.A. *Commitments: Securities Investor Protection Act*, the SEC reporting entity does not include the Securities Investor Protection Corporation (SIPC).

As discussed at Note 1.S. *Disgorgement and Penalties*, disgorgement funds collected and held by the SEC on behalf of harmed investors are part of the SEC reporting entity. However, disgorgement funds held by the U.S. Courts and by non-Federal receivers on behalf of harmed investors are not part of the SEC reporting entity.

#### B. Basis of Presentation and Accounting

The accompanying financial statements present the financial position, net cost of operations, changes in net position, budgetary resources, and custodial activities of the SEC's core business activities as required by the Accountability of Tax Dollars Act of 2002. The statements may differ from other financial reports submitted pursuant to Office of Management and Budget (OMB) directives for the purpose of monitoring and controlling the use of the SEC budgetary resources, due to differences in applicable accounting and reporting principles discussed in the following paragraphs. The SEC's books and records serve as the source of the information presented in the accompanying financial statements.

The agency classifies assets, liabilities, revenues, and costs in these financial statements according to the type of entity associated with the transactions. Intragovernmental assets and liabilities are those due from or to other Federal entities. Intragovernmental revenues are earned from other Federal entities. Intragovernmental costs are payments or accruals due to other Federal entities.

The SEC's financial statements are prepared in conformity with generally accepted accounting principles (GAAP) for the Federal Government and presented in conformity with OMB Circular A-136, *Financial Reporting Requirements*. The Balance Sheet, Statement of Net Cost and Statement of Changes in Net Position are prepared using the accrual basis of accounting. Accordingly, revenues are recognized when earned and expenses are recognized when incurred without regard to the receipt or payment of cash. These principles differ from budgetary accounting and reporting principles on

which the Statement of Budgetary Resources is prepared. The differences relate primarily to the capitalization and depreciation of property and equipment, as well as the recognition of other long-term assets and liabilities. The Statement of Custodial Activity is presented on the modified cash basis of accounting. Cash collections and amounts transferred to Treasury or the Investor Protection Fund are reported on a cash basis. The change in receivables and related payables are reported on an accrual basis.

The SEC presents net cost of operations by program. OMB Circular A-136 defines the term “major program” as describing an agency’s mission, strategic goals, functions, activities, services, projects, processes, or any other meaningful grouping. The presentation by program is consistent with the presentation used by the agency in submitting its budget requests.

Certain FY 2010 balances in the footnotes to the financial statements have been reclassified to conform to FY 2011 presentations.

### C. Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities. These estimates and assumptions include, but are not limited to, the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Estimates are also used in the allocation of costs to the SEC programs presented in the Statement of Net Cost. Actual results may differ from those estimates.

### D. Intra- and Inter-Agency Relationships

The SEC is comprised of a single Federal agency with limited intra-entity transactions. The Investor Protection Fund, which was created in FY 2010, finances the operations of the SEC Office of the Inspector General’s employee suggestion program on a reimbursable basis. This has given rise to a small amount of intra-entity eliminations of the related revenue and expense transactions between the Investor Protection Fund and the SEC’s General Salaries and Expenses Fund.

## E. Fund Accounting Structure

The SEC, in common with other Federal agencies, utilizes various Treasury Appropriation Fund Symbols (Funds), to recognize and track appropriation authority provided by Congress, collections from the public and other financial activity. These funds are described below:

- (1) **General Funds – Salaries and Expenses:** Earned revenues from securities transaction fees from SROs and securities registration, tender offer, merger, and other fees from registrants are deposited into Fund X0100, *Salaries and Expenses, Securities and Exchange Commission*. These collections are earmarked for carrying out the SEC’s mission, functions, and day to day operations and may be used in accordance with spending limits established by Congress. Collections in excess of Congressional spending limits are unavailable by law and reported as Non-Budgetary Fund Balance with Treasury (See Note 3. *Fund Balance with Treasury*). In this context, “earmarked” indicates that these collections are set aside by Congress for the purpose stated. In addition, the SEC received a supplemental appropriation of \$10 million for use in FY 2009 and FY 2010.
- (2) **Deposit Funds:** The Deposit Funds hold disgorgement, penalties, and interest collected and held on behalf of harmed investors, registrant monies held temporarily until earned by the SEC, and collections awaiting disposition or reclassification. This activity is recognized in Fund X6561, *Unearned Fees, Securities and Exchange Commission* and Fund X6563, *Disgorgement and Penalty Amounts Held for Investors, Securities and Exchange Commission*.
- (3) **Miscellaneous Receipt Accounts:** The Miscellaneous Receipt Accounts hold non-entity receipts and accounts receivable from custodial activities that the SEC cannot deposit into funds under its control. These accounts include receipts pursuant to certain SEC enforcement actions and other small collections that will be sent to the U.S. Treasury General Fund upon collection. This activity is recognized in Fund 1060, *Forfeitures of Unclaimed Money and Property*, Fund 1099, *Fines, Penalties, and Forfeitures, Not Otherwise Classified*, Fund 1435, *General Fund Proprietary Interest, Not*

*Otherwise Classified*, and Fund 3220, *General Fund Proprietary Receipts, Not Otherwise Classified*.

**(4) Investor Protection Fund:** The Investor Protection Fund is an earmarked fund that provides dedicated funding for the whistleblower awards as required by the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act). Persons may receive award payments from the Fund if they provide original information to the SEC that results in a successful enforcement action and other conditions are met. In addition, the Fund is used to finance the operations of the SEC Office of the Inspector General's employee suggestion program for the receipt of suggestions for improvements in work efficiency and effectiveness, and allegations of misconduct or mismanagement within the SEC. This activity is recognized in Fund X5567, *Monetary Sanctions and Interest, Investor Protection Fund, Securities and Exchange Commission (Investor Protection Fund)*.

**(5) Reserve Fund:** Effective October 1, 2011, a portion of SEC registration fee collections up to \$50 million in any one fiscal year may be deposited in the Reserve Fund, the balance of which cannot exceed \$100 million. The Reserve Fund may be used by the SEC to obligate amounts up to a total of \$100 million in one fiscal year as the SEC determines necessary to carry out its functions. The SEC must notify Congress after obligating amounts from the Reserve Fund. The SEC established the Fund in FY 2011 in anticipation of beginning Reserve Fund operations in FY 2012.

The SEC's lending and borrowing authority is limited to authority to borrow funds from Treasury and loan funds to SIPC, as discussed in *Note 10. Commitments and Contingencies*. The SEC has custodial responsibilities, as disclosed in *Note 1.M. Liabilities*.

## F. Earmarked Funds

Earmarked funds are financed by specifically identified revenues, often supplemented by other financing sources, which remain available over time. The SEC collects earmarked funds and is required to use these funds for designated activities, benefits or purposes and to account for

them separately from the Government's general revenues. The SEC's earmarked funds include securities transaction fees from SROs and securities registration, tender offer, merger, and other fees from registrants. These are reported as offsetting collections as defined by OMB and are deposited into Fund X0100, *Salaries and Expenses*. Also, all funds held in the Fund X5567, *Investor Protection Fund*, are considered earmarked as described in *Note 11. Earmarked, Other Entity, Disbursement and Penalties, and Other Non-Entity Funds*.

## G. Entity and Non-Entity Assets

Entity assets are assets that the SEC may use in its operations. This includes amounts where SEC management has the authority to decide how funds will be used as well as other amounts that the SEC is legally obligated to use to meet program obligations.

Assets that an agency holds on behalf of another Federal agency or a third party and are not available for the agency's use are non-entity assets. The SEC's non-entity assets include the following: (i) disgorgement, penalties, and interest collected and held or invested by the SEC; (ii) disgorgement, penalties, and interest receivable; (iii) accounts receivable with respect to Freedom of Information Act (FOIA) fees; and (iv) excess filing fees remitted by registrants (registrant deposits).

## H. Fund Balance with Treasury

Fund Balance with Treasury (FBWT) reflects amounts the SEC holds in the U.S. Treasury that have not been invested in Federal securities. The SEC's FBWT consist of several components.

- (1) The aggregate amount of funds in the SEC's general fund accounts with Treasury that the SEC is authorized to use to make expenditures and pay liabilities;
- (2) Filing and securities transaction fees in excess of appropriated amounts;
- (3) Funds held in the Investor Protection Fund;
- (4) Registrant deposits held pending submission of a filing or return to the registrant; and
- (5) Disgorgement funds held on behalf of harmed investors

The SEC conducts all of its banking activity in accordance with directives issued by Treasury's Financial Management Service.

## I. Investments

The SEC has the authority to invest disgorgement funds in Treasury securities including civil penalties collected under the "Fair Fund" provision of the Sarbanes-Oxley Act of 2002. As the funds are collected, the SEC holds them in a deposit fund account and may invest them in overnight and short-term market-based Treasury bills through the Bureau of the Public Debt. The SEC adds interest earned to the funds, and these funds are subject to taxation under Treasury Regulation Section 1.468B-2.

The SEC also has authority to invest amounts in the Investor Protection Fund in overnight and short-term market-based Treasury bills through the Bureau of the Public Debt. The interest earned on the investments is a component of the balance of the Fund and available to be used for expenses of the Investor Protection Fund.

Additional details regarding SEC investments are provided in *Note 5. Investments, Net*.

### ***Intragovernmental Investments in Treasury Securities***

Market-based Treasury securities are debt securities that the U.S. Treasury issues to Federal entities without statutorily determined interest rates. Although the securities are not marketable, the terms (prices and interest rates) mirror the terms of marketable Treasury securities.

The Federal Government does not set aside assets to pay future benefits or other expenditures associated with the investment by Federal agencies in non-marketable Federal securities. The balances underlying these investments are deposited in the U.S. Treasury, which uses the cash for general Government purposes. Treasury securities are issued to the SEC as evidence of these balances. Treasury securities are an asset of the SEC and a liability of the U.S. Treasury. Because the SEC and the U.S. Treasury are both components of the Government, these assets and liabilities offset each other from the standpoint of the Government as a whole.

For this reason, the investments presented by the SEC do not represent an asset or a liability in the U.S. Government-wide financial statements.

Treasury securities provide the SEC with authority to draw upon the U.S. Treasury to make future payments from these accounts. When the SEC requires redemption of these securities to make expenditures, the Government finances those expenditures out of accumulated cash balances, by raising taxes or other receipts, by borrowing from the public or repaying less debt, or by curtailing other expenditures. This is the same manner in which the Government finances all expenditures.

## J. Accounts Receivable and Allowance for Uncollectible Accounts

SEC's entity and non-entity accounts receivable consist primarily of amounts due from the public. Entity accounts receivable are amounts that the SEC may retain upon collection. Non-entity accounts receivable are amounts that the SEC will forward to another Federal agency or to the public upon collection.

### ***Entity Accounts Receivable***

The bulk of SEC entity accounts receivable arise from securities transaction fees and from filing fees paid by registrants. In addition, the SEC has small amounts of activity arising from the sale of goods or services provided by the SEC to other Federal agencies; reimbursement of employee travel by outside organizations; and employee-related debt. Entity accounts receivable balances are normally small at year end due to the timing and payment requirements relative to the largest categories of accounts receivable activity. Specifically, Federal law generally requires payment of filing fees at the time of filing, and securities transaction fees are payable to the SEC twice a year: in March for the period September through December, and in September for the period January through August. Accordingly, the year-end accounts receivable accrual generally represents fees payable to the SEC for one month of securities transaction fee activity (September). At the end of the first, second and third quarters, the receivable reflects four months, three months, and six months of securities transaction fee activity, respectively.

### ***Non-entity Accounts Receivable***

Non-entity accounts receivable arise mainly from amounts assessed against violators of securities laws, including disgorgement of illegal gains, civil penalties, and related assessed interest. The SEC is responsible for collection, and recognizes a receivable, when an order of the Commission or a Federal court directs payment to the SEC or the U.S. Treasury.

Interest recognized by the SEC on non-entity accounts receivable includes prejudgment interest specified by the court or administrative order as well as post-judgment interest on collectible accounts. The SEC does not recognize interest revenue on accounts considered to be uncollectible.

The SEC is also party to court orders directing violators of Federal securities laws to pay amounts assessed to a Federal court or to a non-Federal receiver acting on behalf of harmed investors. These orders are not recognized as accounts receivable by the SEC because the debts are payable to, and collected by, another party.

### ***Allowance for Uncollectible Amounts***

The SEC calculates the allowance for uncollectible amounts and the related provision for estimated losses for filing fees and other accounts receivable using an analysis of historical collection data. No allowance for uncollectible amounts or related provision for estimated losses has been established for securities transaction fees payable by SROs, as these amounts are fully receivable based on historical experience.

The SEC uses a three-tiered methodology to calculate the allowance for loss on its non-entity disgorgement and penalty accounts receivable balances. The first tier involves making an individual collection assessment of the cases constituting the top 90 percent of the value of the disgorgement and penalty accounts receivable portfolio. The second and third tiers are composed of cases in the bottom 10 percent of the value. Separate calculations are performed on accounts that are equal to or less than 30 days old and accounts that are over 30 days old using an allowance rate based on historical collection data.

The SEC writes off receivables aged two or more years by removing the debt amounts from the gross accounts receivable and any related allowance for uncollectible accounts.

## **K. Other Assets**

### ***Advances and Prepayments***

Payments made in advance of the receipt of goods and services are recorded as advances or prepayments, and recognized as expenses when the related goods and services are received.

## **L. Property and Equipment, Net**

The SEC's property and equipment consists of software, general-purpose equipment used by the agency, capital improvements made to buildings leased by the SEC for office space, and, when applicable, internal-use software development costs for projects in development. The SEC reports property and equipment purchases and additions at historical cost. The agency expenses property and equipment acquisitions that do not meet the capitalization criteria as well as normal repairs and maintenance.

The SEC depreciates property and equipment over the estimated useful lives using the straight-line method of depreciation. The agency removes property and equipment from its asset accounts in the period of disposal, retirement, or removal from service. The SEC recognizes the difference between the book value and the proceeds as a gain or loss in the period that the asset is removed.

## **M. Liabilities**

The SEC recognizes liabilities for probable future outflows or other sacrifices of resources as a result of events that have occurred as of the Balance Sheet date. The SEC's liabilities consist of routine operating accounts payable, accrued payroll and benefits, registrant deposit accounts that have not been returned to registrants, liabilities for disgorgement and penalties, legal liabilities, and custodial liabilities for amounts collected or receivable on behalf of Treasury.

### ***Enforcement Related Liabilities***

A liability for disgorgement and penalties arises when an order is issued for the SEC to collect disgorgement, penalties, and interest from securities law violators. When the Commission or court issues such an order, the SEC establishes an accounts receivable due to the SEC offset by a liability. The presentation

of this liability on the Balance Sheet is dependent upon several factors. If the court or Commission order indicates that collections are to be retained by the Federal Government, either by transfer to the U.S. Treasury General Fund or to the Investor Protection Fund, the liabilities are classified as custodial (that is, collected on behalf of the Government) and intra-governmental. If the order indicates that the funds are eligible for distribution to harmed investors, the SEC will recognize a Governmental liability (that is, a liability of the Government to make a payment to the public). This liability is not presented as a custodial liability. The SEC does not record liabilities on its financial statements for disgorgement and penalty amounts that another government entity such as a court, or a non-governmental entity, such as a receiver, has collected or will collect.

Prior to the enactment of the Dodd-Frank Act on July 21, 2010, all collections not distributed to harmed investors were transferred to the U.S. Treasury General Fund. After the enactment of the Dodd-Frank Act, collections not distributed to harmed investors may be transferred to either the Investor Protection Fund or the U.S. Treasury General Fund. Collections not distributed to harmed investors are transferred to the Investor Protection Fund if the Fund's balance does not exceed \$300 million at the time of collection.

### ***Liability Classification***

The SEC recognizes liabilities covered by three types of resources: realized budgetary resources, unrealized budgetary resources that become available without further congressional action, and amounts that do not require the use of current budgetary resources. Realized budgetary resources include obligated balances that fund existing liabilities and unobligated balances as of the relevant Balance Sheet dates. Unrealized budgetary resources represent fee collections in excess of amounts appropriated for current fiscal year spending. The SEC uses these resources to cover liabilities when appropriation language makes these unrealized budgetary resources available in the fiscal year without further congressional action. Amounts that do not require the use of current budgetary resources are liabilities that will be funded in future years, such as annual leave.

## **N. Employee Retirement Systems and Benefits**

The SEC's employees may participate in either the Civil Service Retirement System (CSRS) or the Federal Employees Retirement System (FERS), depending on when they started working for the Federal Government. Pursuant to Public Law 99-335, FERS and Social Security automatically cover most employees hired after December 31, 1983. Employees who are rehired after a break in service of more than one year and who had five years of Federal civilian service prior to 1987 are eligible to participate in the CSRS offset retirement system or may elect to join FERS.

All employees are eligible to contribute to a Thrift Savings Plan (TSP). For those employees participating in FERS, the TSP is automatically established, and the SEC makes a mandatory one percent contribution to this plan. In addition, the SEC matches contributions ranging from one to four percent for FERS-eligible employees who contribute to their TSP. The SEC contributes a matching amount to the Social Security Administration under the Federal Insurance Contributions Act, which fully covers FERS participating employees. Employees participating in CSRS do not receive matching contributions to their TSP.

The SEC does not report CSRS, FERS, Federal Employees Health Benefits Program (FEHBP), Federal Employees Group Life Insurance Program (FEGLIP) assets, accumulated plan benefits, or unfunded liabilities applicable to its employees; the U.S. Office of Personnel Management (OPM) reports this information.

## **O. Injury and Post-employment Compensation**

The Federal Employees' Compensation Act (FECA), administered by the U.S. Department of Labor (DOL), provides income and medical cost protection to covered Federal civilian employees harmed on the job or who have contracted an occupational disease, and dependents of employees whose death is attributable to a job-related injury or occupational disease. The DOL bills the SEC annually as claims are paid, and the SEC in turn accrues a liability to recognize the future payments. Payment on these bills is deferred for two years to allow for funding through the budget process. Similarly, employees that the SEC terminates without cause may receive unemployment compensation benefits under the

unemployment insurance program also administered by the DOL, which bills each agency quarterly for paid claims.

In addition, the SEC records an estimate for the FECA actuarial liability using the DOL's FECA model. The model considers the average amount of benefit payments incurred by the SEC for the past three fiscal years, multiplied by the medical and compensation liability to benefits paid (LBP) ratio for the whole FECA program.

## P. Annual, Sick, and Other Leave

The SEC accrues annual leave and compensatory time as earned and reduces the accrual when leave is taken. The balances in the accrued leave accounts reflect current leave balances and pay rates. No portion of this liability has been obligated. Future financing sources provide funding to the extent that current or prior year funding is not available to pay for leave earned but not taken. The SEC expenses sick leave and other types of non-vested leave as used.

## Q. Revenue and Other Financing Sources

The SEC's revenue and financing sources include exchange revenues, which are generated from arm's-length transactions in which both parties give and receive value, and non-exchange revenues, which arise from the Government's ability to demand payment.

### Exchange Revenue

The SEC's exchange revenue consists primarily of collections of securities transaction fees from SROs and of securities registration, tender offer, merger, and other fees from registrants. The fee rates are calculated by the SEC's Division of Risk, Strategy, and Financial Innovation and established by the SEC in accordance with Federal law and are applied to volumes of activity reported by SROs or to filings submitted by registrants. Fees are recognized as exchange revenue on the effective date of transaction or filing. These fee collections are the primary source of SEC funding and may be used up to limits established by Congress. See *Note 1.E. Fund Accounting Structure*.

The SEC recognizes amounts remitted by registrants in advance of the transaction or filing date as a liability until earned by the SEC or returned to the registrant. Federal

regulation requires the return of registrant deposits when an account is dormant for three years.

### Filing Fee Offsets

The Securities Act of 1933 and the Exchange Act do not permit refunds to registrants for securities that remain unsold after the completion, termination, or withdrawal of an offering. However, Code of Federal Regulations (CFR) Title 17 Chapter II, Part 230, Section 457(p) permits filers to offset a fee paid (filing fee offset) for a subsequent registration statement (offering) filed within five years of the initial filing date of the earlier registration statement. The total aggregate dollar amount of the filing fee associated with the unsold securities may be offset against the total filing fee due on the subsequent offering. Unused filing fee offsets are not a liability to the SEC because registrants cannot obtain refunds of fees or additional services in relation to securities that remain unsold. However, filing fee offsets may reduce revenue earned in future accounting periods.

### Non-exchange Revenue

The SEC's non-exchange revenue mainly consists of amounts collected from violators of securities laws as a result of enforcement proceedings. These amounts may take the form of disgorgement of illegal gains, civil penalties, and related interest. Amounts collected may be paid to injured investors, transferred to the Investor Protection Fund, or transferred to the U.S. Treasury General Fund, based on established policy and regulation.

All non-exchange revenue expected to be forwarded to either the U.S. Treasury General Fund or Investor Protection Fund is recognized on the Statement of Custodial Activity. The Investor Protection Fund recognizes non-exchange revenue on the Statement of Changes in Net Position when funds are transferred into the Investor Protection Fund. The result is that, in accordance with Federal accounting standards, the entire amount of custodial activity is presented on the Statement of Custodial Activity to document the movement of funds and the portion retained by the SEC is also recognized as SEC activity.

The SEC does not recognize amounts collected and held by another government entity, such as a court registry, or a non-government entity, such as a receiver.

## R. Budgets and Budgetary Accounting

The SEC is subject to certain restrictions on its use of statutory fees. The SEC deposits all fee revenues in a designated account at Treasury. However, the SEC may use funds from this account only as authorized by Congress and made available by OMB apportionment, upon issuance of a Treasury warrant. Revenue collected in excess of appropriated amounts is restricted from use by the SEC.

The SEC can use fees other than the restricted excess fees from its operations, subject to annual congressional limitations, which were \$1,185 million and \$1,095 million for the budgets for FY 2011 and FY 2010, respectively. In addition, the SEC had available approximately \$36.1 million and \$16.1 million from prior year balances for FY 2011 and FY 2010, respectively. Funds appropriated that the SEC does not use in a given fiscal year are maintained in a designated account for use in future periods in accordance with the appropriation requirements. As previously mentioned in *Note 1.E. Fund Accounting Structure*, the SEC received a supplemental appropriation for \$10 million from the U.S. Treasury General Fund for use in FY 2009 and FY 2010. Unlike the annual appropriation, the supplemental funds are not offset by fees collected by the SEC.

### General Funds – Salaries and Expenses

Each fiscal year, the SEC receives Category A apportionments, which are quarterly distributions of budgetary resources made by OMB. The SEC also receives a small amount of Category B funds for reimbursable activity, which are exempt from quarterly apportionment.

### Investor Protection Fund

The Investor Protection Fund is a special fund that has the authority to retain revenues and other financing sources not used in the current period for future use. The Dodd-Frank Act provides that the Fund is available to the SEC without further appropriation or fiscal year limitation for the purpose of paying awards to whistleblowers and funding the activities of the Office of the Inspector General's employee suggestion program. However, the SEC is required to request

and obtain an annual apportionment from OMB to use these funds. All of the funds are Category B, exempt from quarterly apportionment.

## S. Disgorgement and Penalties

The SEC maintains non-entity assets related to disgorgements and penalties ordered pursuant to civil injunctive and administrative proceedings. The SEC also recognizes an equal and offsetting liability for these assets as discussed in *Note 1.M. Liabilities*. These non-entity assets consist of disgorgement, penalties, and interest assessed against securities law violators where the Commission, administrative law judge, or in some cases, a court, has determined that the SEC should return such funds to harmed investors or may be transferred to the Investor Protection Fund or the U.S. Treasury General Fund. The SEC does not record on its financial statements any asset amounts that another government entity such as a court, or a non-governmental entity, such as a receiver, has collected or will collect. Additional details regarding disgorgement and penalties are presented in *Note 11. Earmarked, Other Entity, Disgorgement and Penalties, and Other Non-Entity Funds* and *Note 16. Disgorgement and Penalties*.

## T. Investor Protection Fund

The Investor Protection Fund was established through a permanent indefinite appropriation to provide financing for payments to whistleblowers and for the SEC Office of the Inspector General's employee suggestion program. The Investor Protection Fund is financed by transferring a portion of monetary sanctions collected by the SEC in judicial or administrative actions brought by the SEC under the securities laws that are not added to disgorgement fund or other funds intended for harmed investors under Section 308 of the Sarbanes-Oxley Act of 2002 (15 U.S.C. 7246). Sanctions collected by the Commission payable either to the SEC or the U.S. Treasury General Fund will be transferred to the Investor Protection Fund if the balance in that fund is less than \$300 million on the day of collection.

The SEC may request the Secretary of the Treasury to invest Investor Protection Fund amounts in Treasury obligations. Refer to *Note 1.I. Investments* for additional details.

## NOTE 2. Assets

At September 30, 2011, SEC assets consisted of the following:

<i>(DOLLARS IN THOUSANDS)</i>	Entity	Non-Entity	Total
<b>Intragovernmental:</b>			
Fund Balance with Treasury:			
SEC Funds	\$ 6,875,059	\$ —	\$ 6,875,059
Registrant Deposits	—	46,622	46,622
Disgorgement and Penalties (Note 16)	—	73,929	73,929
Investments, Net:			
Disgorgement and Penalties (Note 16)	—	749,810	749,810
Investor Protection Fund	452,715	—	452,715
Accounts Receivable	20	—	20
Advances and Prepayments	7,172	—	7,172
<b>Total Intragovernmental Assets</b>	<b>7,334,966</b>	<b>870,361</b>	<b>8,205,327</b>
Cash and Other Monetary Assets:			
Disgorgement and Penalties (Note 16)	—	—	—
Accounts Receivable, Net:			
SEC Funds	122,910	—	122,910
Disgorgement and Penalties (Note 16)	—	90,982	90,982
Other Non-Entity Assets	—	134	134
Advances and Prepayments	3,656	—	3,656
Property and Equipment, Net (Note 7)	93,939	—	93,939
<b>Total Assets (Note 11)</b>	<b>\$ 7,555,471</b>	<b>\$ 961,477</b>	<b>\$ 8,516,948</b>

At September 30, 2010, SEC assets consisted of the following:

<i>(DOLLARS IN THOUSANDS)</i>	Entity	Non-Entity	Total
<b>Intragovernmental:</b>			
Fund Balance with Treasury:			
SEC Funds	\$ 6,890,369	\$ —	\$ 6,890,369
Registrant Deposits	—	44,729	44,729
Disgorgement and Penalties (Note 16)	—	54,269	54,269
Investments, Net:			
Disgorgement and Penalties (Note 16)	—	924,823	924,823
Investor Protection Fund	—	—	—
Accounts Receivable	—	—	—
Advances and Prepayments	2,198	—	2,198
<b>Total Intragovernmental Assets</b>	<b>6,892,567</b>	<b>1,023,821</b>	<b>7,916,388</b>
Cash and Other Monetary Assets:			
Disgorgement and Penalties (Note 16)	—	2,815	2,815
Accounts Receivable, Net:			
SEC Funds	79,200	—	79,200
Disgorgement and Penalties (Note 16)	—	81,939	81,939
Other Non-Entity Assets	—	4	4
Advances and Prepayments	2,381	—	2,381
Property and Equipment, Net (Note 7)	79,712	—	79,712
<b>Total Assets (Note 11)</b>	<b>\$ 7,053,860</b>	<b>\$ 1,108,579</b>	<b>\$ 8,162,439</b>

### NOTE 3. Fund Balance with Treasury

The Fund Balance with Treasury by type of fund and Status of Fund Balance with Treasury as of September 30, 2011 and 2010 consists of the following:

<i>(DOLLARS IN THOUSANDS)</i>	FY 2011	FY 2010
<b>Fund Balances:</b>		
General Funds	\$ 6,874,986	\$ 6,438,459
Special Fund – Investor Protection Fund	73	451,910
Other Funds	120,551	98,998
<b>Total Fund Balance with Treasury</b>	<b>\$ 6,995,610</b>	<b>\$ 6,989,367</b>
<b>Status of Fund Balance with Treasury:</b>		
Unobligated Balance:		
Available	\$ 8,323	\$ 17,213
Unavailable	38,751	472,136
Obligated Balance not Yet Disbursed	332,707	317,747
Non-Budgetary Fund Balance with Treasury	6,615,829	6,182,271
<b>Total Fund Balance with Treasury</b>	<b>\$ 6,995,610</b>	<b>\$ 6,989,367</b>

The Special Fund consists of the Investor Protection Fund established in FY 2010. This Special Fund provides the financial resources for the whistleblower award program and the SEC Office of Inspector General's employee suggestion program, both of which were mandated in the Dodd-Frank Act.

Other Funds consist of Fund Balance with Treasury held in deposit funds.

Obligated and unobligated balances reported for the status of Fund Balance with Treasury differ from the amounts reported in the Statement of Budgetary Resources due to the fact that budgetary balances are supported by amounts other than Fund Balance with Treasury. These amounts include Investor Protection Fund investments, uncollected payments from Federal sources, and the impact of the change in legal interpretation for leases.

Non-Budgetary Fund Balance with Treasury is comprised of amounts in deposit funds and offsetting collections temporarily precluded from obligation in SEC's General Salaries and Expenses Fund (X0100). Amounts temporarily precluded from obligation represent offsetting collections for filing and securities transaction fees in excess of appropriated amounts.

There were no significant differences between the Fund Balance reflected in SEC financial statements and the balance in the Treasury accounts.

### NOTE 4. Cash and Other Monetary Assets

The SEC did not have a Cash balance as of September 30, 2011. The SEC receives disgorgement and penalties collections throughout the year. Any collections received after the Treasury Department cut-off for deposit of checks are treated as deposits in transit and recognized as Cash on the Balance Sheet. The SEC had a Cash balance of \$2.8 million as of September 30, 2010.

## NOTE 5. Investments, Net

The SEC invests funds in overnight and short-term non-marketable market-based Treasury bills. The SEC records the value of its investments in Treasury bills at cost and amortizes any premium or discount on a straight-line basis (S/L) through the maturity date of these securities. Non-marketable market-based Treasury securities are issued by the Bureau of Public Debt to Federal agencies. They are not traded on any securities exchange but mirror the prices of similar Treasury securities trading in the Government securities market.

At September 30, 2011, investments consisted of the following:

<i>(DOLLARS IN THOUSANDS)</i>	Cost	Amortization Method	Amortized (Premium) Discount	Interest Receivable	Investment, Net	Market Value Disclosure
Non-Marketable Market-Based Securities						
Disgorgement and Penalties	\$ 749,705	S/L	\$ 105	\$ —	\$ 749,810	\$ 749,848
Investor Protection Fund – Entity	453,799	S/L	(2,314)	1,230	452,715	451,696
<b>Total</b>	<b>\$ 1,203,504</b>		<b>\$ (2,209)</b>	<b>\$ 1,230</b>	<b>\$ 1,202,525</b>	<b>\$ 1,201,544</b>

At September 30, 2010, investments consisted of the following:

<i>(DOLLARS IN THOUSANDS)</i>	Cost	Amortization Method	Amortized (Premium) Discount	Interest Receivable	Investment, Net	Market Value Disclosure
Non-Marketable Market-Based Securities						
Disgorgement and Penalties	\$ 924,651	S/L	\$ 171	\$ 1	\$ 924,823	\$ 924,837
Investor Protection Fund – Entity	—	S/L	—	—	—	—
<b>Total</b>	<b>\$ 924,651</b>		<b>\$ 171</b>	<b>\$ 1</b>	<b>\$ 924,823</b>	<b>\$ 924,837</b>

## NOTE 6. Accounts Receivable, Net

At September 30, 2011, accounts receivable consisted of the following:

<i>(DOLLARS IN THOUSANDS)</i>	Gross Receivables	Allowance	Net Receivables
Intragovernmental Entity Accounts Receivable:			
Reimbursable Activity	\$ 20	\$ —	\$ 20
Subtotal Intragovernmental Accounts Receivable	20	—	20
Entity Accounts Receivable:			
Securities Transaction Fees	121,798	—	121,798
Filing Fees	893	109	784
Other	375	47	328
Non-Entity Accounts Receivable:			
Disgorgement and Penalties (Note 16)	952,711	861,729	90,982
Other	1,329	1,195	134
Subtotal Non-Intragovernmental Accounts Receivable	1,077,106	863,080	214,026
<b>Total Accounts Receivable</b>	<b>\$ 1,077,126</b>	<b>\$ 863,080</b>	<b>\$ 214,046</b>

At September 30, 2010, accounts receivable consisted of the following:

<i>(DOLLARS IN THOUSANDS)</i>	Gross Receivables	Allowance	Net Receivables
Intragovernmental Entity Accounts Receivable:			
Reimbursable Activity	\$ —	\$ —	\$ —
Subtotal Intragovernmental Accounts Receivable	—	—	—
Entity Accounts Receivable:			
Securities Transaction Fees	78,461	—	78,461
Filing Fees	690	107	583
Other	180	24	156
Non-Entity Accounts Receivable:			
Disgorgement and Penalties (Note 16)	656,495	574,556	81,939
Other	9	5	4
Subtotal Non-Intragovernmental Accounts Receivable	735,835	574,692	161,143
Total Accounts Receivable	\$ 735,835	\$ 574,692	\$ 161,143

Refer to Note 1.J. *Accounts Receivable and Allowance for Uncollectible Accounts* for methods used to estimate allowances. The SEC estimates that accrued interest (compounded and simple) on uncollectible disgorgement and penalty related accounts receivable to be \$138 million as of September 30, 2011. This estimate does not include interest accruable on debts referred to Treasury for collection.

As of September 30, 2011 and 2010, the balances include disgorgement and penalty accounts receivables, net of allowance, of \$51.7 million and \$42.4 million, respectively designated as payable to the U.S. Treasury General Fund per court order. As discussed in Note 1.M. *Liabilities*, these receivables, their offsetting liabilities, and the associated revenues, are classified as custodial.

## NOTE 7. Property and Equipment, Net

At September 30, 2011, property and equipment consisted of the following:

<b>Class of Property</b> <i>(DOLLARS IN THOUSANDS)</i>	Depreciation/ Amortization Method	Capitalization Threshold for Individual Purchases	Capitalization Threshold for Bulk Purchases	Service Life (Years)	Acquisition Cost	Accumulated Depreciation/ Amortization	Book Value
Furniture and Equipment	S/L	\$ 15	\$ 50	3-5	\$ 81,626	\$ 47,455	\$ 34,171
Software	S/L	300	300	3-5	97,139	80,392	16,747
Leasehold Improvements	S/L	300	N/A	10	90,993	47,972	43,021
Total					\$ 269,758	\$ 175,819	\$ 93,939

At September 30, 2010, property and equipment consisted of the following:

<b>Class of Property</b> <i>(DOLLARS IN THOUSANDS)</i>	Depreciation/ Amortization Method	Capitalization Threshold for Individual Purchases	Capitalization Threshold for Bulk Purchases	Service Life (Years)	Acquisition Cost	Accumulated Depreciation/ Amortization	Book Value
Furniture and Equipment	S/L	\$ 15	\$ 50	3-5	\$ 61,133	\$ 42,754	\$ 18,379
Software	S/L	300	300	3-5	89,827	73,305	16,522
Leasehold Improvements	S/L	300	N/A	10	84,204	39,393	44,811
Total					\$ 235,164	\$ 155,452	\$ 79,712

## NOTE 8. Liabilities

The SEC's liabilities include amounts that will not require the use of budgetary resources. These liabilities include registrant deposit accounts that have not been returned to registrants and the offsetting liability that corresponds to assets the SEC holds relating to collections from disgorgements and penalties and receivables as discussed in *Note 1.M. Liabilities*.

At September 30, 2011, liabilities consisted of the following:

<i>(DOLLARS IN THOUSANDS)</i>	<b>Liabilities Covered by Budgetary Resources</b>	<b>Liabilities Not Covered by Budgetary Resources</b>	<b>Liabilities Not Requiring Budgetary Resources</b>	<b>Total</b>
Intragovernmental:				
Accounts Payable	\$ 8,049	\$ —	\$ —	\$ 8,049
Other Intragovernmental Liabilities				
Accrued Employee Benefits	2,877	—	—	2,877
Unfunded FECA and Unemployment Liability	—	1,770	—	1,770
Custodial Liability	—	—	51,745	51,745
Liability for Non-Entity Assets	—	—	134	134
Subtotal – Other Intragovernmental Liabilities	2,877	1,770	51,879	56,526
Total Intragovernmental	10,926	1,770	51,879	64,575
Accounts Payable	52,768	—	—	52,768
Actuarial FECA Liability	—	7,805	—	7,805
Other Liabilities				
Accrued Payroll and Benefits	18,395	—	—	18,395
Accrued Leave	—	45,472	—	45,472
Registrant Deposits	—	—	46,622	46,622
Liability for Disgorgement and Penalties (Note 16)	—	—	862,976	862,976
Other Accrued Liabilities				
Legal Liability	—	956	—	956
Recognition of Lease Liability (Note 9)	—	6,256	—	6,256
Other	—	—	—	—
Subtotal – Other Liabilities	18,395	52,684	909,598	980,677
Total Liabilities (Note 11)	\$ 82,089	\$ 62,259	\$ 961,477	\$ 1,105,825

Other Liabilities totaled \$1,037 million as of September 30, 2011 and is comprised of current and non-current liabilities totaling \$986 million and \$51 million, respectively. The non-current portion of Other Liabilities includes the appropriate portions of the Unfunded FECA and Unemployment Liability, Accrued Leave, and Lease Liability. Current liabilities not covered by budgetary resources totaled \$3.6 million as of September 30, 2011.

At September 30, 2010, liabilities consisted of the following:

<i>(DOLLARS IN THOUSANDS)</i>	<b>Liabilities Covered by Budgetary Resources</b>	<b>Liabilities Not Covered by Budgetary Resources</b>	<b>Liabilities Not Requiring Budgetary Resources</b>	<b>Total</b>
Intragovernmental:				
Accounts Payable	\$ 5,185	\$ —	\$ —	\$ 5,185
Other Intragovernmental Liabilities				
Accrued Employee Benefits	6,088	—	—	6,088
Unfunded FECA and Unemployment Liability	—	1,719	—	1,719
Custodial Liability	—	—	42,380	42,380
Liability for Non-Entity Assets	—	—	4	4
Subtotal – Other Intragovernmental Liabilities	6,088	1,719	42,384	50,191
Total Intragovernmental	11,273	1,719	42,384	55,376
Accounts Payable	46,260	—	—	46,260
Actuarial FECA Liability	—	7,576	—	7,576
Other Liabilities				
Accrued Payroll and Benefits	31,649	—	—	31,649
Accrued Leave	—	45,629	—	45,629
Registrant Deposits	—	—	44,729	44,729
Liability for Disgorgement and Penalties (Note 16)	—	—	1,021,466	1,021,466
Other Accrued Liabilities				
Legal Liability	—	10,823	—	10,823
Recognition of Lease Liability (Note 9)	—	9,202	—	9,202
Other	9,245	—	—	9,245
Subtotal – Other Liabilities	40,894	65,654	1,066,195	1,172,743
Total Liabilities (Note 11)	\$ 98,427	\$ 74,949	\$ 1,108,579	\$ 1,281,955

Other Liabilities totaled \$1,223 million as of September 30, 2010 and is comprised of current and non-current liabilities totaling \$1,170 million and \$53 million, respectively. The non-current portion of Other Liabilities includes the appropriate portions of the Unfunded FECA and Unemployment Liability, Accrued Leave, and Lease Liability. Current liabilities not covered by budgetary resources totaled \$14.4 million as of September 30, 2010.

The legal liability arose from an award ordered pursuant to case *SEC v. FLRA*, No. 08-1256, 08-1294 (D.C.Cir.). This matter involved a complaint filed by the National Treasury Employees Union (NTEU) before Federal Labor Relations Authority (FLRA). In FY 2010, the SEC developed a methodology for processing the ordered retroactive wage adjustments and began making payments in the fourth quarter of FY 2010. As of September 30, 2011, the remaining legal liability is estimated to be \$1 million.

## NOTE 9. Leases

### Operating Leases

At September 30, 2011, the SEC leased office space at 20 locations under operating lease agreements that expire between FY 2012 and FY 2027. The SEC paid \$99.6 million and \$93.3 million for rent for the fiscal years ending September 30, 2011 and 2010, respectively.

Under existing commitments, minimum lease payments through FY 2017 and thereafter are as follows:

Fiscal Year <i>(DOLLARS IN THOUSANDS)</i>	Minimum Lease Payments
2012	\$ 92,203
2013	95,907
2014	98,169
2015	94,462
2016	91,152
2017 and thereafter	369,849
<b>Total Future Minimum Lease Payments</b>	<b>\$ 841,742</b>

The total future minimum lease payments presented above include rented space through all optional lease periods.

### Continuing Liability

The total future minimum lease payments summarized above includes a continuing liability, until March 31, 2012, for space leased in New York. In FY 2005, to facilitate surrender of the SEC lease obligations for this space, the SEC and U.S. General Services Administration (GSA) entered into separate agreements with the lessor. Under these agreements (including renewals), GSA has agreed to rent the office space for a period of time extending past the end of the SEC's lease term (March 2012). The SEC was responsible for a difference of approximately \$18 million between its lease liability and the lease amount negotiated by GSA. As of September 30, 2011, the SEC is responsible for approximately \$1 million in payments for the space leased in New York. The amount will be paid in FY 2012 and is included in the total future minimum lease payments disclosed in the Operating Leases section above.

### Constitution Center Property

The total future minimum lease payments summarized above includes \$137.7 million for the Constitution Center property, for which a lease became effective on July 28, 2010. The lease was originally for 900,000 square feet of space. Subsequently, the landlord submitted a notification that 600,000 square feet had been assumed by two different third parties. Therefore, the minimum lease payments above reflect the SEC's obligation for the remaining 300,000 square feet. The SEC is also discussing with the General Services Administration (GSA) the possibility of transferring the remaining 300,000 square feet to GSA.

### Expense Recognition of "Rent Holiday"

In addition to the lease liability above, in FY 2005 the SEC moved into temporary office space in New York due to renovations in the new leased office space. This temporary space was provided to the SEC for only the lessor's operating costs. As a result, the SEC did not make rent payments for the New York office for five months of the fiscal year. The SEC allocated the \$8 million of rent expense foregone on a straight-line basis over the life of the new lease. Since 2006, the SEC has recorded a reduction in the unfunded lease liability in the amount of \$2.9 million and currently has a remaining balance of \$5.1 million. The yearly future amortization amounts are shown in the table below. Refer to Recognition of Lease Liability line in *Note 8. Liabilities*.

Fiscal Year <i>(DOLLARS IN THOUSANDS)</i>	Future Amortization Amounts
2012	\$ 533
2013	533
2014	533
2015	533
2016	533
2017 and thereafter	2,399
<b>Total Future Amortization Amounts</b>	<b>\$ 5,064</b>

## NOTE 10. Commitments and Contingencies

### A. Commitments: Securities Investor Protection Act

The Securities Investor Protection Act of 1970 (SIPA), as amended, created the Securities Investor Protection Corporation (SIPC) to restore funds and securities to investors and to protect the securities markets from disruption following the failure of broker-dealers. Generally, if a brokerage firm is not able to meet its obligations to customers, then customers' cash and securities held by the brokerage firm are returned to customers on a pro rata basis. If sufficient funds are not available at the firm to satisfy customer claims, the reserve funds of SIPC are used to supplement the distribution, up to a ceiling of \$500,000 per customer, including a maximum of \$250,000 for cash claims.

SIPA authorizes SIPC to create a fund to maintain all monies received and disbursed by SIPC. SIPA gives SIPC the authority to borrow up to \$2.5 billion from the SEC in the event that the SIPC Fund is or may appear insufficient for purposes of SIPA. To borrow the funds, SIPC must file with the SEC a statement of the uses of such a loan and a repayment plan, and then the SEC must certify to the Secretary of the Treasury that the loan is necessary to protect broker-dealer customers and maintain confidence in the securities markets and that the repayment plan provides as reasonable assurance of prompt repayment as may be feasible under the circumstances. The Treasury would make these funds available to the SEC through the purchase of notes or other obligating instruments issued by the SEC. Such notes or other obligating instruments would bear interest at a rate determined by the Secretary of the Treasury. As of September 30, 2011, the SEC had not loaned any funds to the SIPC, and there are no outstanding notes or other obligating instruments issued by the SEC.

Based on the estimated costs to complete ongoing customer protection proceedings, the current size of the SIPC Fund supplemented by SIPC's ongoing assessments on brokers is expected to provide sufficient funds to cover acknowledged customer claims. There are several broker-dealers that are being liquidated under SIPA or that have been referred to SIPC for liquidation that may result in additional customer claims. In the event that the SIPC Fund is or may reasonably appear to be insufficient for the purposes of SIPA, SIPC may seek a loan from the SEC.

### B. Commitments: Investor Protection Fund

As mentioned in *Note 1.E. Fund Accounting Structure*, the Investor Protection Fund will be used to pay awards to whistleblowers if they voluntarily provide original information to the SEC and meet other conditions. The legislation allows whistleblowers to receive between 10 and 30 percent of the monetary sanctions collected in the covered action or in a related action, with the actual percentage being determined at the discretion of the SEC using criteria provided in the legislation and the related rules to implement the legislation adopted by the SEC.

A contingent liability is recognized in instances where a positive Preliminary Determination has been made by the Claims Review Staff in the Office of the Whistleblower and the amount can be estimated. A Preliminary Determination is a first assessment, made by the Claims Review Staff, as to whether the claim should be allowed or denied and, if allowed, what the proposed award percentage amount should be. Liabilities are recognized in instances where a collection has been received and a positive Proposed Final Determination has been reached by the Claims Review Staff. However, the actual payment of the whistleblower award would not occur until after the Determination became final.

### C. Other Commitments

In addition to future lease commitments discussed in *Note 9. Leases*, the SEC is obligated for the purchase of goods and services that have been ordered, but not received. As of September 30, 2011, net obligations for all of the SEC's activities were \$1,110.6 million, of which \$82.1 million was delivered and unpaid. As of September 30, 2010, net obligations for all of SEC's activities were \$317.7 million, of which \$98.4 million was delivered and unpaid.

### D. Contingencies

The SEC recognizes contingent liabilities 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. The SEC is party to various routine administrative proceedings, legal actions, and claims brought against it, including threatened or pending litigation involving labor relations claims, some of which may ultimately result in settlements or decisions against the Federal Government. No such matters were probable and measurable at September 30, 2011.

## NOTE 11. Earmarked, Other Entity, Disgorgement and Penalties, and Other Non-Entity Funds

SEC's Earmarked funds consist of transactions and balances recorded in its Salaries and Expenses (X0100) and the Investor Protection (X5567) funds, see *Note 1.F. Earmarked Funds*. SEC's Other Entity Funds consist of amounts recorded in its supplemental appropriation which was available for use in FY 2009 and FY 2010; see *Note 1.E. Fund Accounting Structure*.

Amounts disclosed as Disgorgement and Penalties consist of non-entity custodial and Governmental liabilities and related assets stemming from SEC's actions to collect disgorgement, penalties, and investment interest; refer to *Note 1.M. Liabilities - Enforcement Related Liabilities*.

Other Non-Entity Funds mainly consist of liabilities and related assets stemming from excess filing fees (registrant deposits), FOIA fees, and post judgment interest; refer to *Note 1.G. Entity and Non-Entity Assets*.

For FY 2011, the assets, liabilities, net position, and net income from operations relating to earmarked, other entity, disgorgement and penalties, and other non-entity funds consisted of the following:

<i>(DOLLARS IN THOUSANDS)</i>	<b>Earmarked-Salaries &amp; Expenses</b>	<b>Earmarked-Investor Protection Fund</b>	<b>Eliminations</b>	<b>Total Earmarked Funds</b>	<b>Other Entity Funds</b>	<b>Disgorgement and Penalties</b>	<b>Other Non-Entity Funds</b>	<b>Total</b>
<b>Balance Sheet as of September 30, 2011</b>								
<b>ASSETS</b>								
Fund Balance with Treasury	\$ 6,874,218	\$ 73	\$ —	\$ 6,874,291	\$ 768	\$ 73,929	\$ 46,622	\$ 6,995,610
Cash and Other Monetary Assets	—	—	—	—	—	—	—	—
Investments, Net	—	452,715	—	452,715	—	749,810	—	1,202,525
Accounts Receivable, Net	122,930	—	—	122,930	—	90,982	134	214,046
Advances and Prepayments	10,828	—	—	10,828	—	—	—	10,828
Property and Equipment, Net	92,736	—	—	92,736	1,203	—	—	93,939
<b>Total Assets (Note 2)</b>	<b>\$ 7,100,712</b>	<b>\$ 452,788</b>	<b>\$ —</b>	<b>\$ 7,553,500</b>	<b>\$ 1,971</b>	<b>\$ 914,721</b>	<b>\$ 46,756</b>	<b>\$ 8,516,948</b>
<b>LIABILITIES</b>								
Accounts Payable	\$ 60,783	\$ —	\$ —	\$ 60,783	\$ 34	\$ —	\$ —	\$ 60,817
Accrued Payroll and Benefits	21,272	—	—	21,272	—	—	—	21,272
FECA and Unemployment Liability	9,575	—	—	9,575	—	—	—	9,575
Accrued Leave	45,472	—	—	45,472	—	—	—	45,472
Custodial Liability	—	—	—	—	—	51,745	—	51,745
Liability for Non-Entity Assets	—	—	—	—	—	—	134	134
Registrant Deposits	—	—	—	—	—	—	46,622	46,622
Liability for Disgorgement and Penalties	—	—	—	—	—	862,976	—	862,976
Other Accrued Liabilities	7,212	—	—	7,212	—	—	—	7,212
<b>Total Liabilities (Note 8)</b>	<b>144,314</b>	<b>—</b>	<b>—</b>	<b>144,314</b>	<b>34</b>	<b>914,721</b>	<b>46,756</b>	<b>1,105,825</b>

*Continued on next page*

Continued from previous page

<i>(DOLLARS IN THOUSANDS)</i>	Earmarked- Salaries & Expenses	Earmarked- Investor Protection Fund	Eliminations	Total Earmarked Funds	Other Entity Funds	Disgorgement and Penalties	Other Non-Entity Funds	Total
<b>NET POSITION</b>								
Unexpended Appropriations	—	—	—	—	735	—	—	735
Cumulative Results of Operations	6,956,398	452,788	—	7,409,186	1,202	—	—	7,410,388
<b>Total Net Position</b>	6,956,398	452,788	—	7,409,186	1,937	—	—	7,411,123
<b>Total Liabilities and Net Position</b>	\$ 7,100,712	\$ 452,788	\$ —	\$ 7,553,500	\$ 1,971	\$ 914,721	\$ 46,756	\$ 8,516,948
<b>Statement of Net Cost</b>								
<b>For the year ended September 30, 2011</b>								
Gross Program Costs	\$ 1,145,097	\$ 112	\$ 112	\$ 1,145,097	\$ 415	\$ —	\$ 2,626	\$ 1,148,138
Less Earned Revenues Not Attributable to Program Costs	1,640,893	—	112	1,640,781	—	—	2,949	1,643,730
Net (Income) Cost from Operations	\$ (495,796)	\$ 112	\$ —	\$ (495,684)	\$ 415	\$ —	\$ (323)	\$ (495,592)
<b>Statement of Changes in Net Position</b>								
<b>For the year ended September 30, 2011</b>								
Cumulative Results of Operations								
Beginning Balances	\$ 6,426,222	\$ 451,910	\$ —	\$ 6,878,132	\$ 603	\$ —	\$ —	\$ 6,878,735
Appropriations Used	—	—	—	—	1,014	—	—	1,014
Non-Exchange Revenue	—	990	—	990	—	—	—	990
Imputed Financing	34,380	—	—	34,380	—	—	—	34,380
Other	—	—	—	—	—	—	(323)	(323)
Net Income (Cost) from Operations	495,796	(112)	—	495,684	(415)	—	323	495,592
Net Change	530,176	878	—	531,054	599	—	—	531,653
Cumulative Results of Operations	6,956,398	452,788	—	7,409,186	1,202	—	—	7,410,388
Unexpended Appropriations								
Beginning Balances	—	—	—	—	1,749	—	—	1,749
Appropriations Used	—	—	—	—	(1,014)	—	—	(1,014)
Total Unexpended Appropriations	—	—	—	—	735	—	—	735
Net Position, End of Period	\$ 6,956,398	\$ 452,788	\$ —	\$ 7,409,186	\$ 1,937	\$ —	\$ —	\$ 7,411,123

For FY 2010, the assets, liabilities, net position, and net income from operations relating to earmarked, other entity, disgorgement and penalties, and other non-entity funds consisted of the following:

<i>(DOLLARS IN THOUSANDS)</i>	Earmarked- Salaries & Expenses	Earmarked- Investor Protection Fund	Eliminations	Total Earmarked Funds	Other Entity Funds	Disgorgement and Penalties	Other Non-Entity Funds	Total
<b>Balance Sheet as of September 30, 2010</b>								
<b>ASSETS</b>								
Fund Balance with Treasury	\$ 6,436,463	\$ 451,910	\$ —	\$ 6,888,373	\$ 1,996	\$ 54,269	\$ 44,729	\$ 6,989,367
Cash and Other Monetary Assets	—	—	—	—	—	2,815	—	2,815
Investments, Net	—	—	—	—	—	924,823	—	924,823
Accounts Receivable, Net	79,200	—	—	79,200	—	81,939	4	161,143
Advances and Prepayments	4,579	—	—	4,579	—	—	—	4,579
Property and Equipment, Net	79,109	—	—	79,109	603	—	—	79,712
<b>Total Assets (Note 2)</b>	<b>\$ 6,599,351</b>	<b>\$ 451,910</b>	<b>\$ —</b>	<b>\$ 7,051,261</b>	<b>\$ 2,599</b>	<b>\$ 1,063,846</b>	<b>\$ 44,733</b>	<b>\$ 8,162,439</b>
<b>LIABILITIES</b>								
Accounts Payable	\$ 51,313	\$ —	\$ —	\$ 51,313	\$ 132	\$ —	\$ —	\$ 51,445
Accrued Payroll and Benefits	37,622	—	—	37,622	115	—	—	37,737
FECA and Unemployment Liability	9,295	—	—	9,295	—	—	—	9,295
Accrued Leave	45,629	—	—	45,629	—	—	—	45,629
Custodial Liability	—	—	—	—	—	42,380	—	42,380
Liability for Non-Entity Assets	—	—	—	—	—	—	4	4
Registrant Deposits	—	—	—	—	—	—	44,729	44,729
Liability for Disgorgement and Penalties	—	—	—	—	—	1,021,466	—	1,021,466
Other Accrued Liabilities	29,270	—	—	29,270	—	—	—	29,270
<b>Total Liabilities (Note 8)</b>	<b>173,129</b>	<b>—</b>	<b>—</b>	<b>173,129</b>	<b>247</b>	<b>1,063,846</b>	<b>44,733</b>	<b>1,281,955</b>
<b>NET POSITION</b>								
Unexpended Appropriations	—	—	—	—	1,749	—	—	1,749
Cumulative Results of Operations	6,426,222	451,910	—	6,878,132	603	—	—	6,878,735
<b>Total Net Position</b>	<b>6,426,222</b>	<b>451,910</b>	<b>—</b>	<b>6,878,132</b>	<b>2,352</b>	<b>—</b>	<b>—</b>	<b>6,880,484</b>
<b>Total Liabilities and Net Position</b>	<b>\$ 6,599,351</b>	<b>\$ 451,910</b>	<b>\$ —</b>	<b>\$ 7,051,261</b>	<b>\$ 2,599</b>	<b>\$ 1,063,846</b>	<b>\$ 44,733</b>	<b>\$ 8,162,439</b>
<b>Statement of Net Cost</b>								
<b>For the year ended September 30, 2010</b>								
Gross Program Costs	\$ 1,050,910	\$ —	\$ —	\$ 1,050,910	\$ 7,508	\$ —	\$ 5	\$ 1,058,423
Less Earned Revenues Not Attributable to Program Costs	1,382,691	—	—	1,382,691	—	—	165	1,382,856
Net (Income) Cost from Operations	\$ (331,781)	\$ —	\$ —	\$ (331,781)	\$ 7,508	\$ —	\$ (160)	\$ (324,433)

Continued on next page

Continued from previous page

<i>(DOLLARS IN THOUSANDS)</i>	Earmarked- Salaries & Expenses	Earmarked- Investor Protection Fund	Eliminations	Total Earmarked Funds	Other Entity Funds	Disgorgement and Penalties	Other Non-Entity Funds	Total
<b>Statement of Changes in Net Position</b>								
<b>For the year ended September 30, 2010</b>								
Cumulative Results of Operations								
Beginning Balances	\$ 6,058,225	\$ —	\$ —	\$ 6,058,225	\$ —	\$ —	\$ —	\$ 6,058,225
Appropriations Used	—	—	—	—	8,111	—	—	8,111
Non-Exchange Revenue	—	451,910	—	451,910	—	—	—	451,910
Imputed Financing	36,216	—	—	36,216	—	—	—	36,216
Other	—	—	—	—	—	—	(160)	(160)
Net Income (Cost) from Operations	331,781	—	—	331,781	(7,508)	—	160	324,433
Net Change	367,997	451,910	—	819,907	603	—	—	820,510
Cumulative Results of Operations	6,426,222	451,910	—	6,878,132	603	—	—	6,878,735
Unexpended Appropriations								
Beginning Balances	—	—	—	—	9,860	—	—	9,860
Appropriations Used	—	—	—	—	(8,111)	—	—	(8,111)
Total Unexpended Appropriations	—	—	—	—	1,749	—	—	1,749
Net Position, End of Period	\$ 6,426,222	\$ 451,910	\$ —	\$ 6,878,132	\$ 2,352	\$ —	\$ —	\$ 6,880,484

## NOTE 12. Intragovernmental Costs and Exchange Revenue

The Statement of Net Cost presents the SEC's results of operations for its major programs. The SEC assigns all costs incurred to ten programs, consistent with its budget submissions. The full cost of SEC programs is the sum of (1) the costs of resources directly or indirectly consumed by those programs, and (2) the costs of identifiable supporting services provided by other responsibility segments within the agency. Typical examples of indirect costs include costs of general administrative services, technical support, security, rent, and operating and maintenance costs for buildings, equipment, and utilities. The SEC allocates support costs to its programs using activity-based cost accounting.

Intragovernmental costs arise from purchases of goods and services from other components of the Federal Government. In contrast, public costs are those which arise from the purchase of goods and services from non-Federal entities.

Exchange revenue is not directly assignable to a specific program and is presented in total. The Statement of Net Cost, for the fiscal years ended September 30, 2011 and 2010, with a breakout of intragovernmental and public costs is presented below.

	FY 2011		
	Intragovernmental Gross Cost	Gross Cost with the Public	Total
<i>(DOLLARS IN THOUSANDS)</i>			
<b>SEC Programs:</b>			
Enforcement	\$ 72,533	\$ 318,650	\$ 391,183
Compliance Inspections and Examinations	44,396	195,039	239,435
Corporation Finance	24,412	107,248	131,660
Trading and Markets	11,528	50,648	62,176
Investment Management	8,759	38,481	47,240
Risk, Strategy, and Financial Innovation	3,723	16,357	20,080
General Counsel	7,668	33,689	41,357
Other Program Offices	8,367	36,755	45,122
Agency Direction and Administrative Support	30,290	133,067	163,357
Inspector General	1,210	5,318	6,528
<b>Total Program Costs</b>	<b>\$ 212,886</b>	<b>\$ 935,252</b>	<b>1,148,138</b>
<b>Less: Exchange Revenues</b>			
Securities Transaction Fees			1,279,260
Securities Registration, Tender Offer, and Merger Fees			361,284
Other			3,186
<b>Total Exchange Revenues</b>			<b>1,643,730</b>
<b>Net (Income) Cost from Operations</b>			<b>\$ (495,592)</b>

	FY 2010		
	Intragovernmental Gross Cost	Gross Cost with the Public	Total
<i>(DOLLARS IN THOUSANDS)</i>			
<b>SEC Programs:</b>			
Enforcement	\$ 61,669	\$ 293,782	\$ 355,451
Compliance Inspections and Examinations	39,798	189,591	229,389
Corporation Finance	22,757	108,409	131,166
Trading and Markets	9,388	44,719	54,107
Investment Management	8,306	39,567	47,873
Risk, Strategy, and Financial Innovation	3,148	14,995	18,143
General Counsel	6,901	32,879	39,780
Other Program Offices	8,432	40,171	48,603
Agency Direction and Administrative Support	22,300	106,231	128,531
Inspector General	933	4,447	5,380
<b>Total Program Costs</b>	<b>\$ 183,632</b>	<b>\$ 874,791</b>	<b>1,058,423</b>
<b>Less: Exchange Revenues</b>			
Securities Transaction Fees			1,163,633
Securities Registration, Tender Offer, and Merger Fees			218,755
Other			468
<b>Total Exchange Revenues</b>			<b>1,382,856</b>
<b>Net (Income) Cost from Operations</b>			<b>\$ (324,433)</b>

Intragovernmental exchange revenue was \$236 thousand and \$304 thousand for the fiscal years ending September 30, 2011 and 2010, respectively.

### NOTE 13. Imputed Financing

A portion of the retirement benefits provided to SEC employees is funded by OPM. In accordance with Federal accounting standards, the SEC recognizes identified costs paid by OPM on behalf of the SEC as an expense. The funding for this expense is reflected as imputed financing on the Statement of Changes in Net Position. Costs paid by OPM on behalf of the SEC were \$34.4 million and \$36.2 million in FY 2011 and FY 2010, respectively.

## NOTE 14. Status of Budgetary Resources

### A. Apportionment Categories of Obligations Incurred

Category A funds are those amounts that are subject to quarterly apportionment by OMB, meaning that a portion of the annual appropriation is not available to the agency until apportioned each quarter. Category B funds represent budgetary resources distributed by a specified time period, activity, project, object, or a combination of these categories. The SEC's Category B funds represent amounts apportioned at the beginning of the fiscal year for the SEC's reimbursable and Investor Protection Fund activities. For the fiscal years ended September 30, 2011 and 2010, the SEC incurred obligations against Category A and Category B funds as follows:

<b>Obligations Incurred</b> <i>(DOLLARS IN THOUSANDS)</i>	<b>FY 2011</b>	<b>FY 2010</b>
Direct Obligations		
Category A	\$ 1,215,032	\$ 1,103,007
Category A – Change in Legal Interpretation for Lease Obligations	777,928	—
Category B – Investor Protection Fund	112	—
Total Direct Obligations	1,993,072	1,103,007
Reimbursable Obligations		
Category B	388	282
Total Obligations Incurred	\$ 1,993,460	\$ 1,103,289

In addition, the amounts of budgetary resources obligated for undelivered orders include \$1,028.5 million and \$219.3 million at September 30, 2011 and 2010, respectively.

### B. Explanation of Differences between the Statement of Budgetary Resources and the Budget of the U.S. Government

A comparison between the FY 2011 SBR and the actual FY 2011 data in the President's budget cannot be presented, as the FY 2013 President's budget which will contain FY 2011 actual data is not yet available; the comparison will be presented in next year's financial statements. There are no differences between the FY 2010 SBR and the FY 2010 data in the President's budget except for rounding differences of \$1 million in the Unobligated Balances and Obligated Balances, Net, End of Period.

### C. Other Budgetary Disclosures

#### General Provisions of Appropriation

The SEC's annual appropriation bill contains general provisions which limit the amount that can be obligated for international conferences, International Organization of Securities Commission (IOSCO) dues, and representation expenses.

### **Change in Legal Interpretation for Lease Obligations**

The SEC was granted independent leasing authority in 1990. Based on a legal review of its statutory authority at the time, the SEC adopted a policy of obligating only the annual portion of lease payments due each year. On October 3, 2011, the Government Accountability Office (GAO) issued a decision that this longstanding practice of recording lease obligations only on an annual basis violated the recording statute, 31 U.S.C. sect. 1501(a)(1). Specifically, GAO's decision was that the SEC lacks statutory authority to obligate an amount less than the Government's total obligation. If the SEC lacks sufficient budget authority to cover this obligation, the SEC should report a violation of the Antideficiency Act (ADA).

The SEC recorded obligations in the same manner for all its leasing actions between the time the agency was granted independent leasing authority in 1990 and 2010. Further, the agency does not have sufficient remaining unobligated funds in the years in which the various leases were entered to cover the full obligations associated with those leases. As a result, the agency is reporting Antideficiency Act violations between 1990 and 2010.

The SEC appropriately obligated the Government's total financial responsibility for the three lease actions initiated in FY 2011. For the SEC's other 17 current leases for which Antideficiency Act violations occurred, obligations of \$778 million have been recorded.

Further, in a step that will help prevent a recurrence of this type of violation in the future, on August 1, 2011, the SEC and GSA entered into a Memorandum of Understanding pursuant to which the SEC agreed that all future lease acquisitions for the SEC's office space needs shall be performed by GSA, pursuant to GSA's leasing authority. GSA's leasing authority includes the express statutory authority to obligate funds for leases in the fiscal year for which payments are due. Accordingly, in the future, the SEC will recognize annual lease payments due to GSA in accordance with standard GSA lease procedures.

See *Note 10.A. Commitments: Securities Investor Protection Act*, for information on SEC borrowing authority.

## NOTE 15. Reconciliation of Net Cost of Operations (Proprietary) to Budget (formerly the Statement of Financing)

For the fiscal years ended September 30, 2011 and 2010:

<i>(DOLLARS IN THOUSANDS)</i>	<b>FY 2011</b>	<b>FY 2010</b>
<b>RESOURCES USED TO FINANCE ACTIVITIES:</b>		
Budgetary Resources Obligated:		
Obligations Incurred (Note 14)	\$ 1,993,460	\$ 1,103,289
Less: Spending Authority from Offsetting Collections and Recoveries	(1,637,034)	(1,461,657)
Net Obligations	356,426	(358,368)
Other Resources:		
Imputed Financing from Cost Absorbed by Others (Note 13)	34,380	36,216
<b>Total Resources Used to Finance Activities</b>	<b>390,806</b>	<b>(322,152)</b>
<b>RESOURCES USED TO FINANCE ITEMS NOT PART OF THE NET COST OF OPERATIONS:</b>		
Change in Budgetary Resources Obligated for Goods, Services, and Benefits Ordered But Not Yet Provided		
	(815,449)	(67,775)
Resources That Finance the Acquisition of Assets Capitalized on the Balance Sheet	(43,809)	(27,319)
<b>Total Resources Used to Finance Items Not Part of the Net Cost of Operations</b>	<b>(859,258)</b>	<b>(95,094)</b>
<b>Total Resources Used to Finance the Net Cost of Operations</b>	<b>(468,452)</b>	<b>(417,246)</b>
<b>COMPONENTS OF NET COST OF OPERATIONS THAT WILL NOT REQUIRE OR GENERATE RESOURCES IN THE CURRENT PERIOD:</b>		
Components Requiring or Generating Resources in Future Periods:		
Change in Accrued Leave Liability	(157)	2,933
Change in Revenue Receivables Not Generating Resources until Collected	(43,710)	60,320
Change in Lease Liability	(2,946)	(3,311)
Change in Legal Liability	(9,867)	10,823
Change in Unfunded Liability	280	(7,824)
<b>Total Components of Net Cost of Operations That Will Require or Generate Resources in Future Periods</b>	<b>(56,400)</b>	<b>62,941</b>
Components Not Requiring or Generating Resources:		
Depreciation and Amortization	27,951	25,408
Revaluation of Assets or Liabilities	1,631	4,634
Other Costs that will not Require or Generate Resources	(322)	(170)
Total Components of Net Cost of Operations That Will Not Require or Generate Resources in Future Periods	29,260	29,872
<b>Total Components of Net Cost of Operations That Will Not Require or Generate Resources in the Current Period</b>	<b>(27,140)</b>	<b>92,813</b>
<b>Net (Income) Cost from Operations</b>	<b>\$ (495,592)</b>	<b>\$ (324,433)</b>

## NOTE 16. Disgorgement and Penalties

The SEC's non-entity assets consist of disgorgement, penalties, and interest assessed against securities law violators by the Commission, administrative law judge, or in some cases, a court. The SEC also recognizes an equal and offsetting liability for these non-entity assets as discussed in *Note 1.M. Liabilities*. When the Commission or court issues an order for the SEC to collect disgorgement, penalties, and interest from securities law violators, the SEC establishes an account receivable due to the SEC. When collected, the SEC either (a) holds receipts in FBWT or Treasury investments pending distribution to harmed investors or (b) transfers to the Investor Protection Fund or the U.S. Treasury General Fund. Disbursements related to disgorgements and penalties include distributions to harmed investors, payments to tax authorities, and fees paid to plan administrators and the Bureau of Public Debt. When it is not practical to return funds to investors or when court orders expressly state that funds are to be remitted to the U.S. Treasury, the SEC transfers funds to the Investor Protection Fund or to the U.S. Treasury General Fund. The SEC does not record on its financial statements any amounts ordered to another Government entity such as a court, or a non-governmental entity such as a receiver. Additional details regarding disgorgement and penalties are presented in *Note 1.S. Disgorgement and Penalties*, *Note 2. Assets* and *Note 11. Earmarked, Other Entity, Disgorgement and Penalties, and Other Non-Entity Funds*.

At September 30, the net inflows and outflows for FBWT, Investments, and Accounts Receivable related to disgorgement and penalties consisted of the following:

<i>(DOLLARS IN THOUSANDS)</i>	FY 2011	FY 2010
Fund Balance with Treasury:		
Beginning Balance	\$ 54,269	\$ 43,622
Collections	544,200	1,214,911
Purchases and Redemptions of Treasury Securities	175,520	1,036,168
Disbursements	(286,647)	(1,123,799)
Transfers to Investor Protection Fund	—	(451,910)
Transfers to Treasury	(413,413)	(664,723)
Total Fund Balance with Treasury (Note 2)	73,929	54,269
Cash and Other Monetary Assets:		
Beginning Balance	2,815	—
Net Activity	(2,815)	2,815
Total Cash and Other Monetary Assets (Notes 2 and 4)	—	2,815
Investments, Net:		
Beginning Balance	924,823	1,959,611
Net Activity	(175,013)	(1,034,788)
Total Investments, Net (Notes 2 and 5)	749,810	924,823
Accounts Receivable, Net:		
Beginning Balance	81,939	294,508
Net Activity	9,043	(212,569)
Total Accounts Receivable, Net (Notes 2 and 6)	90,982	81,939
Total Disgorgement and Penalties (Note 11)	\$ 914,721	\$ 1,063,846

## Required Supplementary Information (Unaudited)

This section provides the Required Supplementary Information as prescribed by OMB Circular No. A-136, *Financial Reporting Requirements*.

### Statement of Budgetary Resources by Fund

For the fiscal year ended September 30, 2011:

(DOLLARS IN THOUSANDS)	Salaries and Expenses and Other Funds	Supplemental Fund	Investor Protection Fund	Total
	X0100, 1435, 3220	09/10 0100	X5567	
<b>BUDGETARY RESOURCES:</b>				
Unobligated Balance, Brought Forward, October 1	\$ 37,332	\$ 107	\$ 451,910	\$ 489,349
Recoveries of Prior Year Unpaid Obligations	38,628	317	—	38,945
Budget Authority:				
Appropriation	—	—	(847)	(847)
Spending Authority from Offsetting Collections:				
Earned:				
Collected	1,598,067	—	—	1,598,067
Change in Receivables from Federal Sources	20	—	—	20
Change in Unfilled Customer Orders:				
Advance Received	—	—	—	—
Without Advance from Federal Sources	2	—	—	2
Subtotal	1,598,089	—	(847)	1,597,242
Temporarily not Available Pursuant to Public Law	(412,005)	—	—	(412,005)
<b>Total Budgetary Resources</b>	<b>\$ 1,262,044</b>	<b>\$ 424</b>	<b>\$ 451,063</b>	<b>\$ 1,713,531</b>
<b>STATUS OF BUDGETARY RESOURCES:</b>				
Obligations Incurred:				
Direct (Note 14)	\$ 1,215,032	\$ —	\$ 112	\$ 1,215,144
Direct, Change in Legal Interpretation for Lease Obligations (Note 14)	777,928	—	—	777,928
Reimbursable (Note 14)	388	—	—	388
Subtotal	1,993,348	—	112	1,993,460
Unobligated Balance:				
Apportioned	8,297	—	450,951	459,248
Unobligated Balance Not Available	(739,601)	424	—	(739,177)
<b>Total Status of Budgetary Resources</b>	<b>\$ 1,262,044</b>	<b>\$ 424</b>	<b>\$ 451,063</b>	<b>\$ 1,713,531</b>
<b>CHANGE IN OBLIGATED BALANCE:</b>				
Obligated Balance, Net:				
Unpaid Obligations, Brought Forward, October 1	\$ 315,883	\$ 1,889	\$ —	\$ 317,772
Uncollected Customer Payments from Federal Sources, Brought Forward, October 1	(25)	—	—	(25)
Total Unpaid Obligated Balance, Net, Beginning of Fiscal Year	315,858	1,889	—	317,747
Obligations Incurred Net	1,993,348	—	112	1,993,460
Gross Outlays	(1,160,313)	(1,228)	(112)	(1,161,653)
Recoveries of Prior Year Unpaid, Obligations, Actual	(38,628)	(317)	—	(38,945)
Change in Uncollected Customer Payments from Federal Sources	(22)	—	—	(22)
Total, Unpaid Obligated Balance, Net, End of Period (Note 10)	\$ 1,110,243	\$ 344	\$ —	\$ 1,110,587
Obligated Balance, Net, End of Period:				
Unpaid Obligations	\$ 1,110,290	\$ 344	\$ —	\$ 1,110,634
Uncollected Customer Payments from Federal Sources	(47)	—	—	(47)
Total, Unpaid Obligated Balance, Net, End of Period (Note 10)	\$ 1,110,243	\$ 344	\$ —	\$ 1,110,587
<b>NET OUTLAYS:</b>				
Net Outlays:				
Gross Outlays	\$ 1,160,313	\$ 1,228	\$ 112	\$ 1,161,653
Offsetting Collections	(1,598,067)	—	—	(1,598,067)
Distributed Offsetting Receipts	(187)	—	847	660
Net Outlays/(Collections)	\$ (437,941)	\$ 1,228	\$ 959	\$ (435,754)

For the fiscal year ended September 30, 2010:

<i>(DOLLARS IN THOUSANDS)</i>	<b>Salaries and Expenses and Other Funds</b>	<b>Supplemental Fund</b>	<b>Investor Protection Fund</b>	<b>Total</b>
	<b>X0100, 3220, F3875</b>	<b>09/10 0100</b>	<b>X5567</b>	
<b>BUDGETARY RESOURCES:</b>				
Unobligated Balance, Brought Forward, October 1	\$ 19,011	\$ 7,754	\$ —	\$ 26,765
Recoveries of Prior Year Unpaid Obligations	18,753	—	—	18,753
Budget Authority:				
Appropriation	—	—	451,910	451,910
Spending Authority from Offsetting Collections:				
Earned:				
Collected	1,443,347	—	—	1,443,347
Change in Receivables from Federal Sources	(188)	—	—	(188)
Change in Unfilled Customer Orders:				
Advance Received	(157)	—	—	(157)
Without Advance from Federal Sources	(98)	—	—	(98)
Subtotal	1,442,904	—	451,910	1,894,814
Temporarily not Available Pursuant to Public Law	(347,694)	—	—	(347,694)
<b>Total Budgetary Resources</b>	<b>\$ 1,132,974</b>	<b>\$ 7,754</b>	<b>\$ 451,910</b>	<b>\$ 1,592,638</b>
<b>STATUS OF BUDGETARY RESOURCES:</b>				
Obligations Incurred:				
Direct (Note 14)	\$ 1,095,360	\$ 7,647	\$ —	\$ 1,103,007
Direct, Change in Legal Interpretation for Lease Obligations (Note 14)	—	—	—	—
Reimbursable (Note 14)	282	—	—	282
Subtotal	1,095,642	7,647	—	1,103,289
Unobligated Balance:				
Apportioned	17,106	107	—	17,213
Unobligated Balance Not Available	20,226	—	451,910	472,136
<b>Total Status of Budgetary Resources</b>	<b>\$ 1,132,974</b>	<b>\$ 7,754</b>	<b>\$ 451,910</b>	<b>\$ 1,592,638</b>
<b>CHANGE IN OBLIGATED BALANCE:</b>				
Obligated Balance, Net:				
Unpaid Obligations, Brought Forward, October 1	\$ 234,292	\$ 2,107	\$ —	\$ 236,399
Uncollected Customer Payments from Federal Sources, Brought Forward, October 1	(311)	—	—	(311)
Total Unpaid Obligated Balance, Net, Beginning of Fiscal Year	233,981	2,107	—	236,088
Obligations Incurred Net	1,095,642	7,647	—	1,103,289
Gross Outlays	(995,299)	(7,864)	—	(1,003,163)
Recoveries of Prior Year Unpaid, Obligations, Actual	(18,753)	—	—	(18,753)
Change in Uncollected Customer Payments from Federal Sources	286	—	—	286
Total, Unpaid Obligated Balance, Net, End of Period (Note 10)	<b>\$ 315,857</b>	<b>\$ 1,890</b>	<b>\$ —</b>	<b>\$ 317,747</b>
Obligated Balance, Net, End of Period:				
Unpaid Obligations	315,882	1,890	—	317,772
Uncollected Customer Payments from Federal Sources	(25)	—	—	(25)
Total, Unpaid Obligated Balance, Net, End of Period (Note 10)	<b>\$ 315,857</b>	<b>\$ 1,890</b>	<b>\$ —</b>	<b>\$ 317,747</b>
<b>NET OUTLAYS:</b>				
Net Outlays:				
Gross Outlays	\$ 995,299	\$ 7,864	\$ —	\$ 1,003,163
Offsetting Collections	(1,443,190)	—	—	(1,443,190)
Distributed Offsetting Receipts	194	—	—	194
Net Outlays/(Collections)	<b>\$ (447,697)</b>	<b>\$ 7,864</b>	<b>\$ —</b>	<b>\$ (439,833)</b>

# **INVESTOR PROTECTION FUND FINANCIAL STATEMENTS**

---

Investor Protection Fund Financial Statements 158

Notes to the Investor Protection  
Fund Financial Statements 161

## Investor Protection Fund Financial Statements

U.S. SECURITIES AND EXCHANGE COMMISSION  
INVESTOR PROTECTION FUND

### Balance Sheet

As of September 30, 2011 and 2010

(DOLLARS IN THOUSANDS)

	FY 2011	FY 2010
<b>ASSETS:</b>		
Intragovernmental:		
Fund Balance with Treasury (Note 2)	\$ 73	\$ 451,910
Investments, Net (Note 3)	452,715	—
<b>Total Assets</b>	<b>\$ 452,788</b>	<b>\$ 451,910</b>
<b>LIABILITIES:</b>		
Commitments and Contingencies (Note 4)		
<b>NET POSITION:</b>		
Cumulative Results of Operations – Earmarked Funds	\$ 452,788	\$ 451,910
<b>Total Liabilities and Net Position</b>	<b>\$ 452,788</b>	<b>\$ 451,910</b>

The accompanying notes are an integral part of these financial statements.

U.S. SECURITIES AND EXCHANGE COMMISSION  
INVESTOR PROTECTION FUND

## Statement of Net Cost

For the years ended September 30, 2011 and 2010

(DOLLARS IN THOUSANDS)	FY 2011	FY 2010
<b>PROGRAM COSTS (Note 5):</b>		
Employee Suggestion Program	\$ 112	\$ —
<b>Total Program Costs</b>	112	—
<b>Net (Income) Cost from Operations</b>	\$ 112	\$ —

The accompanying notes are an integral part of these financial statements.

U.S. SECURITIES AND EXCHANGE COMMISSION  
INVESTOR PROTECTION FUND

## Statement of Changes in Net Position

For the years ended September 30, 2011 and 2010

(DOLLARS IN THOUSANDS)	FY 2011	FY 2010
<b>CUMULATIVE RESULTS OF OPERATIONS – EARMARKED FUNDS:</b>		
Beginning Balances	\$ 451,910	\$ —
<b>Budgetary Financing Sources:</b>		
Non-Exchange Revenue	990	451,910
Net Income (Cost) from Operations	(112)	—
Net Change	878	451,910
Cumulative Results of Operations	452,788	451,910
<b>Net Position, End of Period</b>	\$ 452,788	\$ 451,910

The accompanying notes are an integral part of these financial statements.

U.S. SECURITIES AND EXCHANGE COMMISSION  
INVESTOR PROTECTION FUND

## Statement of Budgetary Resources

For the years ended September 30, 2011 and 2010

(DOLLARS IN THOUSANDS)

	FY 2011	FY 2010
<b>BUDGETARY RESOURCES:</b>		
Unobligated Balance, Brought Forward, October 1	\$ 451,910	\$ —
Budget Authority:		
Appropriation	(847)	451,910
<b>Total Budgetary Resources</b>	<b>\$ 451,063</b>	<b>\$ 451,910</b>
<b>STATUS OF BUDGETARY RESOURCES:</b>		
Obligations Incurred:		
Direct – Category B (Note 6)	\$ 112	\$ —
Unobligated Balance:		
Apportioned	450,951	—
Unobligated Balance Not Available	—	451,910
<b>Total Status of Budgetary Resources</b>	<b>\$ 451,063</b>	<b>\$ 451,910</b>
<b>CHANGE IN OBLIGATED BALANCE:</b>		
Obligations Incurred Net	\$ 112	\$ —
Gross Outlays	(112)	—
Total, Unpaid Obligated Balance, Net, End of Period (Note 6)	\$ —	\$ —
<b>NET OUTLAYS:</b>		
Net Outlays:		
Gross Outlays	\$ 112	\$ —
Distributed Offsetting Receipts	847	—
Net Outlays/(Collections)	\$ 959	\$ —

The accompanying notes are an integral part of these financial statements.

# Notes to the Investor Protection Fund Financial Statements

U.S. SECURITIES AND EXCHANGE COMMISSION

As of September 30, 2011 and 2010

## NOTE 1. Summary of Significant Accounting Policies

### A. Reporting Structure

The United States Securities and Exchange Commission (SEC) is an independent agency of the United States Government established pursuant to the Securities Exchange Act of 1934 (Exchange Act), charged with regulating this country's capital markets. The Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act) established the Securities and Exchange Commission Investor Protection Fund. The Investor Protection Fund provides funding for a Whistleblower Award Program and finances the operations of the SEC Office of the Inspector General's (OIG) employee suggestion program. The Investor Protection Fund is a fund within the SEC, and these financial statements present a segment of the SEC's financial activity.

### B. Basis of Presentation and Accounting

The accompanying financial statements present the financial position, net cost of operations, changes in net position, and budgetary resources of the Investor Protection Fund as required by Exchange Act Section 21F(g)(5). The Act requires a complete set of financial statements that includes a balance sheet, income statement, and cash flow analysis. The Investor Protection Fund is a Federal reporting entity. As such, its financial statements are prepared in conformity with Generally Accepted Accounting Principles (GAAP) for the Federal Government, and are presented in conformity with OMB Circular A-136, *Financial Reporting Requirements*. The legislative requirements to prepare an income statement and cash flow analysis are addressed by the Statement of Net Cost and Note 2. *Fund Balance with Treasury*, respectively.

The SEC's books and records serve as the source of the information presented in the accompanying financial statements.

The agency classifies assets, liabilities, revenues, and costs in these financial statements according to the type of entity associated with the transactions. Intragovernmental assets and liabilities are those due from or to other Federal entities, including

those activities within the SEC. Intragovernmental revenues and costs result from transactions with other Federal entities.

The Balance Sheet, Statement of Net Cost and Statement of Changes in Net Position are prepared using the accrual basis of accounting. Accordingly, revenues are recognized when earned and expenses are recognized when incurred without regard to the receipt or payment of cash. These principles differ from budgetary accounting and reporting principles on which the Statement of Budgetary Resources is prepared. The statements may differ from other financial reports submitted pursuant to Office of Management and Budget (OMB) directives for the purpose of monitoring and controlling the use of budgetary resources, due to differences in applicable accounting and reporting principles discussed in the following paragraphs. Conceptually, the differences relate primarily to the capitalization and depreciation of property and equipment, as well as the recognition of other long-term assets and liabilities and are not currently applicable to the Investor Protection Fund.

### C. Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities. These estimates and assumptions include the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results may differ from those estimates.

### D. Intra- and Inter-Agency Relationships

#### Transactions with Other SEC Entities

The Investor Protection Fund is comprised of a single Federal Treasury Fund Symbol and has no intra-entity transactions. The Investor Protection Fund is the recipient of non-exchange revenues collected by the SEC and reported on the SEC's Statement of Custodial Activity. The Investor Protection

Fund finances the OIG's employee suggestion program on a reimbursable basis.

Accounts receivable that may be used to fund the Investor Protection Fund are recognized as assets of the SEC. These resources are not assets of the Investor Protection Fund until the determination is made to deposit collections in the Investor Protection Fund.

### Transactions with Other Federal Agencies

Whistleblower payments may be made from the Investor Protection Fund as a result of monetary sanctions paid to other Federal agencies in related actions, but only if there has been a Commission enforcement action resulting in sanctions of a million dollars or greater and the Commission has determined that the whistleblower is eligible for an award and recommended the percentage. In those instances, the SEC remains liable for paying the whistleblower. However, in instances where a whistleblower has already received an award from the Commodity Futures Trading Commission (CFTC), the whistleblower is not entitled to an award from the SEC.

### E. Earmarked Fund

Earmarked funds are financed by specifically identified revenues, often supplemented by other financing sources, which remain available over time. Investor Protection Fund resources are earmarked and may only be used for the purposes specified by the Dodd-Frank Act.

### F. Entity Assets

Assets that an agency is authorized to use in its operations are entity assets. The SEC is authorized to use all funds in the Investor Protection Fund for its operations. Accordingly, all assets are recognized as entity assets.

### G. Fund Balance with Treasury

Fund Balance with Treasury reflects amounts the Investor Protection Fund holds in the U.S. Treasury that have not been invested in Federal securities. The SEC conducts all of its banking activity in accordance with directives issued by the United States Department of the Treasury's Financial Management Service.

### H. Investments

The SEC has authority to invest amounts in the Investor Protection Fund in overnight and short-term, market-based Treasury securities. The interest earned on the investments is a component of the Fund and is available to be used for expenses of the Investor Protection Fund. Additional details regarding Investor Protection Fund investments are provided in *Note 3. Investments, Net*.

Market-based Treasury securities are debt securities that the U.S. Treasury issues to Federal entities without statutorily determined interest rates. Although the securities are not marketable, the terms (prices and interest rates) mirror the terms of marketable Treasury securities.

Treasury securities are an asset of the Investor Protection Fund and a liability of the U.S. Treasury. Because the Investor Protection Fund and the U.S. Treasury are both components of the Federal Government, these assets and liabilities offset each other from the standpoint of the Government as a whole. For this reason, the investments presented by the Investor Protection Fund do not represent an asset or a liability in the U.S. Government-wide financial statements.

The Federal Government does not set aside assets to pay future benefits or other expenditures associated with the investment by Federal agencies in non-marketable Federal securities. The balances underlying these investments are deposited in the U.S. Treasury, which uses the cash for general Government purposes. When the Investor Protection Fund requires redemption of these securities to make expenditures, the Government finances those expenditures out of accumulated cash balances by raising taxes or other receipts, by borrowing from the public or repaying less debt, or by curtailing other expenditures. This is the same manner in which the Government finances all expenditures.

### I. Liabilities

The SEC records liabilities for probable future outflows or other sacrifices of resources as a result of events that have occurred as of the Balance Sheet date. Investor Protection Fund's liabilities will consist of payables to whistleblowers and reimbursable expenses that the Office of Inspector General incurs to operate the Employee Suggestion Program. There

are no liabilities or contingent liabilities related to the Investor Protection Fund as of September 30, 2011 and 2010, respectively.

The Dodd-Frank Act and the SEC implementing regulations establish the eligibility criteria for Whistleblower awards. Refer to *Note 4. Commitments and Contingencies* for information regarding the disclosure and recognition of actual and contingent liabilities for Whistleblower awards.

## J. Program Costs

The Investor Protection Fund reimburses the SEC's General Fund (X0100) for expenses incurred by the Office of Inspector General to administer the Employee Suggestion Program. The Investor Protection Fund also finances payments to whistleblowers under Section 21F of the Exchange Act. The SEC adopted the final rules to implement the Whistleblower Program on May 25, 2011. As of September 30, 2011, there are no amounts paid or payable under the Whistleblower Program.

## K. Non-Exchange Revenue

### Disgorgement and Penalty Transfers

Non-exchange revenue arises from the Government's ability to demand payment. The Investor Protection Fund is financed through the receipt of portions of monetary sanctions collected by the SEC in judicial or administrative actions brought by the SEC under the securities laws that are not either: (1) added to the disgorgement fund or other fund under Section 308 of the Sarbanes-Oxley Act of 2002 (15 U.S.C. 7246) or (2) otherwise distributed to victims of a violation of the securities laws. The Investor Protection Fund recognizes non-exchange revenue for disgorgement and penalty amounts transferred into the fund from the SEC's Disgorgement and Penalties Fund (X6563). No sanction collected by the SEC can be deposited into the Investor Protection Fund if the balance in the fund exceeds \$300 million on the day of collection.

## Interest Earnings on Investments with Treasury

Interest earned from investments in U.S. Treasury securities is classified in the same way as the predominant source of revenue to the fund. The Investor Protection Fund is financed through the receipt of non-exchange revenues and thus interest earnings are also recognized as non-exchange revenues.

## L. Budgets and Budgetary Accounting

The Investor Protection Fund (Fund X5567) is a special fund established through a permanent indefinite appropriation that has the authority to retain revenues and other financing sources not used in the current period for future use. The Dodd-Frank Act provides that the Fund is available to the SEC without further appropriation or fiscal year limitation for the purpose of paying awards to whistleblowers and funding the activities of the OIG's employee suggestion program. However, the SEC is required to request and obtain an annual apportionment from OMB to use these funds. In FY 2010, the SEC received a \$451.9 million apportionment for the Fund for use in FY 2011.

The resources of the Investor Protection Fund are apportioned under Category B authority, which means that the funds represent budgetary resources distributed by a specified time period, activity, project, object, or a combination of these categories and are not subject to quarterly apportionment. Thus, all obligations incurred as presented on the Statement of Budgetary Resources are derived from Category B funds.

## NOTE 2. Fund Balance with Treasury

The Fund Balance with Treasury by type of fund and Status of Fund Balance with Treasury as of September 30, 2011 and 2010 consists of the following:

<i>(DOLLARS IN THOUSANDS)</i>	FY 2011	FY 2010
<b>Fund Balances:</b>		
Special Fund	\$ 73	\$ 451,910
Total Fund Balance with Treasury	\$ 73	\$ 451,910
<b>Status of Fund Balance with Treasury:</b>		
Unobligated Balance		
Available	\$ 73	\$ —
Unavailable	—	451,910
Total Fund Balance with Treasury	\$ 73	\$ 451,910

Unobligated balances reported for the status of Fund Balance with Treasury do not agree with the amounts reported in the Statement of Budgetary Resources due to the fact that unobligated balances are not reduced when investments are purchased.

There were no differences between the Fund Balance reflected in the Investor Protection Fund financial statements and the balance in the Treasury accounts.

### Cash flow

The Investor Protection Fund cash flows are reflected in investments and in the Statement of Budgetary Resources. Such cash flows during FY 2011 consisted of net investment purchases of \$453.8 million (which includes \$2 million of reinvested interest of the total \$2.1 million interest received), and the cost of operating the OIG Employee Suggestion Program of \$112 thousand. Cash flows during FY 2010 consisted of a transfer from Disgorgements and Penalties of \$451.9 million.

## NOTE 3. Investments, Net

The SEC invests funds in overnight and short-term non-marketable market-based Treasury bills. The SEC records the value of its investments in Treasury bills at cost and amortizes any premium or discount on a straight-line basis (S/L) through the maturity date of these securities. Non-marketable market-based Treasury securities are issued by the Bureau of Public Debt to Federal agencies. They are not traded on any securities exchange but mirror the prices of similar Treasury securities trading in the Government securities market.

At September 30, 2011, investments consisted of the following:

<i>(DOLLARS IN THOUSANDS)</i>	Cost	Amortization Method	Amortized (Premium) Discount	Interest Receivable	Investment, Net	Market Value Disclosure
Non-Marketable Market-Based Securities						
Investor Protection Fund – Entity	\$453,799	S/L	\$ (2,314)	\$ 1,230	\$452,715	\$451,696

## NOTE 4. Commitments and Contingencies

As mentioned in *Note 1.I. Liabilities*, the Investor Protection Fund will be used to pay awards to whistleblowers if they voluntarily provide original information to the SEC and meet other conditions. The legislation allows whistleblowers to receive between 10 and 30 percent of the monetary sanctions collected in the covered action or in a related action, with the actual percentage being determined at the discretion of the SEC using criteria provided in the legislation and the related rules to implement the legislation adopted by the SEC.

A contingent liability is recognized in instances where a positive Preliminary Determination has been made by the Claims Review Staff in the Office of the Whistleblower and the amount can be estimated. A Preliminary Determination is a first assessment, made by the Claims Review Staff, as to whether the claim should be allowed or denied and, if allowed, setting forth the proposed award percentage amount. Liabilities are recognized in instances where a collection has been received and a positive Proposed Final Determination has been reached by the Claims Review Staff. However, the actual payment of the whistleblower award would not occur until after the Determination became final.

## NOTE 5. Intragovernmental Costs

The Statement of Net Cost presents the Investor Protection Fund's results of operations for its two activities: the Employee Suggestion Program and Payments to Whistleblowers.

Intragovernmental costs arise from purchases of goods and services from other components of the Federal Government (including other SEC funds). In contrast, public costs are those which arise from the purchase of goods and services from non-Federal entities. The Employee Suggestion Program incurred \$111 thousand of intragovernmental costs and \$1 thousand of costs with the public in FY 2011.

## NOTE 6. Status of Budgetary Resources

### A. Explanation of Differences between the Statement of Budgetary Resources and the Budget of the U.S. Government

A comparison between the FY 2011 Statement of Budgetary Resources (SBR) and the actual FY 2011 data in the President's budget cannot be presented, as the FY 2013 President's budget which will contain FY 2011 actual data is not yet available; the comparison will be presented in next year's financial statements. There are no differences between the FY 2010 SBR and the FY 2010 data in the President's budget.

### B. Other Budgetary Disclosures

There are no budgetary resources obligated for undelivered orders as of September 30, 2011.

There are no legal arrangements affecting the use of unobligated balances of budget authority, such as time limits, purpose, and obligation limitations.

**NOTE 7. Reconciliation of Net Cost of Operations (Proprietary) to Budget  
(formerly the Statement of Financing)**

For the fiscal year ended September 30, 2011, Obligations Incurred equaled the Net Cost of Operations and there were no reconciling items. For the fiscal year ended September 30, 2010, there was no activity in either Obligations Incurred or the Net Cost of Operations.

## OTHER ACCOMPANYING INFORMATION



**T**his section provides additional information regarding the SEC's financial and performance management. It includes a statement prepared by the agency's Office of Inspector General (OIG) summarizing what the OIG considers to be the most serious management and performance challenges facing the agency. The section also includes a response from the SEC's Chairman, outlining the agency's progress in addressing the challenges.

The Summary of Financial Statement Audit and Management Assurances clearly lists each material weakness and non-conformance found and/or resolved during the U.S. Government Accountability Office's (GAO) audit. Additionally, this section provides a detailed explanation of any significant erroneous payments, as required by the Improper Payments Information Act of 2002 as amended.

## Inspector General's Statement on Management and Performance Challenges



UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

### THE INSPECTOR GENERAL'S STATEMENT ON THE U.S. SECURITIES AND EXCHANGE COMMISSION'S MANAGEMENT AND PERFORMANCE CHALLENGES

*As required by the Reports Consolidation Act of 2000 and Office of Management and Budget guidance, I am pleased to submit the following statement summarizing what I consider to be the most serious management challenges facing the Securities and Exchange Commission. This statement has been compiled based on Office of Inspector General audits, investigations, evaluations, and the Office's general knowledge of the agency's operations.*

H. David Kotz  
Inspector General  
September 30, 2011

#### CHALLENGE

#### PROCUREMENT AND CONTRACTING

The Office of Inspector General (OIG) first identified the Securities and Exchange Commission's (SEC or Commission) procurement and contracting function as a management challenge in fiscal year (FY) 2008. While management has reported that improvements were made in the procurement and contracting area during FYs 2010 and 2011, the SEC's efforts in this area have not been completed, and the SEC's procurement and contracting function continues to be a management challenge.

Moreover, work performed by the OIG's investigative unit during FY 2011 demonstrated that there are particular deficiencies in the SEC's processes relating to the use of Justifications for Other than Full and Open Competition. Specifically, on May 16, 2011, the OIG completed an investigation regarding the circumstances surrounding the SEC's entering into a lease for 900,000 square feet of space at a facility located in Washington, D.C., known as Constitution Center. The OIG's Report of Investigation found that after the SEC committed itself to a 10-year lease term at a cost of \$556,811,589 based upon flawed projections of its space needs, the SEC's Office of Administrative Services prepared a Justification and Approval for Other than Full and Open Competition, which the Federal Acquisition Regulation (FAR) requires when an agency decides not to allow for full and open competition on a procurement or lease.

The OIG investigation found that the Justification and Approval to lease space at Constitution Center without competition was inadequate, not properly reviewed, and

backdated. Although the SEC's Competition Advocate signed the Justification and Approval, the OIG investigation found that she did not take sufficient steps to verify that the information in the Justification and Approval was accurate. In addition, the Justification and Approval was not posted publicly within 30 days after contract award as required by the FAR.

The OIG investigation also found that after the SEC's Competition Advocate executed the signature page of the Justification and Approval, she initially backdated her signature to reflect an earlier date and then whited-out a portion of the date of her signature to make it appear that she signed the document nearly a month before she actually did. This action gave the public a false impression about when the SEC finalized the Justification and Approval.

In addition, an OIG report of investigation issued earlier in FY 2011 found that the Justification and Approval for Other than Full and Open Competition used to support the sole source acquisition of approximately \$1 million of information technology equipment relied on an inapplicable provision of the FAR. Similarly, OIG audit reports issued in previous FYs have questioned the propriety of the SEC's use of Justification and Approvals for Other than Full and Open Competition in various circumstances.

Therefore, while the SEC continues to make improvements in the procurement and contracting area, further progress is needed to ensure that the SEC complies fully with all pertinent provisions of the FAR and provides for maximum competition consistent with the requirements of federal laws and regulations.

#### **CHALLENGE                      INFORMATION TECHNOLOGY MANAGEMENT/ INFORMATION SYSTEMS SECURITY**

Information Technology (IT) management continues to be a management challenge for the SEC, although significant improvements have been made in FY 2011. The OIG's *2010 Annual FISMA Executive Summary Report*, Report No. 489, issued March 3, 2011 confirmed that additional improvements are needed in several IT-related areas, specifically relating to Federal Information Security Management Act requirements (e.g., deviations from Federal Desktop Core Configurations), access controls, privacy requirements, and the SEC's continuous monitoring program. During FY 2011, in addition to the Annual FISMA Summary Report, we conducted reviews of two additional areas of IT management and issued the following reports: (1) *Assessment of SEC's Continuous Monitoring Program*, Report No. 497 (issued August 11, 2011), and (2) *Review of SEC Contracts for Inclusion of Language Addressing Privacy Act Requirements*, Report No. 496 (issued July 18, 2011).

In its *2010 Annual FISMA Executive Summary Report*, Report No. 489, the OIG identified concerns with the agency's identification, documentation, and reporting of Federal Desktop Core Configuration requirements to the National Institute of Standards and Technology. Further, this report identified multiple concerns in key areas relating to logical access controls, including the disabling of accounts and oversight of user accounts with elevated privileges.

The OIG's *Assessment of SEC's Continuous Monitoring Program*, Report No. 497, also identified several key areas of concern, including access control, audit and accountability, configuration management, contingency planning, identity and authentication, system and services acquisition, system and communications protection, and system and information integrity.

The OIG's *Review of SEC Contracts for Inclusion of Language Addressing Privacy Act Requirements*, Report No. 496, found that although the sampled SEC's contracts contained language requiring that vendors and their employees comply with the Privacy Act, strengthening the language in SEC contracts pertaining to privacy and information would help to ensure vendors' compliance with those privacy-related provisions and could further reduce the risk that personally identifiable information (PII) will be mishandled.

Additionally, as noted in SEC's FY 2010 Performance & Accountability Report, attention is still needed in specific critical IT areas, such as oversight of IT capital investment, oversight of IT contracts and IT human capital. These key initiatives remain challenges because measures have not been completed to mitigate deficiencies that were identified in the past.

The Office of Information Technology and the Office of the Chief Operating Officer concurred with the recommendations identified in the aforementioned OIG reports and have already begun taking steps to remediate the deficiencies.

## **CHALLENGE**

## **HUMAN RESOURCE MANAGEMENT**

The OIG has identified the SEC's human resource management as a management challenge.

During FY 2011, the OIG conducted audits related to human resource management that identified a number of concerns and the need for increased management controls. Specifically, the OIG issued *Audit of SEC's Employee Recognition Program and Recruitment, Relocation, and Retention Incentives*, Report No. 492, in August 2011, and *Review of Alternative Work Arrangements, Overtime Compensation, and COOP-Related Activities*, Report No. 491 in September 2011.

In OIG Report No. 492, we identified numerous areas in which the Office of Human Resources (OHR) needed to improve its processes related to awards and recruitment, relocation, and retention incentives. Significantly, our audit found that OHR had not fully implemented recommendations pertaining to the SEC's award activities that resulted from a 2007 Office of Personnel Management (OPM) human resources operations audit and, therefore, deficiencies identified in OPM's audit continued to exist.

The OIG's audit also found that there were insufficient resources dedicated to developing and overseeing the SEC's Employee Recognition Program (ERP), and that a large number of sampled awards and recruitment, relocation, and retention incentives lacked

documentary support. The audit also found that OHR lacked updated comprehensive policies and procedures and formal training for awards and incentives. Further, we found that the SEC's budgeting processes for awards and incentives for SEC SK (staff-level) employees was flawed which made it difficult for supervisors to reward employees for outstanding performance in the course of their normal job duties.

In OIG Report No. 491, we determined that several improvements were needed to the SEC's alternative work schedule (AWS), overtime, and telework programs. The OIG audit found that although only three types of AWSs were authorized for SEC employees—Flexitour, 5-4/9 compressed, and 10-4 compressed, SEC employees actually used eight types of AWS in FYs 2008 through 2010. We also determined that, due to the benefits that AWS options provide to employees (i.e., flexibility with respect to their arrival and departure times and the length of workdays within the workweek or pay period), the SEC might benefit from making additional flexible work schedule options officially available to its employees. Our review also found that the SEC did not have a comprehensive manual that addressed the AWS options available to employees. We further determined that the SEC had no official form for employees to use when requesting to participate in AWS programs, and little training on AWS was available to SEC employees.

The OIG audit also found that there was significant confusion with respect to SEC procedures regarding overtime compensation, as well as a lack of formal policies on key issues such as the earning of credit hours by SEC Senior Officers. The audit also identified areas for improvement with respect to the tracking of telework data and ensuring that SEC Continuity of Operations (COOP) personnel have telework agreements in place.

The OIG audits made numerous specific recommendations designed to improve the SEC's operations in the areas reviewed. Agency management concurred with all of the OIG audits' recommendations and indicated that they intend to take steps to remedy the deficiencies.

## **CHALLENGE**

## **FINANCIAL MANAGEMENT**

The GAO's FY 2010 audit of the Commission's financial statements found that they were fairly presented in all material respects, and the GAO found no reportable noncompliance with the laws and regulations tested. However, because of two material weaknesses in internal control it identified, the GAO found that the SEC did not maintain, in all material respects, effective internal control over financial reporting, and thus did not provide reasonable assurance that misstatements, losses, or noncompliance material in relation to the financial statements would be prevented or detected and corrected on a timely basis.

The GAO defines a material weakness as a deficiency or combination of deficiencies in internal control, such that there is a reasonable possibility that a material misstatement of the financial statements will be not be prevented, or detected and corrected on a timely

basis. A significant deficiency is a deficiency, or combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by management. The material weaknesses identified by the GAO included (1) information systems controls, and (2) controls over financial reporting and accounting processes.

The GAO has identified pervasive deficiencies in the design and operation of the SEC's information security and other system controls that span across its general support system and all key applications that support financial reporting. Many of these deficiencies have existed since SEC began preparing financial statements in FY 2004. The identified deficiencies jeopardize the confidentiality, availability, and integrity of information processed by SEC's key financial reporting systems and pose a risk of material misstatement in financial reporting. The continuing and newly-identified general and application control deficiencies are in the areas of (1) security management, (2) access controls, (3) configuration management, (4) segregation of duties, and (5) contingency planning. The significant deficiencies that collectively comprise a material weakness over financial reporting and accounting processes concern internal control over (1) the financial reporting process, (2) budgetary resources, (3) registrant deposits, (4) disgorgement and penalties, and (5) required supplementary information. In addition, the GAO identified other deficiencies in internal controls that although not considered material weaknesses or significant deficiencies, could adversely affect the Commission's ability to meet financial reporting and other internal control objectives. These deficiencies concerned the Commission's (1) proper and timely approvals of disbursements, (2) review of service providers' auditor reports, and (3) controls over travel transactions.

The GAO also reported that it continued to find ineffective automated controls for the SEC's general ledger system and supporting applications, and ineffective security controls over the databases and supporting processes used to generate and maintain the SEC's financial reports. Many of the SEC's key financial reporting applications occurred manually outside the general ledger system through the use of spreadsheets and databases because many of the SEC's key financial system applications did not automatically interface with the general ledger system. Further, the SEC's general ledger system and certain software applications and configurations lacked the capacity to timely and accurately generate and report information needed to prepare financial statements and manage operations on an ongoing basis. Until these system deficiencies, limitations, and vulnerabilities are addressed, the SEC cannot rely on the internal controls contained in its automated accounting system and supporting financial applications systems to provide reasonable assurance that, in the absence of effective compensating procedures, (1) its financial statements, taken as a whole, are fairly stated; (2) the information the SEC relies on to make decisions on a daily basis is accurate, complete, and timely; and (3) sensitive data and financial information are appropriately safeguarded.

The OIG also conducted work in the financial management area in FY 2011. Specifically, in March 2011, the OIG issued *Audit of the SEC Budget Execution Cycle*, Report No. 488, which identified numerous concerns in the SEC's budgeting process.

The audit's findings included: (1) by alternating between two separate appropriations, the SEC may have violated federal law pertaining to the purpose of appropriations and, as a consequence, the Antideficiency Act; (2) the SEC inactivated budgetary controls in the Momentum financial to facilitate processing payroll transactions, which could lead to a violation of the Antideficiency Act; (3) the SEC's Budget and Program Performance Analysis System (BPPAS) was not configured to accept more than one appropriation; (4) the Office of Financial Management (OFM) did not have a formal budgetary training program; (5) OFM did not require written authorization of reprogramming and realignment actions between budget object classes; and (6) OFM did not sufficiently track the reprogramming and realignment of funds. The OIG made nine specific and concrete recommendations to correct the deficiencies found in the audit. OFM agreed to all of the recommendations and has taken significant steps to address them.

## **CHALLENGE**

## **ETHICS**

The OIG has identified the SEC's Ethics program as a management challenge.

In January 2011, the OIG issued a report of investigation in response to a Congressional request regarding whether a senior employee had violated conflict-of-interest restrictions in connection with employment at a trading firm. While the OIG's investigation found no evidence that the former employee violated conflict-of-interest provisions or acted inappropriately in connection with employment at the trading firm, the OIG investigation did find deficiencies in the agency's ethics procedures, including a lack of proper record keeping. The OIG's report made several recommendations for improvement to the SEC Ethics Office, including that it document the advice provided to SEC employees.

In September 2011, the OIG completed an investigation of potential conflicts of interest arising from the participation of the SEC's former General Counsel and Senior Policy Director in determining the SEC's position in the liquidation proceeding brought by the Securities Investor Protection Corporation (SIPC) of Bernard L. Madoff Investment Securities, LLC (BMIS). After the SEC charged BMIS and Bernard L. Madoff with securities fraud, SIPC determined that BMIS customers were in need of certain protections against losses that are provided through a reserve fund that is used to restore money to investors who have assets with bankrupt or financially troubled brokerage firms.

The OIG investigation found that the former General Counsel and Senior Policy Director participated personally and substantially in particular matters in which he had a personal financial interest by virtue of his inheritance of the proceeds of his mother's estate's Madoff account and that the matters on which he advised could have directly impacted his financial position.

The OIG investigation further found that the SEC's former General Counsel and Senior Policy Director had sought ethics advice from the former SEC Ethics Counsel who advised him that he did not have a financial conflict of interest. We found that the former SEC Ethics Counsel's advice was based upon several incorrect assumptions and did not

document the consideration of whether the former SEC's General Counsel and Senior Policy Director's actions constituted an appearance of impropriety. We also found that the former Ethics Counsel reported directly to the former General Counsel and Senior Policy Director, who had given the former Ethics Counsel a performance evaluation just seven months after the ethics advice was provided.

The OIG investigation also found that the Ethics Office considered the former General Counsel and Senior Policy Director's participation differently when matters other than the Madoff liquidation proceeding were involved. In addition, the OIG investigation found that the Ethics Office considered recusals in Madoff-related matters differently in situations that did not involve the former General Counsel and Senior Policy Director, and took a more conservative approach for recusal from Madoff-related matters with respect to other employees in the Office of General Counsel. These findings raised concerns about the consistency of the advice being provided by the SEC Ethics Office.

The OIG Report of Investigation made the following three recommendations with respect to the Ethics Office:

- (1) The SEC Ethics Counsel should report directly to the Chairman, rather than to the General Counsel.
- (2) The SEC Ethics Office should take all necessary steps, including the implementation of appropriate policies and procedures, to ensure that all advice provided by the Ethics Office is well-reasoned, complete, objective, and consistent, and that Ethics officials ensure that they have all the necessary information in order to properly determine if an employee's proposed actions may violate rules or statutes or create an appearance of impropriety.
- (3) The SEC Ethics Office should take all necessary actions to ensure that all ethics advice provided in significant matters, such as those involving financial conflict of interest, are documented in an appropriate and consistent manner.

The SEC Ethics Office has indicated that it intends to implement all three recommendations and take the necessary steps to improve the SEC ethics program.

## Management's Response to Inspector General's Statement



THE CHAIRMAN

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

November 14, 2011

Mr. H. David Kotz, Inspector General  
Office of the Inspector General  
U.S. Securities and Exchange Commission  
100 F Street, NE  
Washington, DC 20549

Dear Mr. Kotz:

Thank you for your "Statement on the U.S. Securities and Exchange Commission's Management and Performance Challenges" issued on September 30, 2011. I appreciate your views and the perspective they provide on the issues facing the agency. We are very focused on the challenges identified in your statement, as well as on a number of other initiatives to strengthen our operations and better protect investors.

We agree with your assessment of the challenges facing the Securities and Exchange Commission (SEC). We also appreciate your acknowledgement of the important progress that the SEC has achieved during the past year. A brief description of the actions—already taken and planned to be taken—to address each of the challenges is provided below.

### **Procurement and Contracting**

The SEC is committed to ensuring that its acquisitions and contract oversight processes are effective and efficient. The agency has made significant improvements in the procurement and contracting area in the past year, and strengthening the procurement and contracting function will remain a significant focus of management attention during FY 2012. Key focus areas are in retaining qualified and certified acquisition staff, steadily improving data management, and strengthening financial controls.

In FY 2011, the SEC completed its transition to an automated procurement system (PRISM), which has strengthened program controls by permitting end-to-end tracking and management of procurements and contracts. The SEC also has made major progress toward replacing its core financial system with one offered by a Federal Shared Service Provider (FSSP), which will be integrated with the procurement and contracting system. This will offer the opportunity to further improve controls relating to the procurement and contracting function, as compared to the current process that is dependent upon significant manual reconciliations.

During FY2011, the SEC has completely revised leasing policies and procedures for the leasing process and entered into a Memorandum of Understanding with the General Services Administration to procure and manage all new leases for real property.

Mr. H. David Kotz  
Page 2

Also during the year, the SEC's Office of Administrative Services (OAS), which oversees the agency's procurement and contract management functions, issued new internal regulations to strengthen internal controls over interagency agreements, contract administration, and leasing procurements. OAS also issued guidance to its acquisitions staff regarding proper procedures for maximizing competition and considering requests to limit competition. In addition, all acquisition personnel completed training in competition requirements. A new Competition Advocate was designated, and the Office of General Counsel began reviewing in advance significant justifications for other than full and open competition. Further, the Head of SEC's Contracting Activity personally reviewed, approved justifications, and instituted rigorous review procedures to assure that competition is limited only when is sufficient reason.

The SEC is also conducting a comprehensive assessment of operations that includes the procurement and contracting functions. The assessment is, among other things, examining the organizational structure, decision-making processes, reporting relationships, quality controls, and staffing levels. The review seeks further improvements in efficiency, internal controls, and cost reduction through improving workforce knowledge, skills, and abilities. The review is expected to be completed this fall.

#### **Information Technology Management/Information Systems Security**

The SEC continues to work intently to achieve compliance with Federal Information Security Management Act (FISMA) requirements. During the year, the SEC's Office of Information Technology (OIT) identified and submitted to the National Institute of Standards and Technology (NIST), as required, Federal Desktop Core Configuration requirement exceptions. The SEC also acquired tools to regularly monitor for compliance with these requirements. Further, OIT conducted a thorough review of all accounts to determine whether the appropriate privilege levels were justified and disabled accounts that were no longer required. This list of users with elevated privileges is maintained and updated on a regular basis. OIT also updated procedures for disabling unneeded accounts and provided training for those staff tasked with administering those procedures. Efforts are currently underway to implement tools to assist in automating these processes. In addition, work continues to integrate logical access controls into the SEC's HSPD-12 program.

Also during FY2011, the SEC continued to make improvements in the Continuous Monitoring Program. In September 2011, NIST released its guidelines for *Information Security Continuous Monitoring for Federal Information Systems and Organizations* (SP 800-137). The SEC is in the process of revising its program to come into compliance with those guidelines and updating controls to address the findings in the OIG's September 2011 report on the agency's Continuous Monitoring Program. In addition, OIT has provided guidance to OAS to help strengthen privacy and security requirements in service contracts handling personally identifiable information.

Finally, the SEC continues to make progress in the capital planning and investment control (CPIC) area. Over the past year, the agency successfully closed all outstanding audit items related to capital planning. OIT addressed policy, procedure, and documentation issues as

Mr. H. David Kotz  
Page 3

required. We also had a cross-organizational team that streamlined the CPIC process and implemented changes to improve acquisition and enterprise architecture involvement in the process.

### **Human Resources Management**

The SEC's Office of Human Resources (OHR) is working to strengthen controls related to human resources management. Immediately after receipt of the OIG's report on the *SEC's Employee Recognition Program and Recruitment, Relocation, and Recruitment Incentives*, published in September 2011, OHR assigned responsibility for the Employee Recognition Program to its Employee and Labor Relations team; defined, documented, and communicated procedures for the special act award process as part of the budget allocation process this fiscal year; and implemented an internal review process to regularly audit a sample of processed awards for compliance and to ensure documentation is accessible. As OHR works to implement the remainder of the report's recommendations, opportunities for management to provide monetary awards based on performance are being explored in conjunction with other current initiatives, such as the performance management system implementation, assessment of SEC's compensation strategy, and collective bargaining agreement (CBA) negotiations with the National Treasury Employees Union.

Also during FY 2011, OHR made improvements to the SEC's alternative work schedule and telework programs. As highlighted in the OIG's September 2011 report, *Review of Alternative Work Arrangements, Overtime Compensation, and COOP-Related Activities at the SEC*, efforts were already underway to strengthen controls in this area and continued during the audit process. These efforts include, among other things, developing a new handbook that addresses alternative work schedule options that are available to employees. Because the SEC's telework options are subject to the current Collective Bargaining Agreement negotiations, and OHR will continue to assess any potential impact on the program as that process continues. OHR is also reviewing its policies and procedures to provide clarity in certain program areas, such as overtime compensation and the earning of credit hours by SEC Senior Officers.

Finally, OHR has efforts underway to revise all related policies and procedures to ensure regulatory compliance and efficient management of these programs. As the revisions are finalized, OHR will ensure that they are effectively communicated to SEC management and employees, as appropriate, to promote compliance and consistency within these program areas.

### **Financial Management**

In FY 2011, the SEC succeeded in remediating both material weaknesses noted in the Inspector General's Statement in internal controls over financial reporting from FY 2010. The agency completed this achievement by working on several fronts to improve financial management practices and strengthen internal controls in the areas of financial operations, financial systems, and budget cycle controls. These efforts are described further below.

Mr. H. David Kotz  
Page 4

### *Financial Operation Improvements*

In FY 2011, the SEC undertook several significant steps to strengthen financial controls. These efforts included:

- Conducting a comprehensive assessment of the spreadsheets and databases used by the agency, and tightening controls over those applications based on risk;
- Evaluating and improving processes for reviewing filing fees paid by registrants, and significantly reducing our backlog of inactive registrant accounts;
- Eliminating a backlog of offering and verification reviews of fees paid on registrant filings;
- Tightening controls over the recording of subsequent orders, post-judgment interest, and deposits-in-transit related to disgorgements and penalties;
- Formalizing the process for performing annual assessments to ensure that financial statements and disclosures comply with all relevant requirements;
- Bolstering the controls related to the use of miscellaneous obligating documents; and
- Strengthening our process for de-obligating funds from completed contracts, and ensuring that appropriate accounting adjustments are recognized.

### *Financial Systems*

In order to ensure our financial controls are sustainable over the long term, the agency will continue to make significant investments in our financial systems. The SEC is transitioning to a Federal Shared Service Provider (FSSP) model, with the Department of Transportation's Enterprise Services Center (ESC). The ESC has successfully served multiple federal agencies, including various components of the Department of Transportation, the Government Accountability Office, and the Commodity Futures Trading Commission. Through this initiative, the SEC will enhance functionality, automate some of its manual processes, and bolster financial management and reporting.

Working closely with the Department of Transportation, the SEC made significant progress in FY 2011 in the effort to migrate its financial system to the FSSP. The effort is on track for a cut-over to the new system in April 2012.

In FY 2011, the SEC also made tremendous progress in the security over its financial systems, successfully eliminating the material weakness in information systems from the previous year. The agency's efforts included strengthening user access controls, updating security patches on SEC systems, and remediating self-identified security deficiencies. These

Mr. H. David Kotz  
Page 5

efforts have not only significantly strengthened the agency's security posture in the short term, but will also help ensure proper SEC procedures in the FSSP environment.

#### *Budget Cycle Controls*

The OIG issued audit 488, *Audit of the SEC Budget Cycle*, on March 29, 2011. The SEC has closed eight of the nine recommendations identified in the audit report, and the remaining recommendation is expected to be closed shortly. Among the remediation actions taken by OFM are the following:

- Developing policies and procedures for handling situations in which the agency receives more than one appropriation;
- Requesting an interpretation of the Purpose Statute from the Comptroller General;
- Improving controls over budgetary control overrides;
- Establishing a training program for budget analysts in consultation with OHR; and
- Strengthening procedures for budget reprogramming and realignments.

#### *Ongoing Efforts*

In FY 2012, the SEC will continue to focus resources on a successful transition to the Department of Transportation's financial system, called Delphi. The SEC's Office of Financial Management also is undergoing an external organizational assessment, and will implement steps to optimize the organizational structure and skill sets needed as the Delphi migration commences. In addition, OFM will continue to address the backlog of dormant registrant deposit accounts, strengthen the efficiency of its disgorgements and penalties processes, and improve the timeliness of its de-obligations of undelivered orders. The SEC is committed to investing the time and energy to ensure that its internal controls over financial reporting are on a strong, sustainable path.

#### **Ethics**

Ensuring that the agency has the strongest possible ethics program is a top priority. Over the past two years, we have made changes to the structure, function, and personnel of the SEC's Ethics Office. We have brought new leadership into our Ethics Office, elevated the profile of the Ethics Office across the agency, emphasized the personal responsibility that each employee carries to avoid a conflict or the appearance of a conflict, and taken steps to address potential conflicts of interest that can arise when employees seek post-SEC employment.

Mr. H. David Kotz  
Page 6

In response to the OIG's recommendations on ways to further improve the agency's ethics program, we have undertaken a number of immediate steps, including the following:

- The SEC Ethics Counsel now reports to me rather than the General Counsel.
- The Ethics Counsel has issued a memorandum to all ethics attorneys regarding procedures to ensure that all advice provided by the Ethics Office is well-reasoned, complete, objective, and consistent, and that ethics officials ensure that they have all the necessary information in order to properly determine if an employee's proposed actions may violate rules or statutes or create an appearance of impropriety. These procedures include, *inter alia*:
  - Review each request for ethics advice and any relevant information or materials submitted along with the request, giving particular attention to determining whether the request involves a "particular matter" and, if so, the scope of the particular matter.
  - Request additional facts as needed in order to render the requested advice, which may include reaching out to the requestor or other sources within the agency for additional relevant facts.
  - If the question is novel, complex, or relates to an unsettled area of law, consult with others to ensure that the advice given is accurate and consistent with past advice.
  - Consider consulting with others if the request relates to the participation of senior employees in matters in which he or she may have a financial interest.
- The Ethics Office has dramatically increased documentation of advice by instituting several procedures including:
  - Using hard copy checklists to record advice given regarding conflicts while seeking employment or post-employment conflicts;
  - Creating a database in which the office can store significant advice;
  - Instructing each ethics attorney to create a mailbox regarding seeking/post employment advice into which advice can be archived; and
  - Creating Memoranda to File to memorialize advice.
- The Ethics Counsel has issued a Memorandum to all ethics attorneys regarding documentation procedures as well as issuing "Standards for Documenting Advice on Employment Issues." These procedures include, *inter alia*, an instruction that each

Mr. H. David Kotz  
Page 7

attorney memorialize in writing “significant advice” on complex, novel, or otherwise significant questions. Significant advice includes the following:

- Certain advice relating to post-employment issues and seeking employment issues;
  - Advice given to senior officials relating to potential conflicts of interest;
  - Advice relating to particularly sensitive pending Commission matters;
  - Advice involving novel legal issues or factual patterns;
  - Advice involving unsettled areas of law;
  - Advice that has required a substantial amount of legal research, factual inquiries, or other commitment of Ethics Office resources;
  - Advice that relates to questions likely to recur for other SEC employees; and
  - Any other advice for which a permanent written record would be useful in ensuring that the Ethics Office provides consistent advice.
- In addition, we have taken the following additional steps to improve the SEC’s ethics program:
    - The Ethics Counsel, whom I hired last year and who has undertaken a top-to-bottom review of our ethics program, has established a number of additional controls to ensure the proper documentation of conflicts advice within the office.
    - Even before receiving these recent recommendations from the Inspector General, our new Ethics Counsel had made a number of changes aimed at improving the quality and consistency of advice given to SEC employees. Among other things, my office has worked with the Ethics Office to:
      - institute strong post-employment controls, including requiring all departing employees to receive an ethics post-employment briefing and a packet of post-employment materials before leaving the agency;
      - increase requirements for counseling regarding seeking employment and related conflicts issues; and
      - increase education regarding conflicts and employee responsibility.
  - Finally, the Ethics Office has increased its communications with the U.S. Office of Government Ethics on complex ethics matters, helping to ensure that the office’s advice is accurate and consistent agency-wide.

Mr. H. David Kotz  
Page 8

I hope that the actions outlined in this letter demonstrate our commitment to strengthening internal controls and improving the agency's performance. We look forward to working with you to further address these challenges.

Sincerely,

A handwritten signature in black ink that reads "Mary L. Schapiro". The signature is written in a cursive, flowing style.

Mary L. Schapiro  
Chairman

## Summary of Financial Statement Audit and Management Assurances

**TABLE 3.1**  
**SUMMARY OF FINANCIAL STATEMENT AUDIT**

**Audit Opinion:** Unqualified  
**Restatement:** No

<b>Material Weaknesses</b>	<b>Beginning Balance</b>	<b>New</b>	<b>Resolved</b>	<b>Consolidated</b>	<b>Ending Balance</b>
Internal Control over Financial Reporting	2	—	2	—	—
<b>Total Material Weaknesses</b>	<b>2</b>	<b>—</b>	<b>2</b>	<b>—</b>	<b>—</b>

**TABLE 3.2**  
**SUMMARY OF MANAGEMENT ASSURANCES**

### Effectiveness of Internal Control over Financial Reporting (FMFIA § 2)

**Statement of Assurance:** Unqualified

<b>Material Weaknesses</b>	<b>Beginning Balance</b>	<b>New</b>	<b>Resolved</b>	<b>Consolidated</b>	<b>Reassessed</b>	<b>Ending Balance</b>
Internal Control over Financial Reporting	2	—	2	—	—	—
<b>Total Material Weaknesses</b>	<b>2</b>	<b>—</b>	<b>2</b>	<b>—</b>	<b>—</b>	<b>—</b>

### Effectiveness of Internal Control over Operations (FMFIA § 2)

**Statement of Assurance:** Unqualified

<b>Material Weaknesses</b>	<b>Beginning Balance</b>	<b>New</b>	<b>Resolved</b>	<b>Consolidated</b>	<b>Reassessed</b>	<b>Ending Balance</b>
Total Material Weaknesses	2	—	2	—	—	—

### Conformance with Financial Management System Requirements (FMFIA § 4)

**Statement of Assurance:** Conformance

<b>Material Weaknesses</b>	<b>Beginning Balance</b>	<b>New</b>	<b>Resolved</b>	<b>Consolidated</b>	<b>Reassessed</b>	<b>Ending Balance</b>
Federal Financial Management System Requirements	1	—	1	—	—	—
<b>Total Non-Conformances</b>	<b>1</b>	<b>—</b>	<b>1</b>	<b>—</b>	<b>—</b>	<b>—</b>

## Improper Payments Elimination and Recovery Act Reporting Details

The Improper Payments Information Act (IPIA) of 2002, as amended by the Improper Payments Elimination and Recovery Act (IPERA) of 2010, requires agencies to review all programs and activities they administer and identify those which may be susceptible to significant erroneous payments. For all programs and activities in which the risk of erroneous payments is significant, agencies are to estimate the annual amount of erroneous payments made in those programs. The Office of Management and Budget (OMB) guidance provided in Circular A-136 and Appendix C of Circular A-123 require detailed information related to SEC's Improper Payments Elimination Program, which is provided below.

### Risk Assessment

In fiscal year (FY) 2011, the U.S. Securities and Exchange Commission (SEC) reviewed the programs and activities it administers to identify those which may be susceptible to significant erroneous payments. The risk assessment included 1) consideration of certain risk factors that are likely to contribute to a susceptibility to significant improper payments, and 2) transaction testing on a sample basis of payments made during the first six months of FY 2011. The risk assessment was performed for the following programs:

- Vendor payments (includes travel and credit card payments);
- Disbursement and penalty distributions (made by SEC to fund and tax administrators and directly to harmed investors); and
- Returned deposits of registration filing fees under Section 6b of the Securities Act of 1933 and Sections 13 and 14 of the Securities Exchange Act of 1934.

Based on the results of transaction testing applied to a sample of payments, consideration of risk factors, and reliance on the internal controls in place over the payment, refund and distribution process, the SEC determined that none of its programs and activities are susceptible to significant improper payments at or above the threshold levels set by OMB. Significant erroneous payments are defined as annual erroneous payments in the program exceeding both \$10 million and 2.5 percent or

\$100 million of total annual program payments. In accordance with Appendix C of Circular A-123, the SEC is not required to determine a statistically valid estimate of erroneous payments or develop a corrective action plan if the program is not susceptible to significant improper payments.

In FYs 2007 and 2008, SEC's testing of its largest programs resulted in improper payment percentages that were well below one-half percent and less than \$30,000 for each program. In FY 2009 and 2010, the SEC performed a risk assessment for all programs and determined that its programs are not susceptible to significant erroneous payments.

Since the level of risk in each program is determined to be low and baseline estimates have been established, the SEC is only required to conduct a formal risk assessment every three years unless the program experiences a significant change in legislation and/or a significant increase in funding level. The SEC will conduct a follow on review in FY 2012 of its programs and activities to determine whether the programs have experienced any unexpected changes in legislation or funding levels. If so, the SEC will re-assess the programs' risk susceptibility and make a statistically valid estimate of erroneous payments for any programs determined to be susceptible to significant erroneous payments.

### Recapture of Improper Payments

The SEC does not administer grant, benefit or loan programs. Implementation of recapture auditing, if determined to be cost-effective, would apply to vendor payments, disgorgement and penalty distributions, and refunds of registration filing fee deposits. Because the definition of payment in the new IPERA legislation means any payment or transfer of Federal funds to any non-Federal person or entity, the SEC is not required to review, and has not reviewed, intra-governmental transactions and payments to employees.

The SEC has determined that implementing a payment recapture audit program for vendor payments, disgorgement and penalty distributions, and refunds of registration filing fee deposits is not cost-effective. That is, the benefits or recaptured amounts associated with implementing and overseeing the program do not exceed the costs, including staff time and

resources, or payments to a contractor for implementation, of a payment recapture audit program. In making this determination, the SEC considered its low improper payment rate based on testing conducted over the past four years. The SEC also considered whether sophisticated software and other cost-efficient matching techniques could be used to identify significant overpayments at a low cost per overpayment, or if labor intensive manual reviews of paper documentation would be required. In addition, the SEC considered the availability of tools to efficiently perform the payment recapture audit and minimize payment recapture audit costs.

The SEC will continue to monitor its improper payments across all programs and activities it administers and assess whether implementing payment recapture audits for each

program is cost-effective. If through future risk assessments the agency determines a program is susceptible to significant improper payments and implementing a payment recapture program may be cost-beneficial, the SEC will implement a pilot payment recapture audit to measure the likelihood of cost-effective payment recapture audits on a larger scale.

Even though the SEC has determined that implementing a payment recapture audit program for its programs is not cost-effective, the agency strives to recover any overpayments identified through other sources, such as payments identified through statistical samples conducted under the IPIA. The amounts identified and recovered, by program, are shown in Table 3.3 below.

**TABLE 3.3**  
**OVERPAYMENTS RECAPTURED OUTSIDE OF PAYMENT RECAPTURE AUDITS (IN DOLLARS)**

Source	Amount Identified (CY)	Amount Recovered (CY)	Amount Identified (PYs)	Amount Recovered (PYs)	Cumulative Amount Identified (CY+PYs)	Cumulative Amount Recovered (CY+PYs)
Vendor Payments						
Improper Payments Sampling	\$ 4.45	\$ —	\$12,758.40	\$12,755.86	\$12,762.85	\$12,755.86
Disbursement and Penalty Distributions						
Improper Payments Sampling	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —
Refunds of Registration Filing Fee Deposits						
Improper Payments Sampling	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —

## Appendix A: Chairman and Commissioners

### Mary L. Schapiro

CHAIRMAN



Mary L. Schapiro is the 29th Chairman of the U.S. Securities and Exchange Commission. Chairman Schapiro was appointed by President Barack Obama on January 20, 2009, unanimously confirmed by the U.S. Senate, and sworn in on January 27, 2009. She is the first woman to serve as the agency's permanent Chairman.

Chairman Schapiro's priorities at the SEC include shaping a more effective and responsive agency; better protecting investors by implementing financial reform legislation and enhancing the structure of America's financial markets; and reinforcing the agency's commitment to enforcement, transparency, and disclosure.

Prior to becoming SEC Chairman, she was CEO of the Financial Industry Regulatory Authority (FINRA) – the largest non-governmental regulator for all securities firms doing business with the U.S. public. Chairman Schapiro joined the organization in 1996 as President of the National Association of Securities Dealers (NASD) Regulation. In 2006, she was named NASD's Chairman and CEO. The following year, she led the organization's consolidation with New York Stock Exchange (NYSE) Member Regulation to form FINRA.

In 1994, Chairman Schapiro was appointed by President Bill Clinton as Chairman of the Commodity Futures Trading Commission, a position she held until joining NASD.

Chairman Schapiro has received appointments to the Commission from four presidents. She was first appointed as a commissioner by President Ronald Reagan in 1988 and was re-appointed a by President George H.W. Bush the following year, before being named acting Chairman by President Clinton in 1993.

A 1977 graduate of Franklin and Marshall College in Lancaster, Pennsylvania, Chairman Schapiro earned a Juris Doctor degree (with honors) from George Washington University in 1980.

**Elisse B. Walter**

COMMISSIONER



Elisse B. Walter was appointed by President George W. Bush to the U.S. Securities and Exchange Commission and sworn in on July 9, 2008. Under designation by President Barack Obama, she served as Acting Chairman during January 2009.

Prior to her appointment as an SEC Commissioner, Ms. Walter served as Senior Executive Vice

President, Regulatory Policy & Programs, for FINRA. She held the same position at NASD before its 2007 consolidation with NYSE Member Regulation.

Ms. Walter coordinated policy issues across FINRA and oversaw a number of departments including Investment Company Regulation, Member Education and Training, Investor Education, and Emerging Regulatory Issues. She also served on the Board of Directors of the FINRA Investor Education Foundation.

Prior to joining NASD, Ms. Walter served as the General Counsel of the Commodity Futures Trading Commission. Before joining the CFTC in 1994, Ms. Walter was the Deputy Director of the Division of Corporation Finance of the Securities and Exchange Commission. She served on the SEC's staff beginning in 1977, both in that division and in the Office of the General Counsel. Before joining the SEC, Ms. Walter was an attorney with a private law firm.

Ms. Walter is a member of the Academy of Women Achievers of the YWCA of the City of New York and the inaugural class of the ABA's DirectWomen Institute. She also has received, among other honors, the Presidential Rank Award (Distinguished), the SEC Chairman's Award for Excellence, the SEC's Distinguished Service Award, and the Federal Bar Association's Philip Loomis and Manuel F. Cohen Younger Lawyer Awards.

She graduated from Yale University with a B.A., cum laude, in mathematics and received her J.D. degree, cum laude, from Harvard Law School. Ms. Walter is married to Ronald Alan Stern, and they have two sons, Jonathan and Evan.

**Luis A. Aguilar**

COMMISSIONER



Luis A. Aguilar was sworn in as a Commissioner at the U.S. Securities and Exchange Commission on July 31, 2008. Prior to this appointment, Mr. Aguilar was a partner with the international law firm of McKenna Long & Aldridge, LLP, specializing in securities law.

Commissioner Aguilar's previous experience includes

serving as the General Counsel, Executive Vice President, and Corporate Secretary of INVESCO. He also served as INVESCO's Managing Director for Latin America in the late 1990s. Additionally, his career includes tenure as a partner at several prominent national law firms and as an attorney at the U.S. Securities and Exchange Commission.

Commissioner Aguilar represents the Commission as its liaison to both the North American Securities Administrators Association (NASAA) and to the Council of Securities Regulators of the Americas (COSRA). In addition, Commissioner Aguilar served as the SEC's primary sponsor of the SEC's first Investor Advisory Committee. Commissioner Aguilar has been listed in the 2005, 2006, 2007, and 2008 editions of the *Best Lawyers in America* and was named by *Hispanic Business Magazine* in 2006 as one of the "100 Influential" Hispanics in the United States. Additionally, he was named Member of the Year in 2005 and the Atlanta Hispanic Businessman of the Year in 1994 by Georgia Hispanic Chamber of Commerce. He received the Mexican American Legal Defense and Educational Fund's "Excellence in Leadership" Award in April 2005. He was also named the 2005 Latino Attorney of the Year by the Hispanic National Bar Association.

He has been active in numerous civic and business associations. From May 2005 to May 2007, he chaired the Latin American Association. He has served on various Boards, including the Mexican American Legal Defense and Education Fund, Girl Scouts Council of Northwest Georgia, Inc., Georgia Hispanic Bar Association, United States Fund for UNICEF Southeast Regional Chapter, and Hispanic National Bar Association.

Commissioner Aguilar is a graduate of the University of Georgia School of Law, and also received a master of laws degree in taxation from Emory University.

Commissioner Aguilar serves as sponsor of the SEC's Hispanic Employment Committee, the African American Council, and the Caribbean American Heritage Committee.

### **Troy A. Paredes**

COMMISSIONER



Commissioner Paredes was appointed by President George W. Bush to the U.S. Securities and Exchange Commission and sworn in on August 1, 2008.

Before joining the SEC, Commissioner Paredes was a tenured professor at Washington University School of Law in St. Louis, Missouri. He also held a courtesy appointment at

Washington University's Olin Business School.

While a professor, Commissioner Paredes made presentations around the country on securities law and corporate governance, and he served as an expert on various legal matters. In addition, he has researched numerous topics such as executive compensation; hedge funds; private placements; the allocation of control within firms among directors, officers, and shareholders; the psychology of corporate and regulatory decision making; behavioral finance; alternative methods of regulation and market-based approaches to corporate accountability and securities regulation; comparative corporate governance, including the development of corporate governance and securities law systems in emerging markets; and the law and business of commercializing innovation. His scholarly work, among other things, has advocated for rigorous cost-benefit analysis when regulating and emphasized the need for accessible and understandable disclosures that investors can use effectively.

As a professor, Commissioner Paredes has authored many articles, and he is also a co-author (beginning with the 4th edition) of a multi-volume securities regulation treatise with Louis Loss and Joel Seligman, entitled *Securities Regulation*.

Before joining the Washington University faculty in 2001, Commissioner Paredes practiced law at prominent national law firms. As a practicing lawyer, he worked on a variety of transactions and legal matters involving financings, mergers and acquisitions, and corporate governance.

He graduated from the University of California at Berkeley with a bachelor's degree in economics in 1992. He went on to graduate from Yale Law School in 1996.

## Appendix B: Major Enforcement Cases

### Introduction

A vigorous enforcement program is at the heart of the U.S. Securities and Exchange Commission's (SEC's) efforts to protect investors and promote the integrity of the securities markets. As the SEC's largest division, the Division of Enforcement investigates potential violations of the Federal securities laws and brings civil charges in Federal district court and administrative proceedings. Successful enforcement actions result in sanctions that protect investors, both now and in the future, such as penalties and the disgorgement of ill-gotten gains that are returned to harmed investors, as well as barring wrongdoers from working in the securities industry.

Over the last two years, the Division of Enforcement carried out the most significant structural reforms of the enforcement program since its inception in 1972 – reforms designed to maximize resources and enable the SEC to more effectively combat securities fraud. Highlights of this programmatic transformation included the launch of five national specialized investigative units dedicated to high-priority areas of enforcement including Asset Management (hedge funds, investment advisers and private equity); Market Abuse (high-volume and computer-driven trading strategies, large-scale insider trading by market professionals and others, and market manipulation schemes); Structured and New Products (various derivative products); Foreign Corrupt Practices Act violations; and Municipal Securities and Public Pensions. In addition, the SEC's home and regional offices are undertaking efforts to focus on targeted areas of concern. This includes creation of the Cross-Border Working Group, a multi-office initiative focusing on accounting and financial statement fraud by U.S. issuers with significant overseas operations, and the establishment of the Microcap Fraud Working Group, which is identifying new strategies to combat manipulation in the trading of over-the-counter securities. Similar specialization initiatives are ongoing in various SEC offices. All of these efforts are utilizing enhanced training, specialized industry experience and skills, and targeted investigative approaches to detect as early as possible any links and patterns that may reflect wrongdoing and ultimately to conduct more efficient and effective investigations.

This section highlights some of the significant enforcement cases filed by the SEC in fiscal year (FY) 2011. For further information on selected enforcement cases, please see "Litigation Releases" at <http://www.sec.gov/litigation/litleases.shtml>.

### Actions Related to the Financial Crisis

A significant priority for the SEC remains to identify and hold accountable firms and individuals who committed securities law violations linked to the financial crisis. To date, the SEC has filed 36 enforcement actions involving misconduct generally associated with the financial crisis, including: (a) concealing from investors risks, terms and improper pricing of collateral debt obligations (CDOs) and other complex structured products; (b) misleading investor disclosures about mortgage-related risks and exposure; and (c) concealing the extent of risky mortgage-related and other high-risk investments in mutual funds and other financial products. Fifteen of those actions were filed in FY 2011, a 25 percent increase over FY 2010.

These financial-crisis related cases have charged 81 individuals and entities, including 39 Chief Executive Officers (CEOs), Chief Financial Officers (CFOs) and other senior corporate officers. In addition, 24 such persons have been barred from the securities industry, from serving as officers and directors and/or from appearing before the Commission. Moreover, more than \$1.97 billion of monetary relief has been ordered in these cases, most of which has or will be returned to harmed investors.

The significant actions filed in this area include an action filed against J.P. Morgan Securities, LLC for misleading investors in a complex mortgage securities transaction just as the housing market was starting to plummet.<sup>1</sup> The SEC alleged that J.P. Morgan structured and marketed a synthetic CDO without informing investors that a hedge fund helped select the assets in the CDO portfolio and had a short position in more than half of those assets. As a result, the hedge fund was poised to benefit from the default of the CDO assets it selected. In a settlement of this action, J.P. Morgan agreed to pay \$153.6 million and to improve its processes for the

<sup>1</sup> *SEC v. J.P. Morgan Securities, LLC, Lit. Rel. No. 22008 (June 21, 2011)* <http://www.sec.gov/litigation/litreleases/2011/lr22008.htm>

review and approval of mortgage securities transactions. The settlement resulted in the full return of losses to harmed investors. J.P. Morgan also agreed to return more than \$56 million to investors in a second CDO. In a related action, the SEC separately charged Edward S. Steffelin who headed the team at an investment advisory firm responsible for selecting the CDO portfolio. The litigation against Steffelin is ongoing.

In another action, the SEC charged Wells Fargo Securities LLC, formerly known as Wachovia Capital Markets LLC, with misconduct by Wachovia in the sale of two CDOs tied to the performance of residential mortgage-backed securities as the housing market was beginning to show signs of distress.<sup>2</sup> The SEC's order found that Wachovia violated the securities laws in two respects. First, the company charged undisclosed excessive markups in the sale of certain preferred shares or equity of one CDO to the Zuni Indian Tribe and an individual investor. Second, Wachovia misrepresented to investors in another CDO that it acquired assets from affiliates "on an arm's-length basis" and "at fair market prices" when, in fact, 40 residential mortgage-backed securities were transferred from an affiliate at above-market prices. Wachovia transferred these assets at stale prices in order to avoid losses on its own books. Wells Fargo consented to an order requiring that it pay more than \$11 million in disgorgement and penalties, most of which will be returned to harmed investors.

The Commission brought enforcement actions against additional individuals in FY 2011 for misconduct related to the financial crisis. In February, the SEC charged three former senior executives at IndyMac Bancorp with securities fraud for misleading investors about the mortgage lender's deteriorating financial condition.<sup>3</sup> The Commission alleged that former CEO, Michael W. Perry, and former CFOs, A. Scott Keys and S. Blair Abernathy, participated in the filing of false and misleading disclosures about the financial stability of IndyMac and its main subsidiary, IndyMac Bank F.S.B. (Federal Savings Bank). The three executives

regularly received internal reports about IndyMac's deteriorating capital and liquidity positions in 2007 and 2008, but failed to ensure adequate disclosure of that information to investors as IndyMac sold millions of dollars in new stock. Abernathy agreed to settle the SEC's charges by consenting to an injunction, disgorgement and financial penalties. Abernathy also consented to the issuance of an administrative order pursuant to SEC Rule 102(e), suspending him from appearing or practicing before the Commission as an accountant, with the right to apply for reinstatement after two years. The cases filed against Perry and Keys, which remain pending, seek permanent injunctions, financial penalties, and officer and director bars.

In a series of actions, the SEC also charged executives of Colonial Bank and Taylor, Bean & Whitaker (TBW), once the nation's largest non-depository mortgage lender, for orchestrating a \$1.5 billion scheme aimed at defrauding the Department of the Treasury's Troubled Asset Relief Program (TARP). In June, the Commission charged Paul R. Allen, the former chief executive officer at TBW, with aiding-and-abetting the efforts of TBW's former chairman, Lee B. Farkas.<sup>4</sup> The Commission's complaint alleged that Allen provided substantial assistance to Farkas in misrepresenting to Colonial BancGroup, Inc. - Colonial Bank's parent company - and others that TBW had secured a \$300 million equity investment in BancGroup that would allow BancGroup and Colonial Bank to qualify for approximately \$550 million in TARP funds. The capital infusion, however, was a sham orchestrated by Farkas in part with Allen's assistance. In a settlement of the SEC's charges, Allen consented to the entry of a judgment permanently enjoining him from violating the anti-fraud provisions of the Federal securities laws. In related actions, the SEC also charged Desiree E. Brown, former treasurer of TBW;<sup>5</sup> Catherine L. Kissick, a former vice president at Colonial Bank who was head of its mortgage warehouse lending division;<sup>6</sup> and Teresa A. Kelly, a former operations

<sup>2</sup> *In the Matter of Wells Fargo Securities, LLC, Exchange Act Rel. No. 64182 (April 5, 2011)* <http://www.sec.gov/litigation/admin/2011/33-9200.pdf>

<sup>3</sup> *SEC v. Michael W. Perry and A. Scott Keys; SEC v. S. Blair Abernathy, Lit. Rel. No. 21853 (February 11, 2011)* <http://www.sec.gov/litigation/litreleases/2011/lr21853.htm>

<sup>4</sup> *SEC v. Paul R. Allen, Lit. Rel. No. 22007 (June 21, 2011)* <http://www.sec.gov/litigation/litreleases/2011/lr22007.htm>

<sup>5</sup> *SEC v. Desiree E. Brown, Rel. No. 2011-49 (February 24, 2011)* <http://www.sec.gov/news/press/2011/2011-49.htm>

<sup>6</sup> *SEC v. Catherine L. Kissick, Rel. No. 2011-56 (March 2, 2011)* <http://www.sec.gov/news/press/2011/2011-56.htm>

supervisor of Colonial Bank's mortgage warehouse lending division, for their role in the scheme.<sup>7</sup> The SEC brought its enforcement actions in coordination with members of the Financial Fraud Enforcement Task Force, including the U.S. Department of Justice Criminal Division, the Federal Bureau of Investigation, the Office of the Special Inspector General for the TARP, the Federal Deposit Insurance Corporation Office of the Inspector General, the Office of the Inspector General of the U.S. Department of Housing and Urban Development, the Office of the Inspector General for the Federal Housing Finance Agency, and the U.S. Attorney's Office for the Eastern District of Virginia. Brown, Kissick, Kelly and Allen have all agreed to settle the charges against them. The case against Farkas, who has been criminally convicted, continues.<sup>8</sup>

In addition, in August, the Commission charged Stifel, Nicolaus & Co. and a former senior vice president, for defrauding five Wisconsin school districts in connection with the sale of highly complex and risky CDO investments.<sup>9</sup> The investments involved a proprietary program created to help the school districts fund retiree benefits by investing in notes linked to the performance of synthetic collateralized debt obligations. The school districts established trusts that invested \$200 million in three transactions from June to December 2006, paid for largely with borrowed funds. According to the complaint, Stifel misrepresented the risk of the investments and failed to disclose material facts to the school districts. In the end, the investments were a complete failure, but generated significant fees for the firm. The Stifel representative had made sweeping assurances to the school districts, misrepresenting that it would take "15 Enrons" – a catastrophic, overnight collapse – for the investments to fail. This matter remains pending.

In a related action, the Commission charged RBC Capital Markets, LLC for its involvement in the fraudulent sale of the CDO investments to the Wisconsin School District trusts. RBC negligently recommended and sold these investments, despite significant internal concerns about the suitability of

the investments for municipalities like the school districts. The SEC's order found that these investments were unsuitable for the school districts, and that RBC's marketing materials failed to explain adequately the risks associated with the investments. To settle the Commission's charges, RBC agreed to pay \$30.4 million, which included disgorgement, interest, and a civil penalty of \$22 million, all of which is being returned to the school districts.<sup>10</sup>

In another important action, the SEC charged six former senior executives of Kansas-based Brooke Corporation, and its other, publicly-traded subsidiaries, Brooke Capital Corporation, an insurance agency franchisor, and Aleritas Capital Corporation, a finance company specializing in providing loans to franchisees.<sup>11</sup> During 2007 and 2008, senior executives at the Brooke companies misrepresented, among other things, the number of Brooke Capital franchisees and their financial health, the deterioration of Aleritas' corresponding loan portfolio, and the increasingly dire liquidity and financial condition of the Brooke companies. When the Brooke companies collapsed in late 2008, securitization investors holding loans originated by Brooke suffered losses estimated at roughly a half a billion dollars, at least six regional banks failed, and one of the company's largest lenders obtained funds under TARP. All six of the former Brooke executives charged – Robert D. Orr, Leland G. Orr, Michael S. Lowry, Michael S. Hess, Travis W. Vrbas, and Kyle L. Garst – agreed to settlements that included full injunctive relief, and permanent officer and director bars. The settlements with Lowry, Hess, Vrbas, and Garst included disgorgement and/or civil penalties ranging from \$130,000 to \$413,504. Leland Orr and Vrbas also consented to the issuance of an administrative order pursuant to SEC Rule 102(e), suspending them from appearing or practicing before the SEC as accountants. The SEC's motion for disgorgement and civil penalties against Robert and Leland Orr remains pending.

<sup>7</sup> *SEC v. Teresa A. Kelly*, Rel. No. 2011-68 (March 16, 2011) <http://www.sec.gov/news/press/2011/2011-68.htm>

<sup>8</sup> *SEC v. Lee B. Farkas*, Rel. No. 2010-102 (June 16, 2010) <http://www.sec.gov/news/press/2010/2010-102.htm>

<sup>9</sup> *SEC v. Stifel, Nicolaus & Co., Inc. and David W. Noack*, Lit. Rel. No. 22064 (August 10, 2011) <http://www.sec.gov/litigation/litreleases/2011/lr22064.htm>

<sup>10</sup> *In the Matter of RBC Capital Markets, LLC (f/k/a RBC Capital Markets Corp.)*, Exchange Act Release No. 65404 (September 27, 2011) <http://www.sec.gov/litigation/admin/2011/33-9262.pdf>

<sup>11</sup> *SEC v. Robert D. Orr, et al.*, Lit. Rel. No. 21957 (May 4, 2011) <http://www.sec.gov/litigation/litreleases/2011/lr21957.htm>; Lit. Rel. No. 22089 (September 8, 2011) <http://www.sec.gov/litigation/litreleases/2011/lr22089.htm>

In FY 2011, the SEC also secured significant settlements in several previously-filed enforcement actions related to the financial crisis. In October, the Commission settled charges against former Countrywide Financial CEO, Angelo Mozilo, who agreed to pay a record \$22.5 million penalty to settle charges that he and two other former Countrywide executives misled investors as the subprime mortgage crisis emerged.<sup>12</sup> Mozilo's financial penalty is the largest ever paid by a public company's senior executive in an SEC settlement. The settlement also permanently bars Mozilo from ever again serving as an officer or director of a publicly traded company. Mozilo also agreed to disgorge \$45 million of ill-gotten gains for a total financial settlement of \$67.5 million that will be returned to harmed investors. The SEC previously charged Mozilo and the two executives on June 4, 2009, alleging that they failed to disclose to investors the significant credit risk that Countrywide was taking on as a result of its efforts to build and maintain market share.<sup>13</sup> Investors were misled by representations assuring them that Countrywide was primarily a prime quality mortgage lender that had avoided the excesses of its competitors. The SEC's complaint further alleged that Mozilo engaged in insider trading in the securities of Countrywide. The two other executives, former Countrywide chief operating officer (COO), David Sambol, and former CFO, Eric Sieracki, agreed to settle the charges against them. Sambol consented to pay \$5 million in disgorgement and a \$520,000 penalty, and a three year officer and director bar. Sieracki agreed to pay a \$130,000 penalty and a one year bar from practicing before the Commission. The penalties and disgorgement paid by Sambol and Sieracki also will be returned to harmed investors.

In another subprime mortgage case, the SEC settled previously-filed charges against Morgan Keegan & Company and Morgan Asset Management, which agreed to pay

\$200 million to settle fraud charges.<sup>14</sup> Two Morgan Keegan employees also agreed to pay penalties for their alleged misconduct, and one of them is now barred from the securities industry. The Memphis-based firms former portfolio manager, James C. Kelsoe Jr., and Comptroller, Joseph Thompson Weller, were charged by the SEC with causing the false valuation of subprime mortgage-backed securities in five funds managed by Morgan Asset Management from January 2007 to July 2007.<sup>15</sup> The SEC's order issued in settling the charges also found that Morgan Keegan failed to employ reasonable pricing procedures and consequently did not calculate accurate "net asset values" (NAV) for the funds. Morgan Keegan nevertheless published the inaccurate daily NAVs and sold shares to investors based on the inflated prices. Under the settlement, Morgan Keegan is required to pay \$25 million in disgorgement and interest and a \$75 million penalty to the SEC to be placed into a Fair Fund for the benefit of investors harmed by the violations. Morgan Keegan will also pay \$100 million into a state fund that also will be distributed to investors. The firms are additionally required to abstain from involvement in valuing fair valued securities on behalf of investment companies for three years. Kelsoe agreed to pay \$500,000 in penalties and be permanently barred from the securities industry, and Weller agreed to pay a penalty of \$50,000. The SEC brought its enforcement action in coordination with Financial Industry Regulatory Authority, Inc. (FINRA) and a task force of state regulators.

### **Actions Involving Municipal Securities**

In December, the SEC's investigation into a series of complex bid-rigging schemes resulted in charges against Banc of America Securities LLC (BAS) with securities fraud for fraudulently rigging the bidding for 92 reinvestment transactions.<sup>16</sup> The bid-rigging involved the temporary investment

<sup>12</sup> *SEC v. Angelo Mozilo, et al.*, Release No. 2010-197 (October 15, 2010) <http://www.sec.gov/news/press/2010/2010-197.htm>

<sup>13</sup> *SEC v. Angelo Mozilo, et al.*, Lit. Rel. No. 21068A (June 4, 2009) <http://www.sec.gov/litigation/litreleases/2009/lr21068a.htm>

<sup>14</sup> *In the Matter of Morgan Asset Management, Inc., et al.*, Exchange Act Rel. No. 64720 (June 22, 2011) <http://www.sec.gov/litigation/admin/2011/34-64720.pdf>; *In the Matter of Morgan Asset Mgmt, Inc.*, Exchange Act Rel. No. 65227 (August 30, 2011) <http://www.sec.gov/litigation/admin/2011/34-65227.pdf>

<sup>15</sup> *In the Matter of Morgan Asset Management, Inc., et al.*, Exchange Act Rel. No. 61856 (April 7, 2010) <http://www.sec.gov/litigation/admin/2010/33-9116.pdf>

<sup>16</sup> *In the Matter of Banc of America Securities, now known as Merrill Lynch, Pierce, Fenner & Smith Incorporated, successor by merger*, Exchange Act Release No. 63451 (December 7, 2010) <http://www.sec.gov/news/press/2010/2010-239.htm>; *In the Matter of Douglas Lee Campbell*, Exchange Act Release No. 63450 (December 7, 2010) <http://www.sec.gov/litigation/admin/2010/34-63450.pdf>

of proceeds of tax-exempt municipal securities. The fraudulent practices both affected the prices of the reinvestment products and jeopardized the tax-exempt status of the underlying municipal securities. In some cases, bidding agents steered business to BAS by giving it information on competing bids. In other instances, bidding agents deliberately obtained off-market “courtesy” bids or purposefully non-winning bids from other bidders so that BAS could win the transaction. In return, BAS steered business to those bidding agents and submitted courtesy and purposefully non-winning bids upon request. In addition, those bidding agents were at times rewarded with, among other things, undisclosed gratuitous payments and kickbacks. BAS, which cooperated in the investigation, agreed to pay more than \$36 million in disgorgement and interest to settle the SEC’s charges, all of which was distributed to affected municipalities located in 20 states, and paid an additional \$101 million to other Federal and state authorities for its misconduct. The Commission also barred Douglas Campbell, a former BAS officer, from the industry. The SEC brought this action in coordination with the Internal Revenue Service, the Office of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System and 20 state attorney generals.

In another case stemming from the SEC’s investigation into corruption in the municipal reinvestment industry, the Commission in May 2011, charged UBS Financial Services Inc. with securities fraud for fraudulently rigging over 100 bids, in a scheme similar to BAS.<sup>17</sup> UBS agreed to pay \$47.2 million, which included disgorgement, interest and a civil penalty of \$32.5 million, to settle the SEC’s charges. All of these monetary sanctions were returned to the affected municipalities located in 36 states. UBS also paid \$113 million to other Federal and state authorities in connection with their parallel cases. The Commission also barred Mark Zaino, a former UBS officer, from the industry.

Similarly, in July the SEC charged J.P. Morgan Securities LLC (JPMS) with fraudulently rigging at least 93 municipal bond

reinvestment transactions in 31 states, generating millions of dollars in ill-gotten gains.<sup>18</sup> To settle the SEC’s fraud charges, JPMS agreed to pay approximately \$51.2 million, which included disgorgement, interest, and a civil penalty of \$32.5 million, that has been returned to the affected municipalities or conduit borrowers. JPMS and its affiliates also agreed to pay \$177 million to settle parallel charges brought by other Federal and state authorities. Separately, the Commission permanently barred James Hertz, a former JPMS officer, from the industry.

### **Actions Involving Mutual Funds, Investment Advisers and Broker-Dealers**

The Commission brought numerous actions against mutual funds, investment advisers and broker-dealers in FY 2011. In January, the SEC charged two former portfolio managers with defrauding a mutual fund that invests primarily in municipal bonds.<sup>19</sup> The Commission found that Kimball Young and Thomas Albright, former co-portfolio managers of the Tax Free Fund for Utah, while working at Aquila Investment Management LLC, improperly charged municipal bond issuers more than a half-million dollars in undisclosed “credit monitoring fees” they pocketed for themselves. Young and Albright settled the SEC’s charges by agreeing to sanctions including industry bars and the return of all credit monitoring fees they received, along with additional financial penalties.

Also in January, the Commission charged Charles Schwab Investment Management (CSIM) and Charles Schwab & Co., Inc. (CS&Co.) with making misleading statements regarding the Schwab YieldPlus Fund and failing to establish, maintain and enforce policies and procedures to prevent the misuse of material, nonpublic information.<sup>20</sup> The misleading statements included descriptions of the fund as a cash alternative that had only slightly higher risk than a money market fund. The SEC also charged CSIM and Schwab Investments with deviating from the YieldPlus and Schwab Total Bond Market funds’ concentration policy without obtaining the required

<sup>17</sup> *SEC v. UBS Financial Services Inc., Lit. Rel. No. 21956 (May 4, 2011)* <http://www.sec.gov/litigation/litreleases/2011/lr21956.htm>; *In the Matter of Mark Zaino, Exchange Act Rel. No. 64398 (May 4, 2011)* <http://www.sec.gov/litigation/admin/2011/34-64398.pdf>

<sup>18</sup> *SEC v. J.P. Morgan Securities LLC, Lit. Rel. No. 22031 (July 7, 2011)* <http://www.sec.gov/litigation/litreleases/2011/lr22031.htm>; *In the Matter of James L. Hertz, Exchange Act Rel. No. 64831 (July 7, 2011)* <http://www.sec.gov/litigation/admin/2011/34-64831.pdf>

<sup>19</sup> *In the Matter of Kimball L. Young, Exchange Act. Rel. No. 63675 (January 7, 2011)* <http://www.sec.gov/litigation/admin/2011/34-63675.pdf>; *In the Matter of Thomas S. Albright, Exchange Act Rel. No. 63675 (Jan. 7, 2011)* <http://www.sec.gov/litigation/admin/2011/34-63676.pdf>

<sup>20</sup> *SEC v. Charles Schwab Inv. Mgmt, Lit. Rel. No. 21806 (January 11, 2011)* <http://www.sec.gov/litigation/litreleases/2011/lr21806.htm>

shareholder approval. The YieldPlus Fund is an ultra-short bond fund that, at its peak in 2007, had \$13.5 billion in assets and more than 200,000 accounts, making it the largest ultra-short bond fund. The fund suffered a significant decline during the credit crisis of 2007 and 2008. CSIM and CS&Co. agreed to pay more than \$118 million to settle the SEC's charges. In addition, CSIM, CS&Co. and Schwab Investments consented to an order requiring them to cease and desist from committing or causing future violations of the Federal securities laws, and to comply with certain undertakings. The court has approved the Commission's plan for distributing funds to harmed investors.

In a related action, the SEC filed a complaint in Federal district court against CSIM's former chief investment officer for fixed income, Kimon Daifotis, as well as Randall Merk, then executive vice president at CS&Co. who also was president of CSIM and a trustee of the YieldPlus and other Schwab funds. The SEC alleged that Daifotis and Merk committed fraud and other securities law violations in connection with the offer, sale and management of the YieldPlus Fund. The SEC's case continues against Daifotis and Merk.

In February, the Commission charged AXA Rosenberg Group LLC and two related entities for concealing a significant error in the computer code of the quantitative investment model that they used to manage client assets.<sup>21</sup> The error disabled one of the model's key components for managing risk. Upon learning of the error, AXA officials directed employees to remain quiet about it, failed to fix the error or to disclose it to clients, and made misrepresentations to clients regarding the model's ability to control risk and blaming underperformance on volatility. AXA did not disclose the error until almost six months later, upon learning of an impending SEC examination. Additionally, the SEC found that the relevant AXA-affiliated entity failed to implement reasonable compliance measures to ensure that the model would assess certain risk factors as intended. The AXA entities settled the SEC's charges by paying \$217 million to harmed clients plus

a \$25 million penalty. In related action, the SEC charged Barr M. Rosenberg, co-founder of AXA Rosenberg, with securities fraud for concealing the error.<sup>22</sup> Rosenberg agreed to settle the charges by paying a \$2.5 million penalty and consenting to a lifetime securities industry bar.

In another action, the Commission charged Merrill Lynch, Pierce, Fenner & Smith Inc. with securities fraud for misusing customer order information to place proprietary trades for the firm and for charging customers undisclosed trading fees.<sup>23</sup> The SEC's order found that Merrill operated a proprietary trading desk between 2003 and 2005 that was known as the Equity Strategy Desk (ESD), which traded securities solely for the firm's own benefit and had no role in executing customer orders. The ESD was located on Merrill's main equity trading floor in New York City, where traders on Merrill's market making desk received and executed customer orders. While Merrill represented to customers that their order information would be maintained on a strict need-to-know basis, the firm's ESD traders obtained information about institutional customer orders from traders on the market making desk. They then used it to place trades on Merrill's behalf after executing the customers' trades. In doing so, Merrill misused this information and acted contrary to its representations to customers. The SEC's order also found that, between 2002 and 2007, Merrill had agreements with certain institutional and high net worth customers that Merrill would only charge a commission equivalent to those for executing riskless principal trades. However, in some instances, Merrill also charged customers undisclosed mark-ups and mark-downs by filling customer orders at prices less favorable to the customer than the prices at which Merrill purchased or sold the securities in the market. To settle the SEC's charges, Merrill agreed to pay a \$10 million penalty and consent to a cease and desist order.

The SEC has held other firms accountable for failing to accurately describe product risk. In February, the Commission charged TD Ameritrade Inc. for failing to reasonably

<sup>21</sup> *In the Matter of AXA Rosenberg Group LLC, et al., Securities Act Rel. No. 9181 (February 3, 2011)* <http://www.sec.gov/litigation/admin/2011/33-9181.pdf>

<sup>22</sup> *In the Matter of Barr M. Rosenberg, Advisers Act Release No. 3285 (September 22, 2011)* <http://www.sec.gov/litigation/admin/2011/ia-3285.pdf>

<sup>23</sup> *In the Matter of Merrill Lynch, Pierce, Fenner & Smith, Inc., Exchange Act Rel. No. 63760 (January 25, 2011)* <http://www.sec.gov/litigation/admin/2011/34-63760.pdf>

supervise its registered representatives, some of whom misled customers when selling shares of the Reserve Yield Plus Fund, a mutual fund that “broke the buck” in September 2008.<sup>24</sup> The SEC’s order found that TD Ameritrade’s representatives offered and sold the fund through the firm’s various sales channels prior to Sept. 16, 2008. The order also found that a number of the representatives violated the securities laws when they mischaracterized the fund as a money market fund, as safe as cash, or as an investment with guaranteed liquidity. They also failed to disclose the nature or risks of the fund when offering the investment to customers. The SEC alleged that TD Ameritrade failed to prevent the misconduct by its representatives because it did not establish adequate supervisory policies and procedures or a system to implement them with respect to the offers and sales of the fund. To settle the SEC’s charges, TD Ameritrade agreed to distribute approximately \$10 million to eligible customers who continue to hold shares of the fund.

In September, the SEC charged a Long Island-based investment adviser with defrauding investors in hedge funds investing in PIPE transactions (Private Investment/Public Equity) and misappropriating more than \$1 million in client assets for his personal use.<sup>25</sup> The SEC alleged that Corey Ribotsky and his firm, The NIR Group LLC, repeatedly lied to investors to hide the truth that his PIPE investment and trading strategy was failing during the financial crisis. For example, Ribotsky falsely told investors that despite the adverse market conditions, he could liquidate all of the PIPE investments in 36 to 48 months – a practical impossibility given the size of the investments. Ribotsky allegedly continued to make this false and misleading representation to investors even after the outside auditor for NIR’s family of AJW Funds calculated that it would take decades – if possible at all – to liquidate all of the AJW Funds’ PIPE investments under NIR’s stated investment and trading strategy. Ribotsky also instructed an NIR employee – who also is charged in the SEC’s complaint – to falsify certain documents sent to investors. Meanwhile, Ribotsky misused investor money by writing checks to pay for personal services and such luxury

items as a Lexus, Mercedes, and Rolex watch. He also wrote checks to himself or to “cash” and then instructed NIR office employees to cash the checks at a nearby bank and then give Ribotsky the money. The complaint seeks injunctive relief, disgorgement of ill-gotten gains plus prejudgment interest and monetary penalties.

### **Actions Involving Financial Fraud and Issuer Disclosure**

The Commission brought a number of cases in FY 2011 involving accounting and financial fraud, issuer disclosure, and reporting violations at public companies. In April, the Commission filed an action against Satyam Computer Services Limited (Satyam) charging the company with fraudulently overstating its revenue, income and cash balances by more than \$1 billion over five years.<sup>26</sup> The SEC alleged that former senior officials at Satyam – an information technology services company based in Hyderabad, India with American Depository Receipts (ADRs) traded on the New York Stock Exchange (NYSE) – used false invoices and forged bank statements to inflate the company’s cash balances and make it appear far more profitable to investors. Satyam agreed to pay a \$10 million penalty to settle the SEC’s charges, require enhancements to training of officers and employees concerning securities laws and accounting principles, and improve its internal audit functions. Satyam also agreed to hire an independent consultant to evaluate the internal controls the company is putting in place. In a related settlement, the SEC sanctioned five India-based affiliates of PricewaterhouseCoopers (PWC) that formerly served as Satyam’s independent auditors.<sup>27</sup> The SEC found that the audit failures by the PWC India affiliates – Lovelock & Lewes; Price Waterhouse Bangalore; Price Waterhouse & Co. Bangalore; Price Waterhouse Calcutta; and Price Waterhouse & Co. Calcutta – were not limited to Satyam, but rather indicative of a larger quality control failure throughout PW India. The PWC India affiliates agreed to settle the SEC’s charges and pay a \$6 million penalty, the largest ever by a foreign-based accounting firm in an SEC enforcement action.

<sup>24</sup> *In the Matter of TD Ameritrade, Inc., Exchange Act Rel. No. 63829 (February 3, 2011)* <http://www.sec.gov/litigation/admin/2011/34-63829.pdf>

<sup>25</sup> *SEC v. The NIR Group, LLC, et al., Lit. Rel. No. 22106 (September 28, 2011)* <http://www.sec.gov/litigation/litrelases/2011/lr22106.htm>

<sup>26</sup> *SEC v. Satyam Computer Services Limited d/b/a Mahindra Satyam, Lit. Rel. No. 21915 (April 5, 2011)* <http://www.sec.gov/litigation/litrelases/2011/lr21915.htm>

<sup>27</sup> *In the Matter of Lovelock & Lewes; Price Waterhouse, Bangalore; Price Waterhouse & Co., Bangalore; Price Waterhouse, Calcutta; and Price Waterhouse & Co., Calcutta, Respondents, Accounting and Auditing Enforcement Rel. No. 3257 (April 5, 2011)* <http://www.sec.gov/litigation/admin/2011/34-64184.pdf>

In another action, the SEC charged DHB Industries, Inc. (DHB), now known as Point Blank Solutions, Inc., for engaging in a massive accounting fraud that occurred between 2003 and 2005. In its complaint, the SEC alleged that DHB, a major supplier of body armor to the U.S. military and law enforcement agencies, engaged in pervasive accounting and disclosure fraud, and misappropriation of company assets that resulted in the company filing materially false and misleading periodic reports with the SEC.<sup>28</sup> In a related action, the SEC also filed separate fraud charges against DHB's former outside directors and audit committee members, Jerome Krantz, Cary Chasin, and Gary Nadelman, for facilitating the company's fraud.<sup>29</sup> The SEC's complaint against Krantz, Chasin, and Nadelman alleges that from at least 2003 through 2005, they were willfully blind to numerous red flags signaling accounting fraud, reporting violations, and misappropriation at DHB. According to the complaint, the three audit committee board members' willful blindness to these red flags, allowed senior management to manipulate the company's reported gross profit, net income, and other key figures in its earnings releases and public filings. The company did so by, among other things, overstating inventory values, failing to include appropriate charges for obsolete inventory, and falsifying journal entries. The complaint further alleges that their willful blindness to red flags enabled DHB's former chief executive officer, David Brooks, to divert at least \$10 million out of the company through fraudulent transactions with a related entity he controlled. Despite being confronted with numerous, significant, and compounding red flags indicating fraud, the three audit committee and board members approved and/or signed DHB's false and misleading filings. DHB, which is currently in bankruptcy, agreed to settle with the SEC and agreed to a permanent injunction from future violations. In addition, the SEC has reached settlements with Krantz, Chasin, and Nadelman which provide for full injunctive relief, including officer and director bars and monetary sanctions.

Previously filed actions against DHB's CEO and two other senior officers are stayed pending full resolution of criminal actions brought by the U.S. Attorney's Office for the Eastern District of New York.

The Commission also charged Office Depot, Inc. and CEO, Stephen A. Odland, and then CFO, Patricia A. McKay, for violating or causing violations of fair disclosure regulations (Regulation FD) when selectively conveying to analysts and institutional investors that the company would not meet analysts' earnings estimates.<sup>30</sup> The complaint alleges that the company violated Regulation FD by making a series of one-on-one calls to analysts. The company did not directly state that it would not meet analysts' expectations, but rather this message was signaled with references to recent public statements of comparable companies about the impact of the slowing economy on their earnings. During the calls, the analysts also were reminded of Office Depot's prior cautionary public statements. Analysts promptly lowered their estimates for the period in response to the calls. Office Depot did not regularly initiate these types of calls to all analysts covering the company. Office Depot settled the SEC's charges by paying a \$1 million penalty. Odland and McKay also agreed to settle the Regulation FD charges by each paying \$50,000.

In addition, the SEC charged the Government website provider NIC, Inc. and four current and former executives for their failure to disclose more than \$1.18 million in perks to the former CEO, Jeffery Fraser.<sup>31</sup> The SEC's actions alleged that NIC's public filings failed to disclose that the company footed the bill for wide-ranging perks enjoyed by Fraser, his girlfriend, and his family – including vacations, computers, and day-to-day personal living expenses. NIC failed to disclose that it paid thousands of dollars per month for Fraser to live in a Wyoming ski lodge and commute by private aircraft to his office at NIC's Kansas headquarters.

<sup>28</sup> *SEC v. DHB Industries, Inc. n/k/a Point Blank Solutions, Lit. Rel. No. 21867 (February 28, 2011)* <http://www.sec.gov/litigation/litrelases/2011/lr21867.htm>

<sup>29</sup> *SEC v. Jerome Krantz, Cary Chasin, and Gary Nadelman, Lit. Rel. No. 21867 (February 28, 2011)* <http://www.sec.gov/litigation/litrelases/2011/lr21867.htm>

<sup>30</sup> *In the Matter of Office Depot, Inc., Accounting and Auditing Enforcement Rel. No. 3198 (October 21, 2010)* <http://www.sec.gov/litigation/admin/2010/34-63152.pdf>; *In the Matter of Stephen A. Odland, Exchange Act Rel. No. 63153 (October 21, 2010)* <http://www.sec.gov/litigation/admin/2010/34-63153.pdf>; *In the Matter of Patricia A. McKay, Exchange Act. Rel. No. 63154 (October 21, 2010)* <http://www.sec.gov/litigation/admin/2010/34-63154.pdf>

<sup>31</sup> *SEC v. NIC Inc., Jeffery S. Fraser, Harry H. Herrington, and Eric J. Bur, Lit. Rel. No. 21809 (January 12, 2011)* *SEC v. Stephen M. Kovzan, Lit. Rel. No. 21809 (January 12, 2011)* <http://www.sec.gov/litigation/litrelases/2011/lr21809.htm>

Meanwhile, NIC and its executives falsely represented to investors that Fraser worked virtually for free from 2002 to 2005, and then continued to materially understate the perks that Fraser received in 2006 and 2007. NIC, Fraser, current CEO, Harry Herington, and former CFO, Eric Bur, agreed to pay a combined \$2.8 million to settle the SEC's charges against them. The SEC's litigation continues against NIC's current CFO, Stephen Kovzan.

In another important action, the SEC charged ArthroCare Corporation for materially overstating its revenue and earnings between 2006 and 2008.<sup>32</sup> The Commission alleged that ArthroCare, a medical device manufacturer, engaged in "channel-stuffing" and similar earnings management schemes by, among other things, shipping huge volumes of unneeded spine products to its distributors at or near the end of quarters, and forcing products on distributors who had no ability to pay for them. According to the Commission, these improper transactions were intended to help ArthroCare meet external revenue and earnings expectations. In a related action, the Commission charged two former ArthroCare officers, John Raffle and David Applegate, with running the earnings management scheme and, on certain occasions, misleading ArthroCare's accountants and auditor about aspects of the transactions.<sup>33</sup> In recognition of the company's cooperation with the investigation, the Commission accepted ArthroCare's offer to consent to a cease and desist order against future violations of the reporting, record-keeping and internal controls provisions and to undertake numerous remedial actions, without paying a civil penalty. The Commission also accepted settlement offers from Raffle and Applegate, under which they consented to antifraud injunctions, officer and director bars and disgorgement of ill-gotten gains. Penalties were not imposed against Raffle or Applegate based on their sworn financial statements.

### **Actions Involving Executive Compensation Clawbacks**

Section 304 of the Sarbanes-Oxley Act of 2002 requires reimbursement by certain senior corporate executives of

categories of compensation and stock sale profits received while their companies were in material non-compliance with financial reporting requirements due to misconduct.<sup>34</sup> Section 304 reimbursement can extend to an individual who has not been personally charged with the underlying misconduct or alleged to have otherwise violated the Federal securities laws.

In FY 2011, the SEC continued to use its executive compensation "clawback" authority. In January, the SEC charged NutraCea, three former executives, and two former accounting personnel for engaging in a fraudulent accounting scheme to inflate NutraCea's product sales revenues.<sup>35</sup> The SEC alleged that NutraCea overstated its sales revenues for the second and third quarters of its FY 2007 and its entire FY 2007 by booking false sales and engaging in improper revenue recognition practices. The SEC also charged NutraCea's former CEO, Bradley D. Edson, and other executives for their roles in the fraudulent accounting scheme. Edson agreed to settle the charges against him by paying a \$100,000 penalty, reimbursing NutraCea \$350,000 in bonuses he received in 2008, and agreeing to a permanent officer and director bar. NutraCea and the remaining executives also agreed to settle the SEC's charges.

In June, the Commission charged two former Basin Water, Inc. executives with fraudulently inflating its revenues, beginning with the company's first financial report after it went public.<sup>36</sup> The complaint alleged that former Basin Water CEO, Peter L. Jensen, and former CFO, Thomas C. Tekulve, Jr., improperly recognized revenue to disguise the company's true financial performance in its FY 2006 and FY 2007 quarterly and annual reports. The SEC also alleged that Jensen sold and donated his own Basin Water shares before the company's true financial condition was revealed, reaping millions of dollars in trading profits and tax benefits. The Commission seeks against each defendant permanent injunctive relief, an officer and director bar, disgorgement of ill-gotten gains plus prejudgment interest, a financial penalty, and reimbursement under Section 304 of the Sarbanes-Oxley Act.

<sup>32</sup> *In the Matter of ArthroCare Corporation, Exchange Act Rel. No. 63883 (February 9, 2011)* <http://www.sec.gov/litigation/admin/2011/34-63883.pdf>

<sup>33</sup> *SEC v. John Raffle, et al., Lit. Rel. No. 22027 (July 5, 2011)* <http://www.sec.gov/litigation/litreleases/2011/lr22027.htm>

<sup>34</sup> See 15 U.S.C. § 7243.

<sup>35</sup> *SEC v. NutraCea, et al., Lit. Rel. No. 21819 (January 20, 2011)* <http://www.sec.gov/litigation/litreleases/2011/lr21819.htm>

<sup>36</sup> *SEC v. Peter L. Jensen and Thomas C. Tekulve, Jr., Lit. Rel. No. 22014 (June 27, 2011)* <http://www.sec.gov/litigation/litreleases/2011/lr22014.htm>

In another action, the Commission in August reached a settlement with the former CFO of Beazer Homes USA to recover his bonus compensation and stock sale profits from the period when the Atlanta-based homebuilder was committing accounting fraud.<sup>37</sup> According to the SEC's complaint, James O'Leary is not personally charged with misconduct, but is still required under Section 304 to reimburse Beazer more than \$1.4 million that he received after Beazer filed fraudulent financial statements during FY 2006. To settle the SEC's action, O'Leary agreed to reimburse Beazer \$1,431,022 in cash, representing his entire FY 2006 incentive bonus. The payment also included \$274,525 in stock sale profits. In a separate settlement with Beazer CEO, Ian McCarthy, McCarthy agreed to reimburse Beazer more than \$6 million in cash, 40,103 restricted stock units (or its equivalent) and 78,763 shares of restricted stock (or its equivalent). This reimbursement also represented McCarthy's entire FY 2006 incentive bonus.<sup>38</sup> Beazer settled an SEC enforcement action in September 2008,<sup>39</sup> and the SEC charged its former chief accounting officer, Michael Rand, in July 2009.<sup>40</sup> The litigation against Rand, who perpetrated the fraud, is ongoing.

### Actions Involving Foreign Corrupt Practices

The Commission's Foreign Corrupt Practices Act (FCPA) Unit focuses on enforcing the laws and regulations that prohibit corporate bribery of foreign officials. The Unit focuses on new and proactive approaches to investigating violations of the FCPA and works closely and extensively with other Federal and foreign law enforcement agencies and foreign regulators to bring wrongdoers in this area to justice. The SEC brought a number of significant FCPA enforcement actions in the last fiscal year.

In November, the Commission filed settled actions against global freight forwarding company Panalpina, Inc. and six other companies in the oil services industry that violated the FCPA by paying millions of dollars in bribes to foreign officials to receive preferential treatment and improper benefits during the customs process.<sup>41</sup> The actions were the result of a sweep by the Division of Enforcement of an industrial sector in order to crack down on public companies and third parties who are paying bribes abroad. The SEC alleged that the companies bribed customs officials in more than 10 countries in exchange for such perks as avoiding applicable customs duties on imported goods, expediting the importation of goods and equipment, extending drilling contracts, and lowering tax assessments. The companies also paid bribes to obtain false documentation related to temporary import permits for oil drilling rigs, and enable the release of drilling rigs and other equipment from customs officials. The SEC's cases were coordinated with the U.S. Department of Justice's (DOJ) Fraud Section, and the sanctions to be paid by the companies under the SEC settlements totaled \$236.5 million. In addition to Panalpina, the SEC also charged Pride International, Inc.; Tidewater, Inc.; Transocean, Inc.; GlobalSantaFe Corporation; Mobile Corporation; and Royal Dutch Shell plc.

The Commission also brought settled charges against Johnson & Johnson (J&J) for violating the FCPA by bribing public doctors in several European countries and paying kickbacks to Iraq to illegally obtain business.<sup>42</sup> The SEC alleged that subsidiaries of J & J paid bribes to public doctors in Greece who selected J&J surgical implants, public doctors and hospital administrators in Poland who awarded contracts to J&J, and public doctors in Romania to prescribe J&J pharmaceutical products. The complaint

<sup>37</sup> *SEC v. James O'Leary, Lit. Rel. No. 22074* <http://www.sec.gov/litigation/litreleases/2011/lr22074.htm>

<sup>38</sup> *SEC v. Ian J. McCarthy, Lit. Rel. No. 21873 (March 4, 2011)* <http://www.sec.gov/litigation/litreleases/2011/lr21873.htm>

<sup>39</sup> *In the Matter of Beazer Homes USA, Inc., Exchange Act Rel. No. 58633 (September 24, 2008)* <http://www.sec.gov/litigation/admin/2008/33-8960.pdf>

<sup>40</sup> *SEC v. Michael T. Rand, Lit. Rel. No. 21114 (July 1, 2009)* <http://www.sec.gov/litigation/litreleases/2009/lr21114.htm>

<sup>41</sup> *SEC v. Panalpina, Inc., Lit. Rel. No. 21727 (November 4, 2010)* <http://www.sec.gov/litigation/litreleases/2010/lr21727.htm>; *SEC v. Tidewater Inc., Lit. Rel. No. 21729 (November 4, 2010)* <http://www.sec.gov/litigation/litreleases/2010/lr21729.htm>; *SEC v. Noble Corporation, Lit. Rel. No. 21728 (November 4, 2010)* <http://www.sec.gov/litigation/litreleases/2010/lr21728.htm>; *SEC v. Pride International, Inc., Lit. Rel. No. 21726 (November 4, 2010)* <http://www.sec.gov/litigation/litreleases/2010/lr21726.htm>; *SEC v. Transocean Inc., Lit. Rel. No. 21725 (November 4, 2010)* <http://www.sec.gov/litigation/litreleases/2010/lr21725.htm>; *SEC v. GlobalSantaFe Corp., Lit. Rel. No. 21724 (November 4, 2010)* <http://www.sec.gov/litigation/litreleases/2010/lr21724.htm>; *In the Matter of Royal Dutch Shell plc, et al., Exchange Act Rel. No. 63243 (November 4, 2010)* <http://www.sec.gov/litigation/admin/2010/34-63243.pdf>

<sup>42</sup> *SEC v. Johnson & Johnson, Exchange Act Rel. No. 34-21922 (April 8, 2011)* <http://www.sec.gov/litigation/litreleases/2011/lr21922.htm>

also alleged that J&J subsidiaries paid kickbacks to Iraq to obtain 19 contracts under the United Nations Oil for Food Program. J&J agreed to settle the SEC's charges by paying more than \$48.6 million in disgorgement and prejudgment interest in the SEC action, and a \$21.4 million fine to settle parallel criminal charges by DOJ.

In another action, the Commission charged Paris-based telecommunications company Alcatel-Lucent, S.A. with violating the FCPA by paying bribes to foreign government officials to illicitly win business in Latin America and Asia.<sup>43</sup> The SEC alleged that Alcatel's subsidiaries used consultants who performed little or no legitimate work to funnel more than \$8 million in bribes to government officials in Costa Rica, Honduras, Malaysia and Taiwan between December 2001 and June 2006 in order to obtain or retain lucrative telecommunications contracts and other contracts. Alcatel agreed to pay more than \$45 million to settle the SEC's charges, and an additional \$92 million to settle criminal charges by DOJ.

In May, the Commission entered into a Deferred Prosecution Agreement (DPA) with Tenaris S.A.<sup>44</sup> Tenaris is the first company to enter into a DPA with the SEC under its cooperation initiative, an approach designed to encourage individuals and companies to provide information about misconduct and assist with an SEC investigation. The agreement with Tenaris involved allegations that the global manufacturer of steel pipe products violated the FCPA by bribing Uzbekistan government officials during a bidding process to supply pipelines for transporting oil and natural gas. The SEC alleged that Tenaris made almost \$5 million in profits when it was subsequently awarded several contracts by the Uzbekistan government. Under the terms of the DPA, Tenaris must pay \$5.4 million in disgorgement and prejudgment interest and enhance its policies, procedures and controls to strengthen its FCPA and anti-corruption practices.

### Actions Involving Insider Trading

Insider trading continues to be a high priority area for the SEC's enforcement program. The Commission brought 57

cases in FY 2011 primarily classified as insider trading cases, charging 124 individuals and entities, a nearly 8 percent increase in the number of filed cases from the prior fiscal year. Many of these cases involved financial professionals, hedge fund managers, corporate insiders and attorneys who unlawfully traded on material non-public information, undermining the level playing field that is fundamental to the integrity and fair functioning of the capital markets.

In November, the SEC charged additional defendants in its ongoing investigations related to two enforcement actions, *SEC v. Galleon Management, LP, et al.*, 09-CV-8811 (S.D.N.Y.) (JSR) and *SEC v. Cutillo, et al.*, 09-CV-9208 (S.D.N.Y.) (RJS). The insider trading rings identified in these enforcement actions included several prominent hedge funds, high-profile hedge fund managers, and Wall Street professionals. In a complaint related to *SEC v. Galleon*, the SEC charged Thomas Hardin, a former managing director at a New York-based hedge fund investment adviser, Lanexa Management LLC, for insider trading in connection with two corporate takeovers and a quarterly earnings announcement.<sup>45</sup> The illicit profits at Lanexa resulting from Hardin's alleged conduct exceed \$950,000. In separate complaints related to *SEC v. Cutillo, et al.*, the SEC charged Hardin as well as two other defendants, Lanexa Management LLC, and former Schottenfeld Group LLC trader, Franz Tudor, for insider trading in connection with corporate acquisitions. The illicit profits alleged in these filings total approximately \$715,000. Hardin agreed to settle the SEC's charges by consenting to an injunction, disgorgement and prejudgment interest, with the amount of civil penalties to be determined by the court at a later date. Separately, the Commission barred Hardin from associating with any investment adviser, broker, dealer, municipal securities dealer, or transfer agent.

In January, the SEC charged additional individuals and entities for their role in the Galleon related scheme, including a New York hedge fund advisory firm, its hedge fund manager, an analyst at the hedge fund, a senior corporate executive in the technology sector, and an investor relations firm employee.<sup>46</sup> The SEC alleged that Robert Feinblatt – a co-founder and principal of New York-based hedge fund investment adviser

<sup>43</sup> *SEC v. Alcatel-Lucent, S.A., Lit. Rel. No. 34-21795 (December 27, 2010)* <http://www.sec.gov/litigation/litrelases/2010/lr21795.htm>

<sup>44</sup> *Press Release No. 2011-112 (May 17, 2011)* <http://www.sec.gov/news/press/2011/2011-112.htm>

<sup>45</sup> *SEC v. Thomas C. Hardin, Lit. Rel. No. 21740 (November 15, 2010)* <http://www.sec.gov/litigation/litrelases/2010/lr21740.htm>

<sup>46</sup> *SEC v. Robert Feinblatt, Jeffrey Yokuty, Trivium Capital Management LLC, Sunil Bhalla, and Shammara Hussain, Lit. Rel. No. 21802 (January 10, 2011)* <http://www.sec.gov/litigation/litrelases/2011/lr21802.htm>

Trivium Capital Management LLC – and Trivium analyst, Jeffrey Yokuty, engaged in insider trading in the securities of Polycorn, Hilton, Google and Kronos. The SEC further alleged that Polycorn senior executive Sunil Bhalla and Shammara Hussain, an employee at investor relations consulting firm Market Street Partners that did work for Google, tipped the inside information that enabled the insider trading by Feinblatt and Yokuty on behalf of Trivium’s hedge funds for illicit profits of more than \$15 million. Feinblatt has agreed to a settlement that included injunctive relief, approximately \$2.6 million in disgorgement and penalties, and a 5 year bar from associating with any investment adviser, broker, dealer, municipal securities dealer, or transfer agent. The remaining defendants also agreed to settle the charges against them.

In another important case, the Commission brought an action against Annabel McClellan, the wife of a former Deloitte Tax LLP partner, for repeatedly leaking confidential merger and acquisition information to family members in the UK.<sup>47</sup> These family members traded in advance of seven deals worked on by Ms. McClellan’s husband, netting nearly \$3 million for themselves (and approximately \$20 million for friends and clients). Ms. McClellan subsequently settled the Commission’s action by agreeing to pay a \$1 million penalty, and, in a related criminal case, she pleaded guilty to obstruction of justice during the Commission’s investigation. In a case of international cooperation, the UK Financial Services Authority filed charges against Ms. McClellan’s family members for their role in the scheme. That case is pending.

In March, the SEC charged Cheng Yi Liang, a chemist at the U.S. Food and Drug Administration (FDA), with insider trading on confidential information concerning upcoming announcements of FDA drug approval decisions, generating more than \$3.6 million in illicit profits and avoided losses.<sup>48</sup> The SEC’s complaint, amended in June, alleged that Liang illegally traded in advance of 28 public announcements about FDA drug approval decisions involving 20 publicly-traded companies for profits and losses avoided totaling over \$3.7 million. Some announcements concerned the FDA’s approval of new drugs while others concerned negative FDA decisions.

In each instance, he traded in the same direction as the announcement. Liang went to great lengths to conceal his insider trading. He traded in eight brokerage accounts, none of which were in his name. The litigation against Liang is continuing.

In another important case, the SEC charged Matthew Kluger, a corporate attorney, and Garrett Bauer, a Wall Street trader, for their involvement in a highly-organized serial insider trading ring that traded in advance of merger and acquisition announcements involving clients of the law firm Wilson Sonsini Goodrich & Rosati. The ring made at least \$32 million in illegal profits between April 2006 and March 2011.<sup>49</sup> The SEC is seeking permanent injunctions, disgorgement of ill-gotten gains with prejudgment interest and financial penalties.

In April, the Commission charged Dr. Joseph F. “Chip” Skowron, a former hedge fund portfolio manager affiliated with a FrontPoint Partners LLC healthcare fund, with insider trading based on confidential information about negative details of an experimental drug that he received from Dr. Yves Benhamou, a medical researcher overseeing a clinical drug trial.<sup>50</sup> The material non-public information that Skowron received allowed the hedge funds that he managed to avoid losses of approximately \$30 million. The SEC previously charged Benhamou for tipping Skowron.<sup>51</sup> Benhamou and Skowron have agreed to settle the charges against them. The hedge funds, which have been charged as relief defendants in the SEC’s amended complaint, have agreed to pay \$33 million to settle the charges.

Additionally, the SEC brought charges against Donald L. Johnson, a former managing director of The Nasdaq Stock Market, for trading on confidential information that he misappropriated while working in a market intelligence unit that communicates with executives at listed companies about impending public announcements that could affect their stocks.<sup>52</sup> Johnson obtained illicit trading profits of at least \$755,000 during a three-year period. Johnson consented to full injunctive relief to settle the SEC’s case. The amount

<sup>47</sup> *SEC v. Arnold McClellan and Annabel McClellan*, Lit. Rel. No. 21758 (Nov. 30, 2011) <http://www.sec.gov/litigation/litreleases/2010/lr21758.htm>

<sup>48</sup> *SEC v. Cheng Yi Liang, et al.*, Lit. Rel. No. 21907 (March 29, 2011) <http://www.sec.gov/litigation/litreleases/2011/lr21907.htm>

<sup>49</sup> *SEC v. Matthew H. Kluger and Garrett D. Bauer*, Lit. Rel. No. 21917 (April 6, 2011) <http://www.sec.gov/litigation/litreleases/2011/lr21917.htm>

<sup>50</sup> *SEC v. Joseph F. “Chip” Skowron III, et al.*, Lit. Rel. No. 21928 (April 13, 2011) <http://www.sec.gov/litigation/litreleases/2011/lr21928.htm>

<sup>51</sup> *SEC v. Dr. Yves M. Benhamou*, Lit. Rel. No. 21721 (November 2, 2010) <http://www.sec.gov/litigation/litreleases/2010/lr21721.htm>

<sup>52</sup> *SEC v. Donald L. Johnson, et al.*, Lit. Rel. No. 21981 (May 26, 2011) <http://www.sec.gov/litigation/litreleases/2011/lr21981.htm>

of monetary sanctions will be determined by the court at a later date.

In the Expert Network insider trading cases, the Commission charged a New York-based hedge fund and four hedge fund portfolio managers and analysts who illegally traded on confidential information obtained from technology company employees moonlighting as expert network consultants.<sup>53</sup> The defendants were involved in a scheme by which employees of Primary Global Research, LLC (PGR), an “expert network” purporting to provide investment research, received material non-public information about various companies and passed it on to hedge funds which traded on that information. Insiders acted as consultants to PGR and its hedge fund clients and were paid for sharing confidential information regarding quarterly earnings and performance data. The hedge funds traded on the information and other PGR employees received and passed the information on to additional clients. The scheme resulted in some \$6 million in illicit profits and losses avoided by PGR clients. The SEC’s action charged the insiders and PGR employees who had acted as conduits, as well as the hedge fund managers. The litigation is ongoing.

### **Actions Involving Offering Frauds/Ponzi Schemes**

The Commission brought numerous cases involving offering frauds in FY 2011. Many offering frauds involved Ponzi schemes, investment frauds that involve the payment of purported returns to existing investors from funds contributed by new investors. Ponzi scheme organizers often solicit new investors by promising to invest funds in opportunities claimed to generate high returns with little or no risk. In many Ponzi schemes, the fraudsters focus on attracting new money to make promised payments to earlier-stage investors and to use for personal expenses, instead of engaging in any legitimate investment activity.

In FY 2011, the Commission continued to vigorously pursue individuals involved in the \$50 billion Madoff Ponzi scheme.

In November, the SEC charged a pair of longtime employees at Bernard L. Madoff Investment Securities LLC (BMIS) for their roles in the scheme.<sup>54</sup> The SEC alleged that Annette Bongiorno produced phony account statements for investors and feathered her own accounts for personal gain. A second employee, JoAnn Crupi, allegedly conspired to cash out Madoff’s friends and family as the fraud collapsed, in addition to creating phony account statements and tracking the Ponzi scheme bank account. In June, the Commission charged a third employee, Eric Lipkin, who for more than a decade helped Madoff defraud investors and mislead auditors and regulators about Madoff’s fraudulent, multi-billion dollar advisory operations.<sup>55</sup> Lipkin consented to the entry of a permanent injunction, with the monetary relief to be determined by the court at a later date. The SEC’s case against Bongiorno and Crupi continues.

In October, the SEC charged an Internet-based investment company with securities fraud for soliciting several million dollars from U.S. investors and promising them guaranteed returns of 1.2 percent per day while in reality siphoning the funds into foreign bank accounts and not paying a single penny back to investors.<sup>56</sup> The SEC obtained an emergency court order freezing the assets of Imperia Invest IBC, which allegedly raised more than \$7 million from approximately 14,000 investors worldwide. More than half the funds were collected from U.S. investors who are members of the Deaf community. Imperia offered the investment opportunity through its Web site by touting such lucrative examples as a \$50 investment turning into a \$134,000 return in six months. Imperia’s Web site stated that investors could only access their profits by purchasing a Visa debit card from Imperia for a few hundred dollars. However, Imperia had no relationship with Visa and was using the Visa name without authorization. In a related action, the SEC charged Jody Dunn for soliciting more than \$3.45 million from several thousand deaf investors in the scheme. The litigation against Dunn continues.<sup>57</sup>

<sup>53</sup> SEC v. Mark Anthony Longoria, et al., Lit. Release No. 21844 (Feb. 8, 2011) <http://www.sec.gov/news/press/2011/2011-40.htm>

<sup>54</sup> SEC v. Joanne Crupi; SEC v. Annette Bongiorno, Lit. Rel. No. 21750 (November 18, 2010) <http://www.sec.gov/litigation/litreleases/2010/lr21750.htm>

<sup>55</sup> SEC v. Eric Lipkin, Press Rel. No. 2011-219 (June 6, 2011) <http://www.sec.gov/news/press/2011/2011-119.htm>

<sup>56</sup> SEC v. Imperia Invest IBC, Lit. Rel. No. 21686 (October 7, 2010) <http://www.sec.gov/litigation/litreleases/2010/lr21686.htm>

<sup>57</sup> SEC v. Jody Dunn, Lit. Rel. No. 22090 (September 12, 2011) <http://www.sec.gov/litigation/litreleases/2011/lr22090.htm>

Additionally, the Commission sued two Florida men for operating a Ponzi scheme disguised as a purported private equity fund that fraudulently raised approximately \$22 million from more than 100 investors, many of whom were Florida teachers or retirees.<sup>58</sup> The SEC's complaint alleged that James Davis Risher, a convicted felon, and Daniel Joseph Sebastian falsely told investors that the fund earned annual returns ranging from 14 percent to 124 percent by investing in public equity securities through a broker-dealer. They sent investors fabricated account statements indicating such high returns to support their false claims. Only a fraction of the money raised was actually invested, with the remainder misappropriated to pay for such unauthorized purchases as jewelry, gifts, and real estate in North Carolina and Florida. The defendants also paid themselves millions of dollars in phony management and performance fees. The SEC's litigation of this case is ongoing. Risher has pled guilty in a related criminal action.

In January, the SEC filed an emergency action in Federal district court and obtained an asset freeze against Connecticut-based registered investment adviser MK Capital Management, LLC and its principal, Francisco Illarramendi, charging that they had misappropriated at least \$53 million in investor assets.<sup>59</sup> The Commission subsequently amended that complaint to allege that Illarramendi and MK Capital misappropriated investor assets and misused two hedge funds they managed for Ponzi-like activity in which they used new investor money to pay off earlier investors. In addition, the SEC added Highview Point Partners LLC as a defendant in the case, and three hedge funds managed by Highview and several entities affiliated with MK Capital as relief defendants, because they were alleged to be in possession of funds tainted by the Ponzi scheme. In June, the court entered an order freezing the assets of the hedge funds and ordered that all assets of the hedge funds, including \$230 million held in offshore accounts, be repatriated to the United States.<sup>60</sup>

Separately, the SEC filed an administrative action against Illarramendi permanently barring him from the industry.<sup>61</sup>

In another action, the SEC charged two hedge fund managers and their firms with fraudulently funneling more than a billion dollars of investor money into a Ponzi scheme operated by Minnesota businessman Thomas Petters.<sup>62</sup> The SEC's complaint alleged that Bruce F. Prévost and David W. Harrold falsely assured investors and potential investors that their funds would be safeguarded by collateral accounts and described a phony process for protecting their assets. When Petters was unable to make payments on investments held by the funds they managed, the defendants and their firms concealed it from investors by engaging in sham note exchange transactions with Petters. To settle the charges against them, the defendants agreed to be permanently enjoined, with the amount of disgorgement and penalties to be determined at a later date.

In March, the SEC charged three executives at Ohio-based Fair Finance Company with orchestrating a \$230 million offering fraud involving at least 5,200 investors, many of them elderly, through the sale of investment certificates by making misrepresentations concerning, among other things, the safety and security of investors' principal and the use of investor proceeds.<sup>63</sup> As part of the scheme, defendants used new investor proceeds to repay earlier investors in the nature of a Ponzi scheme. The SEC's case against the executives continues.

In May, the SEC obtained emergency relief to halt a Ponzi scheme perpetrated by the co-founder of China Voice Holding Corp. and two of his associates that sought to raise at least \$8.6 million from investors across the country.<sup>64</sup> Investors were falsely told that their investments would earn returns of at least 25 percent. Instead, proceeds raised from investors were used to pay back earlier investors as well as to make unauthorized payments that enriched the defendants

<sup>58</sup> *SEC v. James Davis Risher and Daniel Joseph Sebastian*, Lit. Rel. No. 22077 (August 31, 2011) <http://www.sec.gov/litigation/litreleases/2011/lr22077.htm>

<sup>59</sup> *SEC v. Francisco Illarramendi, et al.*, Lit. Rel. No. 21828 (January 28, 2011) <http://www.sec.gov/litigation/litreleases/2011/lr21828.htm>

<sup>60</sup> *SEC v. Francisco Illarramendi, et al.*, Lit. Rel. No. 22015 (June 28, 2011) <http://www.sec.gov/litigation/litreleases/2011/lr22015.htm>

<sup>61</sup> *In the Matter of Francisco Illarramendi, Investment Adviser's Act* Rel. No. 3257 (Aug. 3, 2011) <http://www.sec.gov/litigation/admin/2011/ia-3257.pdf>

<sup>62</sup> *SEC v. Bruce F. Prévost, et al.*, Lit. Rel. No. 21694 (October 14, 2010) <http://www.sec.gov/litigation/litreleases/2010/lr21694.htm>

<sup>63</sup> *SEC v. Timothy S. Durham, et al.*, Lit. Rel. No. 21888 (March 16, 2011) <http://www.sec.gov/litigation/litreleases/2011/lr21888.htm>

<sup>64</sup> *SEC v. David Ronald Allen, et al.*, Lit. Rel. No. 21953 (May 3, 2011) <http://www.sec.gov/litigation/litreleases/2011/lr21953.htm>

and their families. Several of the defendants implicated in the scheme have agreed to settle the actions against them by consenting to the entry of a permanent injunction, with the financial penalties to be determined at a later date. The litigation against certain other defendants is continuing.

In another action, the Commission charged the owner of the Little Loan Shoppe - a payday loan business - with conducting a massive Ponzi scheme and stealing investor money to fund her home improvement projects, gambling jaunts to Las Vegas, and purchases of a Corvette and a Mercedes.<sup>65</sup> The SEC alleged that Doris E. Nelson of Colbert raised approximately \$135 million from at least 650 investors and defrauded these investors by misrepresenting the profitability and safety of their investments and giving them the false impression that their money was being used to grow her business. In truth, Nelson used the vast majority of new investor money to repay principal and purported returns to earlier investors. Nelson also allegedly misappropriated millions of dollars in investor funds for her personal use. The litigation of this case continues.

### Actions Involving Market Manipulation

In FY 2011, the Commission brought a variety of actions against individuals and entities engaged in market manipulation. In October, the SEC charged more than a dozen penny stock promoters and their companies with securities fraud for their roles in various illicit kickback schemes to manipulate the volume and price of microcap stocks and illegally generate stock sales.<sup>66</sup> The defendants, who were all insiders or promoters of publicly-traded microcap companies, sought to manipulate the volume and price of microcap stocks and to generate stock sales through the payment of illegal kickbacks. As part of a sting operation, the defendants wrongly thought they were paying off corrupt pension fund managers, stockbrokers, or promoters. In related criminal prosecutions, the U.S. Attorney's Office for the Southern District of Florida

filed criminal charges against some of the same individuals the SEC sued. Similarly, in December 2010 and June 2011, the Commission collectively charged four more CEOs, and their companies, and three penny stock promoters with securities fraud for their roles in various schemes to manipulate the volume and price of microcap stocks and illegally generate stock sales.<sup>67</sup> The schemes featured illicit kickbacks, bribes to a purported corrupt broker, and the creation of a Web site to deliver e-mail blasts to potential investors. These cases are ongoing.

In another action, the SEC sued a group of seven individuals who perpetrated a fraudulent pump-and-dump scheme in the stock of a sham company that purported to provide products and services to fight global warming.<sup>68</sup> The SEC alleged that the group included stock promoters, traders, and a lawyer who wrote a fraudulent opinion letter, and the head of an offshore asset protection company that effected pump-and-dump schemes on behalf of his clients. The DOJ filed related criminal charges against six of the individuals. The scheme resulted in more than \$7 million in illicit profits from sales of stock in CO2 Tech Ltd. at artificially inflated prices. Despite touting impressive business relationships and anti-global warming technology innovations, CO2 Tech did not have any significant assets or operations. The company was purportedly based in London, and its stock prices were quoted in the Pink Sheets. The litigation is continuing.

In June, the Commission suspended trading in 17 microcap stocks based on questions about the adequacy and accuracy of publicly-available information about the companies, which trade in the over-the-counter (OTC) market.<sup>69</sup> The trading suspensions were the result of a joint investigation by multiple SEC offices, the SEC's Office of Market Intelligence, and its Microcap Fraud Working Group, which uses a coordinated proactive approach to detecting and deterring fraud involving microcap securities. The SEC's investigation is ongoing.

<sup>65</sup> *SEC v. Doris E. Nelson*, Lit. Rel. No. 22101 (September 22, 2011) <http://www.sec.gov/litigation/litreleases/2011/lr22101.htm>

<sup>66</sup> *SEC v. Scott R. Sand, et al.*; *SEC v. Jeffrey Galpern*; *SEC v. Jean R. Charbit, et al.*; *SEC v. Anthony Mellone, et al.*; *SEC v. Bruce Palmer, et al.*; *SEC v. John "Buckeye" Epstein, e. al.*; Lit. Rel. No. 21691 (October 7, 2010) <http://www.sec.gov/litigation/litreleases/2010/lr21691.htm>

<sup>67</sup> *SEC v. Brian Gibson*; *SEC v. Douglas Newton, et al.*; *SEC v. Donald W. Klein, et al.*; *SEC v. Thomas Schroepfer, et al.*; Lit. Rel. No. 22018 (June 30, 2011) <http://www.sec.gov/litigation/litreleases/2011/lr22018.htm>

<sup>68</sup> *SEC v. Jonathan R. Curshen, et al.*, Lit. Rel. No. 21862 (February 18, 2011) <http://www.sec.gov/litigation/litreleases/2011/lr21862.htm>

<sup>69</sup> *In the Matter of American Pacific Rim Commerce Group, et al., Order of Suspension of Trading* (June 7, 2011) <http://www.sec.gov/litigation/suspensions/2011/34-64612-o.pdf>

## Appendix C: SEC Divisions and Offices

### Headquarters Offices

#### **DIVISION OF CORPORATION FINANCE**

Meredith B. Cross, Director  
(202) 551-3110

#### **DIVISION OF ENFORCEMENT**

Robert S. Khuzami, Director  
(202) 551-4500

#### **DIVISION OF INVESTMENT MANAGEMENT**

Eileen Rominger, Director  
(202) 551-6720

#### **DIVISION OF TRADING AND MARKETS**

Robert W. Cook, Director  
(202) 551-5500

#### **DIVISION OF RISK, STRATEGY, AND FINANCIAL INNOVATION**

Craig Lewis, Director and Chief Economist  
(202) 551-6655

#### **OFFICE OF THE CHIEF OPERATING OFFICER**

Jeffery Heslop, Chief Operating Officer  
(202) 551-2105

#### **OFFICE OF COMPLIANCE INSPECTIONS AND EXAMINATIONS**

Carlo V. di Florio, Director  
(202) 551-6200

#### **OFFICE OF THE GENERAL COUNSEL**

Mark D. Cahn, General Counsel  
(202) 551-5100

#### **OFFICE OF THE CHIEF ACCOUNTANT**

James L. Kroeker, Chief Accountant  
(202) 551-5300

#### **OFFICE OF INVESTOR EDUCATION AND ADVOCACY**

Lori Schock, Director  
(202) 551-6500

#### **OFFICE OF INTERNATIONAL AFFAIRS**

Ethiopia Tafara, Director  
(202) 551-6690

#### **OFFICE OF FREEDOM OF INFORMATION ACT, RECORDS MANAGEMENT, AND SECURITY**

Barry Walters, Director/Chief FOIA Officer  
(202) 551-8400

#### **OFFICE OF ADMINISTRATIVE LAW JUDGES**

Brenda P. Murray,  
Chief Administrative Law Judge  
(202) 551-6030

#### **OFFICE OF LEGISLATIVE AND INTERGOVERNMENTAL AFFAIRS**

Eric J. Spitzer, Director  
(202) 551-2010

#### **OFFICE OF PUBLIC AFFAIRS**

John Nester, Director  
(202) 551-4120

#### **OFFICE OF THE SECRETARY**

Elizabeth M. Murphy, Secretary  
(202) 551-5400

#### **OFFICE OF FINANCIAL MANAGEMENT**

Kenneth A. Johnson,  
Chief Financial Officer  
(202) 551-4306

#### **OFFICE OF HUMAN RESOURCES**

Cristin C. Fair, Acting Director  
(202) 551-7500

#### **OFFICE OF ADMINISTRATIVE SERVICES**

Jayne Seidman, Acting Director  
(202) 551-4301

#### **OFFICE OF INFORMATION TECHNOLOGY**

Thomas A. Bayer,  
Chief Information Officer  
(202) 551-7259

#### **OFFICE OF EQUAL EMPLOYMENT OPPORTUNITY**

Alta G. Rodriguez, Director  
(202) 551-6040

#### **OFFICE OF INSPECTOR GENERAL**

H. David Kotz, Inspector General  
(202) 551-6061

#### **OFFICE OF MINORITY AND WOMEN INCLUSION**

Alta G. Rodriguez, Acting Director  
(202) 551-6040

## Regional Offices

### NEW YORK REGIONAL OFFICE

George S. Canellos,  
Regional Director  
3 World Financial Center,  
Room 400  
New York, NY 10281  
(212) 336-1100  
e-mail: newyork@sec.gov

### BOSTON REGIONAL OFFICE

David P. Bergers, Regional Director  
33 Arch Street, Floor 23  
Boston, MA 02110  
(617) 573-8900  
e-mail: boston@sec.gov

### PHILADELPHIA REGIONAL OFFICE

Daniel M. Hawke, Regional Director  
The Mellon Independence Center  
701 Market Street, Suite 2000  
Philadelphia, PA 19106  
(215) 597-3100  
e-mail: philadelphia@sec.gov

### MIAMI REGIONAL OFFICE

Eric Bustillo, Regional Director  
801 Brickell Avenue, Suite 1800  
Miami, FL 33131  
(305) 982-6300  
e-mail: miami@sec.gov

### ATLANTA REGIONAL OFFICE

Rhea Kemble Dignam,  
Regional Director  
3475 Lenox Road, N.E., Suite 1000  
Atlanta, GA 30326  
(404) 842-7600  
e-mail: atlanta@sec.gov

### CHICAGO REGIONAL OFFICE

Merri Jo Gillette, Regional Director  
175 W. Jackson Boulevard,  
Suite 900  
Chicago, IL 60604  
(312) 353-7390  
e-mail: chicago@sec.gov

### DENVER REGIONAL OFFICE

Donald M. Hoerl, Regional Director  
1801 California Street, Suite 1500  
Denver, CO 80202  
(303) 844-1000  
e-mail: denver@sec.gov

### FORT WORTH REGIONAL OFFICE

David R. Woodcock, Jr., Regional Director  
Burnett Plaza, Suite 1900  
801 Cherry Street, Unit 18  
Fort Worth, TX 76102  
(817) 978-3821  
e-mail: dfw@sec.gov

### SALT LAKE REGIONAL OFFICE

Kenneth D. Israel, Jr.,  
Regional Director  
15 W. South Temple Street  
Suite 1800  
Salt Lake City, UT 84101  
(801) 524-5796  
e-mail: saltlake@sec.gov

### LOS ANGELES REGIONAL OFFICE

Rosalind R. Tyson, Regional Director  
5670 Wilshire Boulevard, Floor 11  
Los Angeles, CA 90036  
(323) 965-3998  
e-mail: losangeles@sec.gov

### SAN FRANCISCO REGIONAL OFFICE

Marc J. Fagel, Regional Director  
44 Montgomery Street, Suite 2600  
San Francisco, CA 94104  
(415) 705-2500  
e-mail: sanfrancisco@sec.gov

## Appendix D: Acronyms

---

ABS	Asset-Backed Securities	FBWT	Fund Balance with Treasury
ADR	American Depository Receipts	FCPA	Foreign Corrupt Practices Act
ATS	Alternative Trading System	FDA	U.S. Food and Drug Administration
BCG	Boston Consulting Group	FECA	Federal Employees' Compensation Act
CCO	Chief Compliance Officer	FEGLIP	Federal Employees Group Life Insurance Program
CCOutreach	Chief Compliance Officer Outreach	FEHBP	Federal Employees Health Benefits Program
CDO	Collateralized Debt Obligation	FERS	Federal Employees Retirement System
CEO	Chief Executive Officer	FFMIA	Federal Financial Management Improvement Act
CF	Division of Corporation Finance	FINRA	Financial Industry Regulatory Authority
CFO	Chief Financial Officer	FISMA	Federal Information Security Management Act
CFR	Code of Federal Regulations	FLRA	Federal Labor Relations Authority
CFTC	Commodity Futures Trading Commission	FMFIA	Federal Managers' Financial Integrity Act
Commission	U.S. Securities and Exchange Commission	FOIA	Freedom of Information Act
COO	Chief Operating Officer	FSOC	Financial Stability Oversight Council
COSRA	Council of Securities Regulators of the Americas	FSSP	Federal Shared Service Provider
CSIP	College of Securities and Investor Protection	FTE	Full-Time Equivalent
CSRS	Civil Service Retirement System	Funds	Treasury Appropriation Fund Symbols
Dodd-Frank Act	Dodd-Frank Wall Street Reform and Consumer Protection Act	FY	Fiscal Year
DOI	U.S. Department of Interior	GAAP	Generally Accepted Accounting Principles
DOJ	U.S. Department of Justice	GAO	U.S. Government Accountability Office
DOL	U.S. Department of Labor	GSA	U.S. General Services Administration
DPA	Deferred Prosecution Agreement	IAPD	Investment Adviser Public Disclosure System
ECN	Electronic Communications Network	ICFR	Internal Control over Financial Reporting
EDGAR	Electronic Data Gathering, Analysis, and Retrieval System	IM	Division of Investment Management
EMMA	Electronic Municipal Market Access	IT	Information Technology
ESD	Equity Strategy Desk	IOSCO	International Organization of Securities Commissions
Exchange Act	Securities Exchange Act of 1934	IPERA	Improper Payments Elimination and Recovery Act
FACTS	Federal Agencies' Centralized Trial-Balance System	IPIA	Improper Payments Information Act of 2002
FAR	Federal Acquisition Regulation		

LBP	Liability to Benefits Paid	Regulation FD	Regulation Fair Disclosure
LLC	Limited Liability Corporation	RSFI	Division of Risk, Strategy, and Financial Innovation
MD&A	Management's Discussion and Analysis	S/L	Straight-Line Basis
MSRB	Municipal Securities Rulemaking Board	SBR	Statement of Budgetary Resources
MUI	Matter Under Inquiry	SDR	Swap Data Repository
N/A	Not Applicable	SEC	U.S. Securities and Exchange Commission
NAL	No-Action Letters	Securities Act	Securities Act of 1933
NASAA	North American Securities Administrators Association	SIPA	Securities Investor Protection Act of 1970
NASD	National Association of Securities Dealers	SIPC	Securities Investor Protection Corporation
NAV	Net Asset Values	SRO	Self-Regulatory Organization
NEP	National Exam Program	SWG	Specialized Working Group
NOC	Network Operations Center	TARP	Troubled Asset Relief Program
NRSRO	Nationally Recognized Statistical Rating Organization	TBD	To Be Determined
NTEU	National Treasury Employees Union	TCR	Tips, Complaints and Referrals
NYSE	New York Stock Exchange	TM	Division of Trading and Markets
OCA	Office of the Chief Accountant	Treasury	U.S. Department of the Treasury
OCIE	Office of Compliance Inspections and Examinations	UDA	User Developed Application
OFM	Office of Financial Management	VERA	Voluntary Early Retirement Authority
OGC	Office of General Counsel		
OHR	Office of Human Resources		
OIA	Office of International Affairs		
OIEA	Office of Investor Education and Advocacy		
OIG	Office of Inspector General		
OIT	Office of Information Technology		
OMB	Office of Management and Budget		
OMWI	Office of Minority and Women Inclusion		
OPM	Office of Personnel Management		
OTC	Over-the-Counter		
PCAOB	Public Company Accounting Oversight Board		
PIPE	Private Investment/Public Entity		
PMIS	Performance Management Information System		



This Performance and Accountability Report was produced through the energies and talents of the SEC staff. To these individuals we offer our sincerest thanks and acknowledgement. We would also like to acknowledge the Government Accountability Office and the SEC's Office of Inspector General for the professional manner in which they conducted the audit of the FY 2011 financial statements. Finally, we offer special thanks to AOC Solutions and The DesignPond for their contributions in the design and production of this report. To comment on, or obtain additional copies of the SEC's FY 2011 Performance and Accountability Report, please send an e-mail to: [SECPAR@sec.gov](mailto:SECPAR@sec.gov).



**U.S. SECURITIES AND EXCHANGE COMMISSION**

100 F Street, NE, Washington, DC 20549

