Written Testimony of H. David Kotz
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Before the Economic Development, Public Buildings and Emergency Management Subcommittee of the Committee on Transportation and Infrastructure,
U.S. House of Representatives

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Introduction

Thank you for the opportunity to testify before this Subcommittee on the lease of Constitution Center by the U.S. Securities and Exchange Commission (SEC or Commission). I appreciate the interest of the Chairman, the Ranking Member, and the other members of the Subcommittee, in the SEC and the Office of Inspector General (OIG). In my testimony, I am representing the OIG, and the views that I express are those of my Office, and do not necessarily reflect the views of the Commission or any Commissioners.

Role of and Reports Issued by the OIG

The mission of the OIG is to promote the integrity, efficiency and effectiveness of the critical programs and operations of the SEC. The OIG's audit unit conducts, coordinates and supervises independent audits and evaluations related to the internal programs and operations of the Commission. The Office's investigations unit conducts thorough and independent investigations in response to allegations of violations of statutes, rules, and regulations, and other misconduct by Commission staff and contractors.

Over the past three and one-half years since I became the Inspector General of the SEC, my Office has issued numerous audits and investigative reports involving matters critical to SEC programs and operations and the investing public. On the audit side, some of the significant reports we have issued have included an examination of the Commission's oversight of Bear Stearns and the factors that led to its collapse, a review of the SEC's bounty program for whistleblowers, an analysis of the SEC's oversight of credit rating agencies, and audits of the SEC's compliance with Homeland Security

Presidential Directive 12 and its oversight of the Securities Investment Protection Corporation's activities. Investigative reports issued during this same period have addressed a myriad of issues, including the failures of the SEC to uncover the Bernard Madoff $50 billion Ponzi scheme and the Robert Allen Stanford $8 billion alleged Ponzi scheme, improper securities trading by Commission employees, conflicts of interest by Commission staff members, post-employment violations, unauthorized disclosure of nonpublic information, and procurement violations.

Many of the reports we have issued have identified costs savings, including questioned costs and funds that could be put to better use. The OIG has calculated that for the period from October 1, 2009 through June 30, 2011, the return on investment for the OIG (*i.e.*, total identified costs savings divided by the OIG's budget) is 64.2 to 1.

The OIG's Leasing Investigation

On June 16, 2011, I testified before this Subcommittee about a May 16, 2011 report of investigation we issued into the circumstances surrounding the SEC's decision to lease approximately 900,000 square feet of office space at a newly-renovated office building known as Constitution Center.

As described in my previous testimony, we opened our investigation on November 16, 2010, as a result of receiving numerous written complaints concerning the SEC's decisions and actions relating to Constitution Center. These complaints alleged that the decision to lease space at Constitution Center was ill-conceived, resulted from poor management practices, and was made without Congressional funding for the significant projected growth necessary to support the decision.

My previous testimony described in detail our investigative efforts, including the review of over 1.5 million e-mails during the course of the investigation and the testimony or interviews of 29 individuals with knowledge of facts or circumstances surrounding the SEC's leasing activities.

I also testified concerning the results of our investigation, which found that the circumstances surrounding the SEC's entering into a lease for 900,000 square feet of space at the Constitution Center facility in July 2010 were part of a long history of missteps and misguided leasing decisions made by the SEC since it was granted independent leasing authority by Congress in 1990. The investigation further found that based upon estimates of increased funding, primarily to meet the anticipated requirements of financial reform legislation that was enacted on July 21, 2010, the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank), between June and July 2010, the SEC's Office of Administrative Services (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. Specifically, we found that OAS grossly overestimated (by more than 300 percent) the amount of space needed for the SEC's projected expansion and used these groundless and unsupportable figures to justify the SEC's commitment to an expenditure of approximately $557 million over 10 years.

In my earlier testimony, I also described how the OIG investigation found that OAS prepared a faulty Justification and Approval document to support entering into the lease for the Constitution Center facility without full and open competition. We determined that this Justification and Approval document was prepared after the SEC had already signed the contract to lease the Constitution Center facility. Further, we found

that OAS backdated the Justification and Approval, thereby creating the false impression that it had been prepared only a few days after the SEC entered into the lease when, in actuality, the Justification and Approval was not finalized until a month later. Additional details regarding the findings of our leasing investigation were provided in my June 16, 2011 testimony, as well as in the 91-page report of investigation with over 150 exhibits, which has been provided to the Subcommittee.

Recommendations of the OIG's Leasing Investigation

Our report of investigation made numerous recommendations designed to ensure that the requisite improvements to policies and procedures are made and that appropriate disciplinary action is taken. Specifically, we recommended that the SEC's Chief Operating Officer carefully review the report's findings and conduct a thorough and comprehensive review and assessment of all matters currently under the purview of OAS including, but not limited to:

(1) The adequacy of written policies and procedures currently in place for all aspects of the SEC's leasing program, including, but not limited to, putting in place written procedures for leasing approvals;

(2) The methods and processes utilized to accurately project spacing needs based on concrete and supportable data;

(3) The determination to employ a standard of 400 square feet per person for planning agency space needs;

(4) The necessity of retaining architects, furniture brokers, or other consultants to assist in the work generally performed by OAS officials; and

(5) All pending decisions in which OAS is committing the SEC to expend funds, including decisions relating to regional office lease renewals.

We further recommended that the Chief Operating Officer, upon conclusion of this review and assessment, determine the appropriate disciplinary and/or performance-based action to be taken for matters related to the findings in this report of investigation, as well as other issues identified during the review and assessment. We specified that such disciplinary action should include, at a minimum, consideration of disciplinary action, up to and including dismissal, against two senior individuals, and consideration of disciplinary action against a third individual, for their actions in connection with the gross overestimation of the amount of space needed at SEC Headquarters for the SEC's projected expansion, failures to provide complete and accurate information to the Chairman's office, and the preparation of a faulty and back-dated Justification and Approval to support eliminating competition.

Finally, we recommended that the Office of Financial Management, in consultation with the Office of General Counsel, request a formal opinion from the Comptroller General as to whether the Commission violated the Antideficiency Act, by failing to obligate appropriate funds for the Constitution Center lease.

Follow-Up Efforts

My Office is committed to following up with respect to all of the recommendations we made in our report of investigation to ensure that appropriate changes and improvements are made in the SEC's leasing operations as a result of our findings.

Subsequent to the issuance of our report of investigation on May 16, 2011, my Office has requested and received a corrective action plan with regard to the substantive recommendations we made for improvements in the operations of the Office of

Administrative Services. We will monitor the planned activities carefully to ensure that the necessary improvements are made. We have also communicated with the SEC's Office of General Counsel with regard to its review of the evidentiary record to determine appropriate disciplinary action, and have provided the Office of General Counsel with records requested to assist in those efforts. We intend to monitor the disciplinary process to ensure that the individuals who we identified as being responsible for the failures and improprieties described in our report are held appropriately accountable for their actions.

In addition to these efforts, we have met with the newly-installed acting head of the Office of Administrative Services to provide additional information concerning the failings and deficiencies we have identified in that Office. As a result of this briefing, a large renovation project that had been initiated by the previous head of the Office of Administrative Services has been discontinued.

We understand that the Chief Operating Officer, under the direction of Chairman Schapiro, has already begun to implement the improvements needed in the SEC's leasing functions. We are confident that under Chairman Schapiro's leadership, the SEC will continue to review our report and take appropriate steps to implement our recommendations and ensure that fundamental changes are made in the SEC's leasing operations so the errors and failings we found in our investigation are remedied and not repeated in the future.

Conclusion

In conclusion, I appreciate the interest of the Chairman, the Ranking Member, and the Subcommittee in the SEC and my Office and, in particular, in the facts and circumstances pertinent to our leasing report. I believe that the Subcommittee's and

Congress's continued involvement with the SEC is helpful to strengthen the accountability and effectiveness of the Commission. Thank you.