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# **Management Report to Accompany the Semiannual Report of the Inspector General**

for the period April 1, 2010 through September 30, 2010

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**U.S. Securities and Exchange Commission**

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**November 2010**

**U.S. SECURITIES AND EXCHANGE COMMISSION**

**MANAGEMENT REPORT TO ACCOMPANY THE  
SEMIANNUAL REPORT OF THE INSPECTOR GENERAL  
(APRIL 1 – SEPTEMBER 30, 2010)**

Section 5(b) of the Inspector General Act of 1978, as amended, requires the Commission to transmit to the appropriate committees or subcommittees of the U.S. Congress a Management Report, containing certain statistical tables and any comments deemed appropriate, to accompany the Office of Inspector General's ("OIG's") Semiannual Report. This Management Report presents the required information for the reporting period between April 1 and September 30, 2010.

## I. OVERVIEW OF AUDIT FOLLOW-UP ACTIVITIES

This section provides a summary of actions taken by the U.S. Securities and Exchange Commission (“SEC”) to follow up on OIG recommendations during the six-month reporting period.

Timely completion of audit recommendations is a priority for the SEC. In keeping with that focus, in 2009 the agency strengthened internal policies and procedures with respect to audit follow-up activities by adopting SEC Administrative Regulation (SEC-R) 30-2 (“Audit Follow-up and Resolution”). During the reporting period, the Office of the Executive Director (“OED”) worked closely with SEC offices in obtaining supporting documentation to close numerous audit recommendations. OED also received regular updates from offices on the progress of audit resolution and corrective actions, and provided periodic reports to the Office of the Chairman on the status of audit follow-up activity.

**Table 1. Summary of SEC Audit Follow-Up Activity**

| <i>OIG Recommendations</i>               | <i>Total</i> |
|--|--------------|
| Pending at the start of the period       | 157          |
| Completed <sup>1</sup> during the period | - 80         |
| Issued during the period                 | + 96         |
| Pending at the end of the period         | = 173        |

The SEC began the reporting period with 157 pending OIG recommendations.<sup>2</sup> During the reporting period, SEC offices completed corrective action on 80 recommendations. Also during the period, OIG issued 96 new recommendations. As a result, the SEC ended the reporting period with 173 pending OIG recommendations.

Of the 80 recommendations on which corrective action was completed during the reporting period, 71 have to date been closed with OIG concurrence. With respect to the remaining nine, documentation of corrective actions taken has been submitted to OIG and a final closure decision is pending. In addition to recommendations completed in the

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<sup>1</sup> A completed recommendation is a recommendation on which management has completed corrective action. The SEC’s established audit follow-up procedures require management to submit appropriate documentation of completed actions to OIG for review, and require concurrence by OIG or by the agency’s designated audit follow-up official before a recommendation is formally closed in the agency’s audit recommendation tracking system.

<sup>2</sup> This includes the 154 recommendations that were reported, in the previous Management Report, as pending as of April 1, 2010. It also includes three recommendations (446A #21, ROI-502 #1, and 455 #1) that had been reported as completed in the prior period but for which management in the current period agreed to take additional corrective actions. As a result, management has adjusted, from 133 to 130, the number of recommendations completed during the previous period, which also results in an adjustment, from 154 to 157, in the number of recommendations pending as of the start of the current period.

current period, OIG has to date affirmed management's decision to close 40 of the 48 remaining recommendations on which corrective action was completed in prior semiannual reporting periods.

In total, SEC offices have completed corrective action on 313 OIG recommendations over the past 18 months (April 1, 2009 to September 30, 2010). This is a rate of audit follow-up activity that is double that of the comparable preceding period, during which time the agency completed action on 155 OIG recommendations.

SEC management made it a particular priority to take timely action with respect to lessons learned from the agency's failure prior to 2008 to detect Bernard L. Madoff's ponzi scheme. This includes taking immediate and long-term actions (detailed at [www.sec.gov/spotlight/secpostmadoffreforms.htm](http://www.sec.gov/spotlight/secpostmadoffreforms.htm)) to reduce the chances that such frauds will occur or be undetected in the future, and also addressing the 69 recommendations for management action contained in three Madoff-related audit reports (Reports #467, 468, and 470) issued by OIG during the fall of 2009. Six months ago, in the Management Report for the period ending March 31, 2010, the SEC reported that it had completed corrective action on 35 of the 69 recommendation. During the current reporting period, SEC offices completed corrective action on all of the remaining 34 recommendations. With respect to all 69 recommendations, corrective action was completed within one year, and OIG also agreed that the recommendations have been addressed and are considered closed.

During the reporting period, OIG issued 96 new recommendations for management action. These were the result of six audit reports that contained 79 recommendations, and five investigations and preliminary investigations that contained 17 recommendations.

## **II. REPORTS WITH MONETARY SAVINGS**

Sections 5(b)(2) and (3) of the Inspector General Act require the SEC Management Report to include statistical tables summarizing the progress that the agency has taken on audit reports, inspection reports, and evaluation reports containing "disallowed costs" and "recommendations that funds be put to better use."

*Disallowed Costs.* Whenever OIG questions whether costs incurred by the agency are necessary, supported by adequate documentation, or in accordance with law, regulation, or contracts governing the use of funds, SEC management will review the facts and determine whether such costs should be officially disallowed. If the SEC agrees that such costs should not be charged to the government, the agency will then take appropriate action, such as commencing collection efforts to recover the disallowed costs.

*Funds Put to Better Use.* Whenever OIG recommends specific dollar amounts that it believes can be saved by improving the efficiency of agency operations, SEC management will review the facts and determine whether to implement such recommendations. "Funds put to better use" refers to the specific dollar value of cost

savings that the SEC has agreed can and should be implemented through appropriate corrective action.

Table 2 (below) presents the required information on audit, inspection, and evaluation reports with disallowed costs or recommendations that funds be put to better use.

**Table 2. Status of Final Action on Audit, Inspection, and Evaluation Reports with Disallowed Costs or Funds Put to Better Use**

| <i>Audit, Inspection, and Evaluation Reports...</i>   | <i>Number</i> | <i>Dollar Value of Disallowed Costs</i> | <i>Dollar Value of Funds Put to Better Use</i> |
|---|---------------|---|--|
| A. For which final action had not been taken by the beginning of the reporting period (4/1/10)                                      | 1             | \$20,076                                | \$0  |
| B. On which management decisions were made during the reporting period (4/1/10 – 9/30/10)   | 1             | \$0                                     | \$6,832,414                                    |
| C. For which final action was taken during the reporting period   | 0             |   |  |
| (i) Dollar value of disallowed costs that were recovered through collection, offsets, property in lieu of cash, or otherwise        |               | \$5,700                                 | ---  |
| (ii) Dollar value of disallowed costs that were written off by management   |               | \$0                                     | ---  |
| (iii) Dollar value of recommendations that were actually completed  |               | ---                                     | \$4,454,202                                    |
| (iv) Dollar value of recommendations that management has subsequently concluded should not or could not be implemented or completed |               | ---                                     | \$0  |
| D. For which no final action has been taken by the end of the reporting period (9/30/10)  | 2             | \$14,376                                | \$2,378,212                                    |

In addition to the information required by the Inspector General Act, SEC management is providing additional information (see Table 3, on the following page) on the status of management’s ongoing actions with respect to individual OIG reports with disallowed costs or funds put to better use. This supplemental information is, among other things, intended to make it easier to understand how management’s actions on these reports relate to the summary data included in Table 2 of the OIG Semiannual Report, which includes cost savings identified not only in OIG audit, inspection, and evaluation reports but also in investigative reports.

**Table 3. Status of Specific OIG Reports with Questioned Costs and Recommendations that Funds be Put to Better Use (Includes Investigative Reports)**

| <i>Report</i>                       | <i>Savings Identified by OIG</i> | <i>Amount Sustained by Management</i> | <i>Amount Collected, Written Off, or Put to Better Use as of 9/30/10</i> | <i>Amount Remaining as of 10/1/10</i> | <i>Status of Final Action</i>   |
|-------------------------------------|----------------------------------|---------------------------------------|--|---------------------------------------|---|
| 439, Student Loan Program (3/27/08) | \$129,336                        | \$129,336                             | \$114,960  | \$14,376                              | Management to date has taken final action with respect to \$114,960 (89%) of the disallowed costs, which included the collection of \$5,700 during the reporting period. Of the four remaining former employees with balances due, two are on payment plans to collect the remaining debt by 2011 and the other two have been referred to Treasury for debt collection. (Since management and OIG successfully resolved this report in a prior period, this report is not among those included in Table 2 of OIG's Semiannual Report.)  |
| ROI-492 (3/18/09)                   | \$5,312                          | \$1,733                               | \$0  | \$1,733                               | This Investigative Report uncovered instances of time and attendance abuse by an SEC employee. Management has removed the employee from federal service. Management also charged the employee with being Absent Without Leave (AWOL) for 36.7 hours which was previously paid, which equated to \$1,733 in excess salary. In consideration of potential litigation, management only charged as AWOL those hours when the employee worked less than eight hours per day. During the reporting period, management notified the former employee of the existence of this debt and began collection efforts. (This report corresponds to one of the two reports included in Table 2, Row C of OIG's Semiannual Report.) |
| ROI-504 (9/30/09)                   | \$25,000                         | \$0                                   | \$0  | \$0                                   | This Investigative Report centered on allegations of misconduct by an SEC employee who received an early retirement buyout payment, and found that the former employee had violated SEC rules and policies regarding the use of SEC office equipment. Since the employee had already left SEC employment and there was no evidence of a violation in the terms of the buyout, management concluded that there would be no legal basis to pursue revocation of the buyout, and therefore is unable to sustain the amount as disallowed costs. (This report corresponds to one of the two reports included in Table 2, Row C of OIG's Semiannual Report.)   |

| <i>Report</i>                                     | <i>Savings Identified by OIG</i> | <i>Amount Sustained by Management</i> | <i>Amount Collected, Written Off, or Put to Better Use as of 9/30/10</i> | <i>Amount Remaining as of 10/1/10</i> | <i>Status of Final Action</i>   |
|---|----------------------------------|---------------------------------------|--|---------------------------------------|---|
| 460, Interagency Acquisition Agreements (3/26/10) | \$6,945,831                      | \$6,832,414                           | \$4,454,202  | \$2,378,212                           | Management concurred with OIG's recommendation to deobligate unused funds remaining on 23 expired Interagency Acquisition Agreements (IAAs). With respect to three of the expired IAAs (totaling \$113,417 in outstanding balances), these contracts were subsequently extended, and as a result these funds will not be deobligated. Of the remaining balances, management during the reporting period deobligated \$4,257,736 associated with eight of the expired IAAs and made ongoing payments of \$196,466 on three other IAAs, which reduced total outstanding balances by \$4,454,202. (These amounts are included in Table 2, Row E of OIG's Semiannual Report.) Management continues to review the 13 remaining IAAs with outstanding balances in order to determine how much of the \$2,378,212 in outstanding balances can be deobligated. (This amount is included in Table 2, Row D of OIG's Semiannual Report.) Under SEC policy, unused funds on expired IAAs cannot be deobligated until the acquisition closeout process is complete and final invoices have been paid. |
| ROI-524 (7/23/10)                                 | \$22,796                         | *                                     | *  | *                                     | This Investigative Report examined whether three headquarters SEC employees improperly used "leave without pay" to create a <i>de facto</i> part-time schedule without reducing benefits and leave accruals. As of the end of the reporting period, management was analyzing OIG's recommendation to determine an appropriate course of action. (This report corresponds to one of the four reports included in Table 2, Row D of OIG's Semiannual Report.)   |
| PI-09-103 (9/27/10)                               | \$5,568                          | *                                     | *  | *                                     | This Investigative Memorandum examined whether a regional office SEC employee improperly used "leave without pay" to create a <i>de facto</i> part-time schedule without reducing benefits and leave accruals. As of the end of the reporting period, management was analyzing OIG's recommendation to determine an appropriate course of action. (This report corresponds to one of the four reports included in Table 2, Row D of OIG's Semiannual Report.)   |
| 484, Real Property Leasing (9/30/10)              | \$203,000                        | *                                     | *  | *                                     | The questioned costs identified by OIG is an estimate of the amount paid between November 2009 and March 2010 as a result of hold-over costs associated with leased office space for the SEC's San Francisco Regional Office. Management in its comment letter acknowledged that there were costs associated with continuing the existing rental rate to provide time for a full and open competition for a new lease, and noted that the new lease that resulted from this competition resulted in savings of \$1.8 million, an amount well in excess of the cost of five months hold-over rent. As of the end of the reporting period, management was analyzing OIG's recommendation to determine an appropriate course of action. (This report corresponds to one of the four reports included in Table 2, Row D of OIG's Semiannual Report.)  |

\* Indicates that a management decision on the amount of cost savings to be sustained was pending as of September 30, 2010.

### **III. REPORTS MORE THAN ONE YEAR OLD WITH PENDING CORRECTIVE ACTION**

Section 5(b)(4) of the Inspector General Act requires the SEC Management Report to include a statement with respect to audit reports on which management decisions have been made but final action has not been taken, other than audit reports on which a management decision was made within the preceding year.

At the start of the reporting period, there were 85 pending OIG recommendations that were more than one year old or that would become more than one year old if not completed by September 30, 2010. SEC offices completed corrective action on 56 of these (66%) during the reporting period. This includes 51 recommendations for which OIG has to date affirmed management's decision to close, and five recommendations that have been sent to OIG and are awaiting a final closure decision. The SEC ended the reporting period with 29 pending recommendations that are more than one year old.

Table 4 (on the following page) presents the required information on OIG audit reports with open recommendations that are more than one year old as of the end of the reporting period. The table lists seven reports that contained 81 recommendations. Corrective action on 18 of these recommendations was pending as of September 30, 2010. With respect to the remaining 63 (78%), 60 have to date been closed with OIG concurrence, and three others have been sent to OIG and are awaiting a final closure decision.

Although the Inspector General Act does not require federal agencies to report on non-audit reports (such as inspections, evaluations, investigations, or memoranda to management) with pending recommendations that are more than one year old, SEC management is also providing this supplemental information (see Table 5). The table lists seven such reports that contained 69 recommendations. Corrective action on 11 of these recommendations was pending as of September 30, 2010. With respect to the remaining 58 (84%), 48 have to date been closed with OIG concurrence, while 10 others have been sent to OIG and are awaiting a final closure decision.

**Table 4. Audit Reports Open More Than One Year**

| <i>Audit Report No./Title</i>   | <i>Report Date</i> | <i>Funds Put to Better Use</i> | <i>Disallowed Costs</i> | <i>Status of Final Action</i>  |
|---|--------------------|--------------------------------|-------------------------|--|
| 439, Student Loan Program   | 3/27/08            | \$0                            | \$129,336               | 18 of 19 recommendations from this report have been closed. To address the one remaining recommendation, management is holding discussions with the National Treasury Employees Union on the process for handling excess Student Loan Program funds. If the Union does not agree with management's current process, this matter is expected to be addressed in the 2011 negotiations on a new Collective Bargaining Agreement.   |
| 446B, Oversight of Bear Stearns and Related Entities: Broker-Dealer Risk Assessment Program | 9/25/08            | \$0                            | \$0                     | Seven of 10 recommendations from this report have been closed. Management has completed action on one additional recommendation which is under OIG review. To address the remaining recommendations, in 2011 the Broker-Dealer Risk Assessment IT system is expected to be completely overhauled.  |
| 450, Practices Related to Naked Short Selling Complaints and Referrals                      | 3/18/09            | \$0                            | \$0                     | Eight of 11 recommendations from this report have been closed, including three that were closed during the reporting period. The future-state Tips, Complaints, and Referrals system will permit the agency to close the remaining recommendations. The target completion date is December 2010.   |
| 456, Transit Benefits Program   | 3/27/09            | \$0                            | \$549                   | Nine of 10 recommendations from this report have been closed. To address the final recommendation, new Transit Benefit Subsidy policy and procedures that address both headquarters and regional office programs are being developed, and are expected to be implemented by calendar year-end.   |
| 459, Regulation D Exemption Process   | 3/31/09            | \$0                            | \$0                     | 15 of 17 recommendations from this report have been closed, including all of the recommendations directed to the Division of Corporation Finance. To address the final two recommendations, an evaluation of authentication processes for the EDGAR system was completed during the reporting period. Management is currently considering the costs and benefits of potential solutions, which may require a fundamental change in EDGAR's unique requirements. The estimated completion date for this recommendation is dependent upon on the outcome of these deliberations. |

| <i>Audit Report No./Title</i>  | <i>Report Date</i> | <i>Funds Put to Better Use</i> | <i>Disallowed Costs</i> | <i>Status of Final Action</i>   |
|--|--------------------|--------------------------------|-------------------------|---|
| 461, Review of Commission's Restacking Project                             | 3/31/09            | \$0                            | \$0                     | One of four recommendations from this report has been closed. Management conducted a staff survey to address another recommendation and is presently in discussion with OIG regarding closure. The SEC also recently issued a new real leasing regulation to address another recommendation, and is in negotiations with the NTEU on a policy developed to address the final remaining recommendation.  |
| 471, Office of Acquisitions' Procurement and Contract Management Functions | 9/25/09            | \$0                            | \$0                     | Two of 10 recommendations from this report have been closed. Management completed corrective action on one additional recommendation and provided documentation to OIG in September 2010. Corrective action is expected to be completed on five additional recommendations during the second quarter of FY11. Management is reexamining its plan of action for the two remaining recommendations due to the agency's recent decision to replace its financial management system with a Shared Service Provider. |

**Table 5. Inspection, Evaluation, and Other Reports Open More Than One Year**

| <i>Report No./Title (Type)</i>   | <i>Report Date</i> | <i>Funds Put to Better Use</i> | <i>Disallowed Costs</i> | <i>Status of Final Action</i>   |
|--|--------------------|--------------------------------|-------------------------|---|
| 428, Electronic Documents Program (Evaluation)   | 7/25/07            | \$0                            | \$0                     | 17 of 19 recommendations from this report have been closed. To address the two remaining recommendations, the Division of Enforcement plans to issue new program guidance and standard operating procedures in conjunction with the deployment of the Commission's new e-Discovery system, which is scheduled for initial deployment at the end of the calendar year. |
| 455, Attorney Annual Certification of Bar Membership (Memorandum)  | 9/9/08             | \$0                            | \$0                     | During the reporting period, management instituted a new program to require SEC attorneys to annually certify their bar membership status. Shortly after the end of the reporting period, management provided documentation to OIG to close the recommendation in this memorandum.  |
| 464, Notification to OIG of Decisions on Disciplinary Action and Settlement Agreements Involving Subjects of OIG Investigations (Memorandum) | 1/23/09            | \$0                            | \$0                     | Management has taken corrective action in response to the two recommendations in this memorandum, and is presently in discussions with OIG regarding closure.   |

| <i>Report No./Title (Type)</i>   | <i>Report Date</i> | <i>Funds Put to Better Use</i> | <i>Disallowed Costs</i> | <i>Status of Final Action</i>   |
|--|--------------------|--------------------------------|-------------------------|---|
| ROI-481, Employee Securities Transactions (Investigative Report)                         | 3/3/09             | \$0                            | \$0                     | Nine of 11 recommendations from this investigative report have been closed. Management has completed final action on the two remaining recommendations and provided closing documentation to OIG after the period ended.  |
| 458, Oversight of Nationally Recognized Statistical Rating Organizations (Review)        | 8/27/09            | \$0                            | \$0                     | 12 of 24 recommendations from this report have been closed. Management has completed corrective action on five other recommendations and is presently in discussion with OIG regarding closure. Corrective action to address the remaining seven recommendations had initially been planned for completion during the reporting period, but was delayed in order to consider how best to implement the recommendations in light of the significant new credit rating agency provisions enacted as part of Dodd Frank Act. |
| 465, Review of the SEC's Compliance with the Freedom of Information Act (Inspection)     | 9/25/09            | \$0                            | \$0                     | Nine of 10 recommendations from this report have been closed. Management completed action on the final recommendation and is presently in discussions with OIG regarding closure.   |
| ROI-502, Allegations of Improper Disclosures and Assurances Given (Investigative Report) | 9/30/09            | \$0                            | \$0                     | Management in September 2010 completed corrective action on the two recommendations. At this writing, OIG has affirmed the closure of one of the two recommendations.   |