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THE SECURITIES AND EXCHANGE COMMISSION'S $500 MILLION FLEECING OF AMERICA

(112–37)

HEARING

BEFORE THE

SUBCOMMITTEE ON
ECONOMIC DEVELOPMENT, PUBLIC BUILDINGS, AND
EMERGENCY MANAGEMENT

OF THE

COMMITTEE ON
TRANSPORTATION AND
INFRASTRUCTURE
HOUSE OF REPRESENTATIVES

ONE HUNDRED TWELFTH CONGRESS

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June 10, 2011

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BRIEFING MEMORANDUM

TO: Members of the Subcommittee on Economic Development, Public Buildings, and Emergency Management
FROM: Subcommittee on Economic Development, Public Buildings, and Emergency Management Staff
SUBJECT: Oversight Hearing on "The Securities and Exchange Commission's $500 Million Fleecing of America"

PURPOSE

The Subcommittee on Economic Development, Public Buildings and Emergency Management will meet on Thursday, June 16, 2011, at 10:00 a.m. in 2167 Rayburn House Office Building to receive testimony from the U.S. Securities and Exchange Commission (SEC), the SEC Inspector General (SEC IG), and the General Services Administration (GSA). The hearing will focus on the SEC's management of its independent authority to lease space and, in particular, the Subcommittee will examine issues detailed in a May 16, 2011, SEC IG report related to SEC's most recent lease procurement of 900,000 square feet of space under a 10-year lease worth over $500 million. While GSA was not involved in the procurement of SEC's leased space, GSA will provide the Subcommittee with information on the processes and standards it uses to evaluate the need for new space and how it conducts procurements for leased space to assist the Subcommittee in better evaluating SEC's actions.

BACKGROUND

Public Buildings and Leases

The Subcommittee has jurisdiction over all of GSA's real property activity through the Property Act of 1949, the Public Buildings Act of 1959, and the Cooperative Use Act of 1976. These three Acts are now codified as title 40 of the United States Code. The GSA's Public Buildings Service (PBS) is responsible for the construction, repair, maintenance, alteration, and operation of United States courthouses and public buildings

of the Federal Government. Additionally, PBS leases privately owned space for Federal use. GSA owns or leases 9,600 assets and maintains an inventory of more than 362 million square feet of workspace. GSA acts as the "landlord" for the federal government, obtaining and managing space to meet the space needs of other federal agencies. GSA, however, is just one of nine[1] federal agencies that, in total, own or manage 93% of federal real property.

While GSA has generally been the "landlord" for the federal government for civilian properties, over time several agencies have obtained their own authority independent of GSA to procure and lease new space. As a result, authority to lease space has proliferated and, in some cases, to agencies that neither have the mission nor expertise to appropriately manage such authority. The SEC is one of those agencies that has been granted this authority.

SEC's Lease of 900,000 Square Feet at Constitution Center

On July 28, 2010, the SEC entered into a sole source lease for 900,000 square feet of space with an option to lease 500,000 additional square feet at Constitution Center located at 7th and D Streets, SW, in Washington, D.C. (A timeline related to the leasing of Constitution Center is attached). The SEC's rationale for the need for new space related to passage of Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank) which expanded SEC's responsibilities. The $556 million lease was "negotiated" in three business days and signed on July 28, 2010 and not long after it was signed questions were raised regarding whether the SEC needed the space. The building is owned by David Nassif Associates (Landlord) and is the former location of the Department of Transportation headquarters. The building was completely renovated by the Landlord to be a modern, efficient class A office building, reportedly exceeding Level IV security standards and is expected to be rated LEED Gold, a top green building certification. Following reports of the lease agreement, the SEC IG initiated an investigation into the lease. On May 16, 2011, the SEC IG concluded its investigation and, at the request of the Subcommittee, the SEC released the report to the Subcommittee.

Findings and Recommendations of the Inspector General

In the report, the SEC IG concluded: "[w]e found that OAS [Office of Administrative Services at SEC] grossly overestimated the amount of space needed at SEC Headquarters for the SEC's projected expansion by more than 300 percent and used these groundless and unsupportable figures to justify the SEC committing an expenditure of $556,811,589 over 10 years."[2] In fact, in the course of the SEC IG's investigation, one

[1] The other major land-holding departments and agencies include the Department of Defense, Veterans Affairs, Department of Energy, Department of Homeland Security, Department of the Interior, Department of State, National Aeronautics and Space Administration, and the U.S. Postal Service.
[2] *Improper Actions Relating to the Leasing of Office Space, Report of Investigation,* Office of the Inspector General, U.S. Securities and Exchange Commission, May 16, 2011 (OIG-553), p. 2.

SEC Realty Specialist described the standard used to develop the needed space figures "as a 'WAG' (wild-ass guess) and a 'back of the envelope' calculation."[3]

After the SEC recognized that it may not have needed the leased space, the Landlord worked with SEC to allow other federal agencies to assume portions of the lease. Since then, the Office of the Comptroller of the Currency (OCC) and the Federal Housing Finance Agency (FHFA) entered into leasing agreements for space at Constitution Center, leaving approximately 350,000 square feet remaining on SEC's lease. The Landlord, however, has claimed that SEC's actions have caused it to incur damages totaling more than $93 million.[4]

Key Findings of the Inspector General

- **Inflated Staffing Numbers:** SEC inflated the projected numbers of future employees, contractors, interns, and temporary workers to justify its space requirements, by assuming:
  - all new SEC positions would be located in D.C.;
  - a ratio of 20% -- contractors to employees (twice as much as is standard);
  - a ratio of 16.5% -- interns and temporary workers to employees, more than 3 times more than the actual ratio;
  - a 10% growth or "inventory" factor, double the standard;
  - SEC would obtain approval from OMB and Congress for the full SEC appropriation requests for FY2011, FY2012 and a 50% increase for FY2013.

- **Inflated Space Standards:** SEC further inflated the space requirements by using a standard of 400 square feet per person for needed space (GSA recommends 230 or lower). The use of this figure results in further inflation of the projected number of people. For example, the 400 square foot figure already includes 5% for growth and 10% for contractors and temporary workers.

- **Inflated Numbers Cut Viable Alternatives:** As a result of the inflated numbers, SEC's initial estimates that reflected a need for less than 300,000 square feet increased to more than 900,000 square feet. This led to the exclusion of a number of available commercial buildings in walking distance to the current SEC Headquarters near Union Station.

- **Lease Not Negotiated:** SEC signed an un-negotiated, 10-year lease just 5 days after approval by the Chairman of the SEC which was obtained in a meeting lasting approximately 10 minutes. The rush to sign the contract also led to the omission of standard lease terms intended to protect the government.

- **Violation of Contracting Rules:** SEC did not follow requirements of the Competition in Contracting Act (CCA) and the Federal Acquisition Regulations

[3] Id at p. 5.
[4] Id. at p. 10.

(FAR) that require full and open competition. An exception to this requirement can be "when the agency's need for the supplies or services is of such an unusual and compelling urgency that the Government would be seriously injured unless the agency is permitted to limit the number of sources from which it solicits bids or proposals."[5] The SEC IG concluded there was no unusual or compelling urgency or that the Government would be seriously injured had full and open competition occurred. In addition, the SEC IG found the *Justification and Approval For Other Than Full and Open Competition* generated by the SEC was publically noticed more than five weeks after the contract was signed (beyond the 30-day period required in the FAR); was backdated to make it appear it was approved earlier than it was; and had at least one date altered. Moreover, three of the four signatures required were signed separate from the document for which the signatories were attesting.

- **Lack of OMB Approval:** SEC may not have complied with OMB requirements for government leases by not submitting information to OMB pursuant to Appendix B of the OMB Circular No. A-11.

- **Possible Violation of Anti-deficiency Act:** The SEC may have violated the Anti-deficiency Act that prohibits officers or employees of the government from entering into an obligation or contract before an appropriation is made unless otherwise authorized by law.

- **Work Environment Discourages Questions:** The SEC IG found evidence of a rigid, closed, and hostile atmosphere within the Office of Administrative Services (OAS) (the SEC office responsible for leasing) that suggested employees with relevant experience were discouraged from questioning decisions.

Recommendations of the Inspector General

The IG recommended that the SEC:

"...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;

[5] Id. at p. 68 (quoting 48 CFR § 6.3202-2).

> (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.[6]"

The SEC IG further recommended that the "Chief Operating Officer/Executive Director, upon conclusion of such review and assessment, determine the appropriate disciplinary and/or performance-based action to be taken for matters that are discussed in this report of investigation, as well as any other issues identified during the review and assessment, including, at a minimum, consideration of disciplinary action against Sharon Sheehan and, up to and including dismissal..."[7]

Finally, the SEC IG 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."[8]

Problems Related to SEC Leases Pre-Date Constitution Center Lease

In 1990, Congress provided the SEC with independent leasing authority with the intent that such authority would be "exercised vigorously by the Commission to achieve actual savings and to increase the Commission's productivity and efficiency."[9] Despite this responsibility, the SEC did not establish a Leasing Branch until 2009, 19 years after being granted this authority. The SEC currently leases space in 12 cities[10] and the District of Columbia. These include its headquarters in D.C. and regional offices. The SEC manages approximately 2.4 million square feet of space at an average annual cost of $83 million. Questions regarding SEC's management of its leasing authority date back more than a decade. Some examples include:

- In 2001, the SEC leased space for its Regional Office in New York City and subsequently entered into a dispute with the landlord regarding the handling of asbestos allegedly found in the building. While the lease agreement assigned responsibility to the landlord, instead of addressing the issue, in 2004, the SEC issued a *Justification and Approval for Other than Full and Open Competition* to enter into a sole source lease agreement for other leased space. While SEC subsequently worked with GSA and the landlord to mitigate the costs, the SEC has paid more than

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[6] Id. at p. 90.
[7] Id.
[8] Id. at p. 91.
[9] *Improper Actions Relating to the Leasing of Office Space, Report of Investigation*, Office of the Inspector General, U.S. Securities and Exchange Commission, May 16, 2011 (OIG-553), p. 19 (quoting House Conf. Report 101-924).
[10] These include Atlanta, Boston, Chicago, Denver, Fort Worth, Los Angeles, New York, Philadelphia, Salt Lake, San Francisco, and Alexandria (VA).

$15 million since 2005 for space that SEC has not occupied since that time.[11]

- In 2001, the SEC entered into a lease for new headquarters in D.C., known as Station Place One and subsequently exercised an option to lease Station Place Two. In 2005, SEC disclosed to the House Appropriations Committee that it had approximately $48 million of unbudgeted costs associated with the construction of the new facilities in D.C. and improvements in new leased facilities in New York and Boston.[12]

- In 2007, the SEC embarked on a "restacking" project at its D.C. headquarters building. Restacking is the movement of employees from one physical location in the building to another for purposes of better collaboration between employees. While the then-Chairman of the SEC requested that the Executive Director conduct a cost-benefit analysis prior to restacking or moving approximately 1,700 employees and initiating reconstruction, there is no evidence that a cost analysis was ever completed. The restacking cost the taxpayers $3 million and there is no evidence the restacking improved efficiency. [13]

- In 2009, the SEC's lease for the San Francisco Regional Office was expiring and despite taking steps to exercise a one-year extension while it conducted a full and open competition for replacement space, the extension was never executed and the SEC began paying a higher holdover lease rate. Subsequently, the SEC awarded the new lease to the existing landlord which allowed the SEC to negotiate a credit for the higher rate paid. However, SEC still paid excess rent totaling over $200,000.[14]

Witnesses

In addition to the witnesses listed, the Subcommittee also sent invitations to certain current and former SEC staff involved in the leasing of Constitution Center requesting they provide testimony. The witnesses have either refused to testify or, as of this memorandum, failed to respond to the Subcommittee request.

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[11] *See Real Property Leasing Procurement Process*, Office of Audits, Office of the Inspector General, U.S. Securities and Exchange Commission, September 30, 2010 (Report No. 484).
[12] *See U.S. Securities and Exchange Commission: Building Project Management and Related Budget Planning*, U.S. Government Accountability Office Letter to The Honorable Frank R. Wolf, Chairman, Subcommittee on Science, the Departments of State, Justice, and Commerce, and Related Agencies, Committee on Appropriations, U.S. House of Representatives, October 20, 2005 (GAO-06-61R).
[13] *See Review of the Commission's Restacking Project*, Office of Audits, Office of the Inspector General, U.S. Securities and Exchange Commission, March 31, 2009 (Report No. 461).
[14] *See Real Property Leasing Procurement Process*, Office of Audits, Office of the Inspector General, U.S. Securities and Exchange Commission, September 30, 2010 (Report No. 484).

WITNESSES

The Honorable H. David Kotz
Inspector General
U.S. Securities and Exchange Commission

Mr. Jeff Heslop
Chief Operating Officer/Executive Director
U.S. Securities and Exchange Commission
Accompanied by:
Mr. Mark D. Cahn
General Counsel
U.S. Securities and Exchange Commission

Ms. Elaine Clancy
Director of Leasing, National Capital Region
U.S. General Services Administration

ATTACHMENT

Timeline of Constitution Center Lease

June 2009	SEC decides to not exercise option to lease Station Place 3 (contiguous to its existing headquarters) due to uncertainty of budget. Station Place owner warns SEC it will lease to other potential tenants.
July 2009	SEC staff realizes need for space, General Counsel contacts owner regarding costs of buying out leases to other tenants.
August 2009	SEC decides to lease 200,000 square feet left in Station Place 3.
March 2010	SEC executes lease for 200,000 square feet of space at Station Place 3.
April/May 2010	SEC decides not to buy out the tenants in the remaining 200,000 square feet of space in Station Place 3.
May 7-10, 2010	SEC Office of Administrative Services (OAS) told of the 800 new employees expected but not to expect all to locate in D.C. (371 would be assigned to regional offices)
May 14, 2010	SEC submits authorization request to Senate authorizing committee for $1.5 billion in FY2012 for 800 positions.
May 27, 2010	OAS alerts staff there is an urgent need for new space in D.C. for 400 staff (~ 250,000 sq.ft.) and reaches out to 3 potential properties near Station Place headquarters.
June 2, 2010	OAS receives email from a real estate broker regarding Constitution Center.
June 11, 2010	OAS decides to solicit offers for space for 316,000 sq. ft. and expand the delineated area to include Constitution Center.
June 17, 2010	OAS and the Executive Director meet with the Chairman of the SEC and inform her of the need for 280,000 to 315,000 sq. ft. Chairman prefers locations closer to Station Place and questions if SEC needs that much space given much of the growth would be in the regional offices.
July 7-14, 2010	OAS's employee growth numbers in D.C. expanded.
July 20, 2010	New projections requiring over 900,000 square feet presented to Executive Director.
July 23, 2010	Executive Director recommends to SEC Chairman leasing 900,000 square feet at Constitution Center. Chairman approves after 10 minute meeting and after being told of urgent need to act.
July 28, 2010	SEC signs Letter Contract with Landlord for lease of 900,000 square feet at Constitution Center.
August 2, 2010	Three of four signatures needed to complete the

	justification for a sole source lease obtained before a final draft of justification completed.
August 27, 2010	Deadline for publically noticing justification under federal regulations.
August 31, 2010	Fourth signature needed for justification provided but backdated to August 27.
September 1, 2010	Significant revisions of justification sent to General Counsel.
September 2, 2010	Justification finalized.
September 3, 2010	Justification publically noticed with the date of the fourth signature altered.
September 7, 2010	OAS inquires of General Counsel regarding notifying OMB.
October 5, 2010	Draft lease action summary to OMB completed but never sent to OMB.
October 6, 2010	OAS meets with Chairman to inform her the budget will be flat and the SEC needs to find other federal agencies to assume 600,000 square feet of the space leased at Constitution Center.
November 11, 2010	Landlord begins negotiations with FHFA and OCC to lease space at Constitution Center.
November 19, 2010	Landlord sends email to SEC asking if SEC is prepared to reimburse the landlord's broker's fees and build out costs.
December 8, 2010	SEC informs Landlord that it agrees to a conditional release of space to be leased to FHFA and OCC but that the SEC would retain 300,000 square feet on floors 2-10 in the SW quadrant of the building.
January 2011	OCC and FHFA lease space at Constitution Center, leaving 350,000 square feet of the leased SEC space.
March 2011	SEC informs landlord it hopes to sublease some or all of the remaining space.

THE SECURITIES AND EXCHANGE COMMISSION'S $500 MILLION FLEECING OF AMERICA

THURSDAY, JUNE 16, 2011

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON ECONOMIC DEVELOPMENT, PUBLIC BUILDINGS, AND EMERGENCY MANAGEMENT,
COMMITTEE ON TRANSPORTATION AND INFRASTRUCTURE,
Washington, DC.

The subcommittee met, pursuant to notice, at 10:10 a.m. in room 2167, Rayburn House Office Building, Hon. Jeff Denham (chairman of the subcommittee) presiding.

Mr. DENHAM. The subcommittee will come to order. First, let me welcome our witnesses and thank them for testifying today.

After reading the inspector general's report, it is hard to comprehend how easily the SEC can just commit to spending $500 million of the American people's money in just a few days. It is as though the SEC did not get the memo that Congress and the administration have both been talking about cutting the waste in our Federal buildings. But it seems the SEC thought it was business as usual, and operated with a Congress-is-throwing-money-at-us mentality, in total disregard that it is not their money, but the American people's money.

Our subcommittee has been working to cut waste in Federal buildings. Billions of taxpayer dollars are wasted in underused property, the overbuilding of Federal facilities, and in our over-reliance on costly leases to meet long-term space needs. Unfortunately, examples of waste abound in our management of Federal real property. But the SEC's massive half-a-billion-dollar lease for space it did not need goes far beyond mismanagement. There must be accountability and consequences for this type of cavalier spending of taxpayer money.

As outlined in the inspector general's report issued last month on July 28, 2010, the Securities and Exchange Commission signed a letter contract to lease space at Constitution Center in Washington, DC. The agreement was more than 900,000 square feet of space, with an option to lease an additional 500,000 square feet.

Let's put this in perspective. This is a total of 1.4 million square feet of space for an agency that has just over 3,000 personnel working in the national capital region. The 1.4 million would be on top of the 1.3 million square feet the SEC leases for its headquarters at station—near Union Station. Just to give you an example, 3,000 employees, by GSA's standards, we would have enough room be-

tween these 2 facilities for 12,000 employees. That is by GSA standards.

Constitution Center is the former location of the DOT headquarters, and was completely renovated and upgraded by the owner. And we will start the slides now.

[Slide.]

Mr. DENHAM. This first slide is the interior courtyard of the building. Next slide.

[Slide.]

Mr. DENHAM. Here is an image of one of the lobby areas overlooking the courtyard. Next slide.

[Slide.]

Mr. DENHAM. This slide is taken from one of the top floors facing northwest, towards the Capitol building. Next slide.

[Slide.]

Mr. DENHAM. Another view looking north.

[Slide.]

Mr. DENHAM. And finally, a view looking southwest towards the water and the airport.

[Slide.]

Mr. DENHAM. This last view is from the quadrant of the remaining 300,000 square feet of space SEC insisted the building owner reserve for them.

The total cost of this lease is over $550 million over 10 years. The findings of the inspector general are breathtaking. The SEC bound the taxpayer to more than a half-a-billion dollars based on the back-of-the-envelope calculations that were inflated, and just simply wrong.

There was no formal written approval process. In fact, the final decision was made orally, after only a 10-minute meeting with the chairman of the SEC. There was no OMB approval and no ional approval. And, on top of that, SEC proceeded with a sole source contract negotiated over the course of just days.

The justification for this, as required by law, was completed after the fact, and three of the four signatures were signed before the document was even completed. One of the signatures was backdated. And then the date was later altered, giving the impression that justification for the sole source procurement was completed more than a month before it actually was.

And there is a serious question as to whether the Antideficiency Act was violated. It appears someone at the SEC saw Constitution Center and decided that's where they wanted the SEC to move, and then everything else had to fit: the staffing figures, space needs, and justification.

But today, in addition to the investigation, what led to this lease agreement, we are also examining whether the SEC should keep its independent leasing authority. And we know that this is not the first time SEC has mismanaged its leasing authority. Next slide.

[Slide.]

Mr. DENHAM. Here we have a slide showing a timeline of just some of the instances of mismanagement by the SEC, and the cost to the taxpayer. What this shows is a number of troubling trends.

The SEC has a history of sole-source leases that even GSA, in its management of over 180 million square feet of leased space,

rarely uses. SEC has a history of bad leasing decisions that cost the taxpayer millions: double rent payments in New York, unbudgeted cost in SEC's headquarters, and holdover fees in San Francisco.

In addition to these, we know the SEC is now paying nearly $20 more per square foot for its more recent Station Place headquarters lease than comparable Federal leases near it. And SEC has paid $200,000 a year of taxpayer dollars for off-duty officers to provide security at a Virginia facility already secured by the Federal agency in the building, the Commerce Department.

It is bad decision after bad decision, and it is the taxpayer that loses. The SEC must realize that it is real money they have spent, and that it is accountable to the American people who expect all of us to be good stewards of Federal resources.

At some point the waste has to end. There are very serious issues raised in the IG report. And the more our subcommittee investigates, more questions are raised.

I would like to state for the record that we formally requested the presence of certain current and former employees of the SEC, including associate executive director Sharon Sheehan, and former executive director Diego Ruiz. And they either refused to testify, or failed to respond to our request.

I will be listening closely to the responses of the witnesses today. And based on the responses we get, I will be talking further with Ranking Member Norton, the IG, and the GAO, to determine the appropriate next steps in our investigation.

I would now like to recognize Ranking Member Norton from the District of Columbia for 5 minutes to make any opening statements she may have.

Ms. NORTON. Thank you. Thank you very much, Mr. Chairman. And thank you for calling today's hearing. I certainly want to welcome today's witnesses to the hearing on the inspector general's May 16, 2011, report on the SEC leasing deal for the Constitution Center building located here in southeast Washington.

The shocking findings by the IG on a leasing agreement for more than half-a-billion dollars painted an outrageous picture of an agency that was incompetent to engage in real estate transactions, and consequently developed a culture that allowed bureaucrats to make major unsupported financial commitments on behalf of the agency using outright deceit, and possibly fraud.

The IG findings are so serious that they point towards possible criminal violations by Federal employees in the course of official activities, leading to the execution of the leasing agreement. According to the IG, several SEC employees worked in concert to repeatedly subvert the direction provided by the SEC chairwoman on the placement of new employees, made false representations, and doctored documents to justify a sole-source leasing agreement.

SEC employees relied on the self-delusion that Congress would appropriate all the authorized funds under Dodd-Frank, the new regulatory reform legislation, although the notion that SEC would obtain an appropriation for a full authorization for new employees was historically inconsistent with SEC's budget, and flies in the face of the simple fact and widespread knowledge that authorization of funding never has ensured full appropriation of those funds.

More importantly, the notion that all the new employees would be housed at the SEC headquarters was found to be completely unsupported, and at odds with the express direction by the SEC chair to the staff that most of the growth should be concentrated in regional offices.

The abuse did not end there. Contrary to the General Services Administration standard of 230 square feet per person in an office, the SEC Office of Administrative Services, or OAS, provided an estimated need for 400 square feet per person, nearly double the GSA standard. This overly generous standard was later inflated by a factor of 49 percent for auxiliary staff, even though the 400 square feet per person actually was meant to accommodate the auxiliary staff.

The IG concluded that this inflation by the SEC OAS "employed a series of unfounded egregiously flawed and irresponsible projections to derive the purported need to lease 900,000 square feet."

Even if the SEC had received all the authorized funds provided by Dodd-Frank, the SEC would have needed, at most, an additional 300,000 square feet, only a third of the 900,000 the Agency eventually leased. Why, then, did the SEC lease 900,000 square feet? The answer provided by the IG is that a few SEC OAS officials had what he called grandiose plans to lease the upscale Constitution Center. Having set the target square footage, they worked backwards, using a "deeply flawed and unsound analysis" to justify the lease, according to the IG.

To compound the damage, the $556 million lease agreement was conducted as the Government never does, as a sole-source contract that was completed in over 3 days, just over 3 days. Only after the contract was signed was a justification and approval for other than full and open competition prepared. And, according to the IG, it was inadequate, not properly reviewed, and back-dated, and prepared well past the deadline—regulatory deadline for such contracts.

The IG also has raised the serious question that this leasing agreement may have violated the Antideficiency Act, which prohibits officers or employees of the Government from committing the Government to a payment of money before an appropriation is made, authorized by law.

Astonishingly, this transaction represents a pattern, since the SEC was granted leasing authority in 1990. The Agency has made repeated missteps from the build-to-suit lease for the SEC headquarters behind Union Station that led to $48 million in construction overages, and the mishandling of lease transactions in San Francisco and New York, forming a leasing division only 19 years after receiving leasing authority.

The SEC was granted its own leasing authority, with the expectation that the authority would be "exercised vigorously by the Commission to achieve cost savings and to increase the Commission's productivity and efficiency." Sadly, the opposite has been the case, and calls into serious question the grant of leasing authority to the SEC or to any Federal agency.

This subcommittee has an obligation to taxpayers to understand the steps that led to the Constitution Center lease, to take corrective measures to ensure the SEC can no longer engage in leasing

activities, and to ensure that appropriate action regarding the employees involved is taken.

Notably, several employees implicated in this leasing transaction have refused the invitation of this subcommittee to testify. And at least one of the principal players named in the IG report still has oversight of the SEC leasing program.

The SEC leadership is on notice that if there is retaliation against the employees that provided testimony to the SEC IG, we will respond immediately. I appreciate the testimony that has been prepared. I look forward to hearing from today's witnesses.

Mr. Chairman, I have served on this subcommittee for 20 years. I have seen mishaps by agencies of various kinds, some of them deliberate. I doubt that I or any other Member of Congress has ever seen an abuse approaching this, that was as determinedly done by the employees involved. I have, therefore, drafted a bill to revoke SEC's leasing authority. I recognize that the BRAC bill which you and I are working on now will, in fact, revoke the authority of agencies outside of the GSA to engage in such leasing, agencies that may have expertise in the mission assigned to them by Congress, but certainly not in a very complicated different area of enterprise, and that is real estate areas.

I believe that taxpayers would not be content if we said, "Don't worry, we will get to this when the BRAC bill is done." That takes two Houses, it takes going to the floor. I believe an immediate response by this committee is necessary, particularly since it has always been doubtful that agencies outside the GSA should have such authority.

So, I will be asking you, Mr. Chairman, to look at the bill I have drafted, and hope that you will cosponsor that bill with me. And perhaps we can get that bill to the floor before this calendar year is over.

Mr. DENHAM. Thank you. I look forward to that. This abuse is not going to be tolerated, and we will look forward to seeing that, and working with you on the issue.

Today we are going to ask the witnesses to provide testimony under oath. I would ask each of the witnesses to please stand and raise their right hand to be sworn in under oath.

Do you swear that the testimony you are about to provide to the subcommittee is the truth, the whole truth, and nothing but the truth, so help you, God?

WITNESSES. I do.

Mr. DENHAM. You may be seated. Our first and only panel will be the Honorable David Kotz, inspector general, U.S. Securities and Exchange Commission; Mr. Jeff Heslop, chief operating officer and executive director, U.S. Securities and Exchange Commission—and Mr. Heslop is accompanied by Mr. Mark Cahn, SEC general counsel; and Ms. Elaine Clancy, director of leasing, national capital region, U.S. General Services Administration.

I ask unanimous consent that our witnesses' full statements be included in the record.

[No response.]

Mr. DENHAM. Without objection, so ordered. Since your testimony has been made part of the record, the subcommittee would request that you limit your oral testimony to 5 minutes.

Mr. Kotz, you may proceed.

TESTIMONY OF THE HONORABLE H. DAVID KOTZ, INSPECTOR GENERAL, U.S. SECURITIES AND EXCHANGE COMMISSION; JEFFERY HESLOP, CHIEF OPERATING OFFICER AND ACTING EXECUTIVE DIRECTOR, U.S. SECURITIES AND EXCHANGE COMMISSION; MARK D. CAHN, GENERAL COUNSEL, U.S. SECURITIES AND EXCHANGE COMMISSION; AND ELAINE CLANCY, DIRECTOR OF LEASING, NATIONAL CAPITAL REGION, U.S. GENERAL SERVICES ADMINISTRATION

Mr. KOTZ. Thank you. Thank you for the opportunity to testify before this subcommittee. 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.

On November 16, 2010, we opened an investigation as a result of receiving numerous written complaints concerning the SEC's decisions and actions related to the leasing of office space at Constitution Center.

As part of our investigative efforts, we obtained and searched over 1.5 million emails, for a total of 27 current and former SEC employees for various time periods pertinent to the investigation. We carefully reviewed and analyzed thousands of pages of documents, and interviewed or took the testimony of 29 witnesses with knowledge of facts or circumstances surrounding the SEC's activities.

On May 16, 2011, we issued a comprehensive report of our investigation containing over 90 pages of analysis, and over 150 exhibits. Our investigation concluded 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 represented another in a long history of missteps and misguided leasing decisions made by the SEC since it was granted independent leasing authority by Congress in 1990.

We found that, based on estimates of increased funding, primarily to meet the requirements of Dodd-Frank, between June and July of 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. We found that OAS grossly over-estimated the amount of space needed for the SEC's projected expansion by more than 300 percent, and used these groundless and unsupportable figures to justify the SEC committing to an expenditure of over $556 million over 10 years.

We found that OAS used the standard of 400 square feet per person to calculate how much space would be needed for the additional positions it believed it was gaining. The 400-square-foot standard was described by one of the people working on the lease as a back-of-the-envelope calculation.

The standard was an all-inclusive number that included common space and amenities, an additional 10 percent for contractors, 10 percent for interns and temporary staff, and 5 percent for future growth. Notwithstanding this all-inclusive number, when OAS later did its calculations to justify the Constitution Center lease, it added even more unnecessary space by double-counting for contrac-

tors, interns, and temporary staff. We also found that each one of these estimates was wildly inflated, and unsupported by the data OAS was using.

After the SEC committed itself to the 10-year lease term at a cost of over $556 million, it entered into a justification and approval for other than full and open competition, which is required by the Federal Acquisition Regulation, FAR, when an agency decides not to allow for full and open competition on a procurement or lease. The FAR permits other than full and open competition when the agency's need is of such an unusual and compelling urgency that the Government would be seriously injured unless the agency is permitted to limit the number of sources from which it solicits bids.

The IG investigation found that the justification and approval to lease space at Constitution Center without competition was inadequate, not properly reviewed, and back-dated. The OAS analyst who signed the justification and approval as the SEC's competition advocate acknowledged in testimony that the SEC would not, in fact, be seriously injured if it lost the opportunity to rent this space. She admitted that she took no substantive steps to verify that the information in the justification and approval was accurate, and that when she signed the document she was not aware that the funding had not been appropriated, and she did not have an understanding of when the projected personnel were expected to be hired.

The FAR also requires that the justification and approval be publicly posted within 30 days after contract award. As the letter contract for Constitution Center was signed on July 28th, the deadline for publication of the justification of approval was August 27. On September 3rd, the SEC publicly posted the justification and approval, which was signed by 4 individuals as dated August 2nd.

Our investigation found, however, that the justification and approval was not finalized until September 2nd, and that substantial revisions were being made up to that date. We found that three of the four signatories executed the signature page on August 2nd, before a draft even remotely close to the final version existed. We found that the SEC's competition advocate executed the signature page on August 31st, initially back-dated her signature to August 27th, and then subsequently whited out the "7" to make it appear that she signed the document on August 2nd.

The actions of the signatory to the justification and approval gave the public the false impression that the document was finalized a few days after the letter contract was signed, and that there was only a minor delay in its publication.

Based on these findings, we issued a report recommending that a thorough and comprehensive review and assessment of all matters currently under OAS's purview be conducted, and that the SEC determine the appropriate disciplinary and/or performance-based actions to be taken for the matters discussed in the investigation.

Thank you, and I am happy to answer any questions.

Mr. DENHAM. Thank you, Mr. Kotz.

Mr. Heslop, you may proceed.

Mr. HESLOP. My name is Jeff Heslop, chief operating officer and acting executive director of the U.S. Securities and Exchange Commission. I appreciate the opportunity to testify on behalf of the Commission with respect to the Agency's lease of office space at Constitution Center, and to share with you information on the actions the SEC is taking in response to the IG report.

The IG report on the leasing of Constitution Center revealed a number of flaws in the SEC's leasing process. Although the SEC has not paid any rent, and is no longer obligated for the majority of the space, it is clear that this leasing decision lacked the rigor and attention to detail demanded for decisions of this magnitude. As such, we are committed to implementing whatever changes are needed to improve the process, starting with the retention of outside experts to conduct an assessment, a comprehensive assessment, of our entire leasing organization.

On July 28th of 2010, the SEC entered into an agreement to lease approximately 900,000 rentable square feet of office space at Constitution Center to house new staff necessitated by the Dodd-Frank Act and to address the facilities needs created by expiring leases in Alexandria, Virginia, at our back office operations center. The SEC's agreement contained a 10-year term, and envisioned space being delivered to the SEC in phases.

In the fall of 2010, when it became apparent that the SEC would be limited by the continuing resolution and would not be receiving further funding for fiscal year 2011 to hire additional staff for the new responsibilities it received under regulatory reform, and in light of significant uncertainty regarding the Agency's budget for fiscal year 2012, the Agency's leasing branch worked with the Constitution Center landlord to identify two non-appropriated financial regulatory agencies—the Office of the Comptroller of Currency and the Federal Housing Finance Agency—that were able to take the majority of the space allocated to the SEC, a total of approximately 558,000 square feet. The SEC's releases that enabled the landlord to lease space to other Federal tenants were conditioned upon the SEC being released from all obligations for the space.

With respect to the remaining space, the SEC earlier this year determined that the uncertainty of the Agency's budget for fiscal year 2012 and beyond counsels against retaining it. To this end, SEC staff is currently working with the General Services Administration to identify other Federal Government agencies to fill the remaining space.

The inspector general has identified a number of flaws with the leasing process. My charge from the commissioner—from the chairman is to address the issues identified in the IG report, and improve that process.

The SEC is actively at work, implementing the inspector general's recommendations, and taking steps to strengthen our real property leasing program. For example, the authority previously exercised by the executive director has been transferred to me, as the chief operating officer. All future property leasing decisions must be approved by me, as the COO, before any leases are signed.

Second, as I mentioned, we're conducting a comprehensive, independent assessment of our leasing operations with outside experts.

Third, all future leasing obligations will require consultation with an executive senior-level facilities management committee before they can be incurred or recommended for approval. This cross-organizational committee will provide oversight and guidance to the SEC leasing process, and will serve as a forum for the executive-level discussion of the Agency's leasing decisions.

Fourth, we're in the process of developing a more clearly defined leasing policy and associated process.

And, fifth, we have initiated efforts to acquire technology that will permit us to automate, and will provide more efficient space planning, move management, and asset management. Such systems, available on an off-the-shelf basis, and commonly used in private industry as a best practice, should provide managers with significantly more timely and accurate analysis and planning to deliver these efficient space utilization at our office locations.

In addition, the IG report recommends that the Agency consider whether disciplinary action should be taken against current staff members. The SEC has begun this review, in accordance with Federal personnel law. At present, the Office of Human Resources and the Office of General Counsel are analyzing the investigative record, and will recommend appropriate disciplinary action to me. I would then decide any appropriate disciplinary action that should be taken.

In conclusion, the SEC is actively at work on a number of fronts to strengthen the Agency's real property leasing program. Although the SEC has paid no rent on the space, and has worked with the landlord to identify substitute tenants, the OIG report identified flaws in the leasing process in need of correction. We are endeavoring to take all necessary and appropriate steps, including implementing new controls and procedures to ensure that we address the significant issues identified in the IG's report.

I would be happy to answer any questions at this time.

Mr. DENHAM. Thank you, Mr. Heslop.

Ms. Clancy, you may proceed.

Ms. CLANCY. Good morning, Chairman Denham, Ranking Member Norton, and members of the committee. I appreciate the opportunity to be here today, and be invited to discuss the GSA's approach to acquiring lease space for Federal agencies.

The GSA searches for effective ways to provide space for Federal agencies, to help them achieve their missions while protecting the public's interest. In order to accomplish these goals, the GSA implements a deliberate and comprehensive process that ensures adequate competition, and considers other public interest. We manage an inventory of over 370 million square feet of space, approximately half of which is leased space.

The GSA effectively manages our leased space, which currently has a vacancy rate of less than 1 percent. Leases under the current prospectus threshold represent approximately 98 percent of all of our leases. Prospectus-level leases represent 2 percent of our leases transacted, and 33 percent of the annual GSA rent pays—that the GSA pays to lessors.

The requirements development evaluation process of these leases is more extensive, due to the size and the cost. These large leases require review and clearance by GSA's central office and OMB

prior to submission to Congress. OMB ensures that proposed leases comply with lease scoring rules, and ensures that the proposed action is consistent with personnel and resource estimated in the President's budget.

Once the GSA has worked with an agency to carefully define their requirements, and assess that their needs are based on accurate projections and available funds, GSA's lease acquisitions process runs through a carefully sequenced set of steps to ensure adequate competition and a fair rental rate for taxpayers.

One of GSA's fundamental strategies is to promote competition by attempting to maximize the number of potential qualified offerors for a lease solicitation. By improving communication with the commercial real estate sector, GSA's presence in the market is strengthened, and a sense of partnership with leasing industry practitioners emerges, resulting in increased competition for GSA leases.

GSA follows a sequenced and efficient leasing acquisition process, which includes market advertising, surveying assessments, evaluation, negotiations, and contract execution, which are outlined in detail in my written statement. GSA constantly looks for ways to streamline, standardize, and simplify our leasing process, to minimize the cost associated with acquiring a lease.

We also constantly assess our performance against other rental rates in the market. GSA is committed to adapting its internal processes to mirror leasing in the private sector, and to fully utilize the market leverage that results from the Federal Government being a reliable and desirable tenant.

In regards to the SEC—the lease procured by the SEC at Constitution Center in Washington, DC, the SEC has recently reached out to the GSA to request our assistance in filling the remaining vacant space. The GSA is gathering additional details pertaining to this contract, and the conditions under which the SEC procured the lease. To the extent that we can reasonably assist in protecting the public's interest and meeting the space needs of other agencies, we will consider doing so.

In conclusion, the GSA's approach to leasing Federal space allows agencies to achieve their mission effectively, and protect the public's interest in ensuring that space is acquired at a fair rate, while being flexible to ensure that the highest levels of controls are placed on the largest potential leasing actions.

In addition, we aim to constantly improve our processes, to attract further competition from the private sector, and to minimize cost to the taxpayers.

Thank you for inviting me to appear before you today, and I appreciate the opportunity to discuss the GSA's leasing practices and expertise. I welcome your questions.

Mr. DENHAM. Thank you, Ms. Clancy. We will now start our first round of questioning. We expect that there will be several rounds today, because I don't think there is any shortage of questions that need to be answered here.

First, Mr. Heslop, can you state for the record your position and responsibilities at the SEC?

Mr. HESLOP. I am the chief operating officer and acting executive director of the SEC. My responsibilities include oversight of our IT

operation, our human resources operation, the Office of Administrative Services, FOIA, and records management, and Office of Financial Management.

Mr. DENHAM. Leasing authority under one of those?

Mr. HESLOP. Yes, the Office of Administrative Services.

Mr. DENHAM. And does the SEC intend to issue a formal response to the IG report issued in May?

Mr. HESLOP. We are taking appropriate action against the IG's report that was issued. We are, as I stated, having a comprehensive independent outside assessment done of the OAS organization, and looking at every recommendation in the IG's report, and taking appropriate action against them.

Mr. DENHAM. So are you going to be issuing a formal response to the IG report?

Mr. HESLOP. At this time there is no intent to issue a formal response.

Mr. DENHAM. Why? Why wouldn't you respond to them formally?

Mr. HESLOP. There is no requirement to respond to them formally.

Mr. CAHN. If I could, Chairman Denham, if I could?

Mr. DENHAM. Sure, Mr. Cahn.

Mr. CAHN. Mark Cahn, I am the general counsel at the SEC. Typically, when the inspector general issues investigative reports such as this, the agency reviews the report and responds, as Mr. Heslop describes, to take responsive action——

Mr. DENHAM. Will you pull your microphone closer, please?

Mr. CAHN. Oh, I'm sorry—to take responsive action in response to the report. It is not the practice of the Agency, in response to investigative reports such as these, to issue any sort of formal response. That is as distinguished from audits that the inspector general prepares, in which the practice is to have a management response to the audit. But I suppose the inspector general could speak more directly to that.

Mr. DENHAM. What is customary, Mr. Kotz?

Mr. KOTZ. Yes, I mean we don't generally have a formal response to our investigative reports. What we do expect is that the recommendations in our report be implemented, that a process be put in place, and that our disciplinary action recommendations be implemented, as well.

So, I mean, I am not sure we need a formal response. What we need them to do is fix the problems in the Office of Administrative Services, and discipline the people who we found to have violated the rules.

Mr. DENHAM. I will look at it from a business perspective. When a Government agency comes down on a business, they are not only expected to have the recommendations implemented, but to have a quick, rapid response on the timeline on when you are going to get these things done.

So, I would expect to see some type of response, you know. I want to know. Is it going to take you a year to fix this? Ten years? I want to know what the response is to the American taxpayers. So I am looking for how long—what you are going to do to correct the action, how long it is going to take. And I would think a simple response to the IG's report would at least be a good starting point.

Mr. Heslop, one of the critical steps in space planning and determining how much new space is needed is developing a program of requirements. Was there a program of requirements developed prior to July 28, 2010?

Mr. HESLOP. To my knowledge, I don't know. I have recently inherited this function. Again, my role is to try to fix the process, a very flawed process that led us to this situation. We are in the process of doing it, taking a number of steps that I outlined in my testimony. So I can't address the question about the history.

Mr. DENHAM. And how long has it been since you have assumed these new—this new role?

Mr. HESLOP. Approximately 7 weeks.

Mr. DENHAM. Mr. Cahn, same question.

Mr. CAHN. I am not—I don't know whether a program of requirements was prepared. The inspector general reviewed the documentation in connection with this particular leasing activity. So he may be aware of whether that sort of documentation was prepared. I just don't know.

Mr. DENHAM. You guys were both aware you were going to testify in front of Congress today, correct?

Mr. CAHN. Yes, sir.

Mr. DENHAM. This seems like a pretty basic question. I mean this is standard procedure, is it not?

Mr. CAHN. I assume it is. I just don't—I was not involved in the transaction. I assumed the position of general counsel in March of this year. That is not to say that the general counsel position would have been involved in that level of detail of documentation of a leasing decision; I just don't know what documentation was prepared by the Office of Administrative Services, but we will be happy to look into that inquiry and get back to you.

Mr. DENHAM. Chief operating officer, is this not part of standard operating procedure?

Mr. HESLOP. Again, I am new to the position, I am reviewing the current process, and trying to improve and fix that process, going forward. So I can't speak to past operating practices, other than to tell you, as you have seen, they were deeply flawed, and we are doing our best to turn them around.

Mr. DENHAM. Ms. Clancy, the GSA's—when GSA goes out and does a lease—program of requirements?

Ms. CLANCY. Yes. For a lease of this size, we would work with an agency initially to develop that program of requirements, specifically looking at their existing space use, the use of their existing space, how we might house that agency efficiently, given the current Presidential directives, and then directives from OMB to reduce their space requirements, overall.

And as we were developing that requirement, we would then—we have a number of checks and balances that we use, because we work with those agencies at the NCR level. Then it goes, again, as I said before, to our central office, and then to OMB. Once it reaches OMB, it is not just the GSA's examiners who are looking at the space requirements, but it is also the agency's examiners who would be looking at those requirements in conjunction with ours, to confirm that those requirements are, in fact, what the agency actually needs.

Mr. DENHAM. Standard operating procedure. GSA goes out for a very large-size lease, you put together a program of requirements. You know what you are going out there to lease, for how many employees, how big of a space you need, what location you need. I mean there has got to be a program of requirements that you are looking at before you go out and secure space, do you not?

Ms. CLANCY. That is correct. And it is a fairly extensive process that we use.

Mr. DENHAM. Mr. Kotz, just a quick follow-up. Standard operating procedure between different agencies, program of requirements?

Mr. KOTZ. Yes, I do believe it is a standard operating procedure, and I don't believe it was done in this case.

Mr. DENHAM. Thank you. And more of a statement than a question, because I am out of time and will come back to this. But you have been the chief operating officer prior to assuming the new duties, have you not?

Mr. HESLOP. That is correct, for about half of the duties I outlined when you asked me the original question. I did not have oversight of the Office of Administrative Services, which is where this leasing branch resides.

Mr. DENHAM. But as chief operating officer—I am a new guy here, but I can understanding a program of requirements in—both from a business perspective, as well as from GSA and the IG. You've been COO—I mean that seems pretty basic, that you would at least know that a program of requirements is something that every agency, every business, would be going out to get some specific requirements on.

Ranking Member Norton?

Ms. NORTON. Thank you, Mr. Chairman. The chairman asked about your response to the IG report. I can understand that it is an interesting response, very much along protocol lines, even though the actions of the Agency have tended to ignore rules, as well as protocol.

So, let me take his question even further. Have you taken—Mr. Heslop and Mr. Cahn, have you taken any action of the kind recommended by the IG, such as disciplining employees, such as issuing—getting—asking for a formal opinion from the GAO about whether there has been a violation of the Antideficiency Act?

Mr. CAHN. I can start, Congresswoman Norton. As to the last matter, the—with regard to the Antideficiency Act, yes, we have. We have recently sent over a formal request for an opinion from the comptroller general on the question of whether the manner in which we obligate funds in connection with our multiyear leases is consistent with the Antideficiency Act. So that letter has gone over.

And I know that Mr. Heslop can speak to the other recommendations in the inspector general's report.

Ms. NORTON. Thank you, Mr. Cahn. That is minimally necessary, to know whether there has been—of course, Mr.—the IG indicated that there may have been, he is not an expert on that. You need to know that. The appropriators will need to know that very, very much, especially in light of your new responsibilities.

And I must say it grieves me that this Agency has had to deal with a real estate problem outside of its mission, and now faces an

aura of abuse, right at the time when we are expecting the Agency to zero in on what it is Dodd-Frank asked you to do. Talking about a distraction, they are distractions. And they are distractions that an agency cannot afford.

What about the other recommendations, Mr. Heslop?

Mr. HESLOP. With regard to disciplinary action, we are aggressively managing it. Federal personnel law affords the named individuals due process, and we are letting that process play itself out.

Ms. NORTON. So what processes have been instituted, as to these employees?

Mr. HESLOP. Again, our general counsel and our Office of Human Resources are reviewing the investigative record. Upon completion of that review, they will provide me with recommendations for disciplinary action. I am the deciding official. I will take—I will make those decisions at that time——

Ms. NORTON. So, Mr. Cahn, you have not—the Agency has taken no action against the employees who were involved in this matter.

Mr. CAHN. The Agency has commenced the review, the disciplinary process review, which——

Ms. NORTON. When will that review be over?

Mr. CAHN. I can't predict precisely when that will be over. I imagine it can be completed quickly. The process that is required under the Federal personnel laws requires some degree of time lapse——

Ms. NORTON. Mr. Cahn, you are going to have your head handed to you by the appropriators, given the great amount of process that is involved here, when there was very little process——

Mr. CAHN. We recognize——

Ms. NORTON [continuing]. Very little process involved, with respect to these transactions.

I am the first to want due process. But the notion that no process has even begun, even though the IG had to take—has issued a report, is very troubling.

Let me ask you about an employee that—whose name runs repeatedly through the IG report. The name is Sharon Sheehan. She is named as one of the principal players in signing the Constitution Center deal. Is Sharon Sheehan still on staff?

Mr. HESLOP. Yes, Sharon Sheehan is still on staff.

Ms. NORTON. Does her—do her responsibilities—does she have responsibilities in the SEC's OAS office?

Mr. HESLOP. Yes, she does. She is the director of the OAS office.

Ms. NORTON. Why is she still the director of the office?

Mr. HESLOP. Again, we are following Federal personnel law, and letting that process play out. Once that process has played out——

Ms. NORTON. Say that again.

Mr. HESLOP. We are following Federal personnel law, and letting that process play out.

Ms. NORTON. Is she still doing oversight of the leasing program?

Mr. HESLOP. She is in that capacity. I have retained all——

Ms. NORTON. Mr. Cahn——

Mr. HESLOP [continuing]. Oversight of the leasing program.

Ms. NORTON [continuing]. Don't you think, as an attorney, officer of the court, that you should advise Mr. Heslop that he has, under Federal law and regulations, no obligation to retain a person in the

position where abuses have been charged by the IG? You now are taking it on the Agency, when you maintain her in that position.

What—we are moving people out of positions all the time. I insist upon it, as a matter of due process, that they not be deprived, ultimately, of what they are entitled to. At the same time, the Government requires the Agency to take action to make certain that someone charged with abuse is not sitting there, doing exactly what she was doing when the charges were laid. So you will have to explain to me, as counsel, how this individual cited repeatedly in the IG report is left doing precisely what she was doing before.

And I understand the chairman just said that we asked her that she be made available to come here, and the Agency refused to make her available. So you then have to respond for her, sir, because you, the Agency, have the ability to move this person or not. Why have you chosen not to do so?

Mr. CAHN. Congresswoman Norton, my understanding is that this particular employee is under heightened supervision right now, under the direction of Mr. Heslop.

Ms. NORTON. Why have you chosen not to remove her? Obviously, she has to be under some kind of supervision. But she is a supervisory employee, herself. Why are you spending the time and energy of Agency officials supervising a supervisor? Why do you not remove her? What is the reason for not removing her from the position of supervising leasing activities at the SEC? I need an answer to that question.

Mr. HESLOP. Yes, ma'am. As mentioned in the IG report, the recommendation was to conduct a comprehensive assessment of the report, and post that review, look at disciplinary action. It is very clearly stated.

Ms. NORTON. All right. Let me—I want to make sure I am not violating law and regulations here. Let me ask the IG.

Is there anything that, in your judgement, requires the Agency to keep this employee doing what she was doing at the time your report was issued? Must they do that? Must they do a review before they even move her to another position, paying her in the same salary? Are they required to leave her at the helm, doing exactly what you criticized her for doing?

Mr. KOTZ. Yes, I don't believe they are. Before they go forward with a disciplinary process, you can move an employee into another office, as long as they are getting the same salary, has the same equivalence. That person could be moved to another office, so they are not involved in those duties. There are also other methods that could be used under personnel law, to my understanding.

The disciplinary process, if one were to terminate Ms. Sheehan, which we are recommending in our report, that action be taken up to and including dismissal, that would take more time, and there would have to be a proposal and a decision made on that.

Ms. NORTON. Mr. Chairman, I know my time is up.

You have heard the opinion of the IG. Are you willing to consider removing this employee from presiding over or being involved in leasing activities at the SEC? Yes or no?

Mr. HESLOP. Yes, ma'am. As I mentioned, I am the deciding official on the disciplinary action, and that is one of——

Ms. NORTON. Before disciplinary action is taken, Mr. Heslop, are you willing to remove her tomorrow to another position so she is not sitting there, in oversight of leasing activities still going on at the SEC? Yes or no?

Mr. HESLOP. I will take it under consideration.

Ms. NORTON. Thank you, Mr. Chairman.

Mr. DENHAM. Amazing. We ought to take some other things under consideration.

Mr. Heslop, your testimony suggests that the reason the space at Constitution Center was not needed is because Congress did not provide full funding for the new staff that SEC had anticipated. Putting aside the appropriateness of entering into a lease before funding is secured, the IG report suggests—and I would agree—that the SEC's anticipated staffing levels still would not have justified 900,000 square feet of space, and certainly not a sole-source procurement.

Are you suggesting that the amount of the space procured by the SEC was an appropriate amount of space?

Mr. HESLOP. No, sir, I am not suggesting that at all.

Mr. DENHAM. What do you believe an appropriate amount of space is?

Mr. HESLOP. An appropriate amount of space will be determined once we get the resources for the requirements that Congress has given us to execute our new responsibilities, based upon consideration of regional strategy.

By the way, I should mention that we are undergoing a review of our regional strategy, which may influence our regional footprint, and how many people we put in those regions, as well as a determination in the local capital region of how many employees of the different mixes will require—will need to be housed.

We intend to land on an industry best practice, Government best practice square-footage estimate, and use that in our calculations. We intend to cooperate closely with GSA to obtain their wise counsel and subject matter expertise. It is something we haven't done in the past, it is part of our plan.

Mr. DENHAM. Your plan. So your plan is to develop a program of requirements?

Mr. HESLOP. Our plan—I would expect very surely to develop a program of requirements.

Mr. DENHAM. So we should have had a program of requirements prior to this.

Mr. HESLOP. It is quite apparent that we should have, yes. The previous process was very flawed. And our role is to fix that process going forward, so this does not happen again. That is my role.

Mr. DENHAM. Mr. Kotz, the inflation of the numbers, as detailed in your report—breathtaking. The increase in numbers for contractors, interns, temporary workers, coupled with the 400-square-foot per person standard used is disturbing, at best.

What do you believe the needed space—shot out from under 300,000 square feet, what it originally was, all the way up to 900,000 square feet in just the course of 1 month—was it some big change in Government that we, you know, go through, some new operation nationally that would suggest that all of a sudden we

were going to get a huge number of employees, and we absolutely had to have this space?

Mr. KOTZ. No, I think it was that they looked into Constitution Center and saw how beautiful it was, and what a nice space it was, and so that's what happened in that interim period. And they decided only to focus on Constitution Center, as opposed to all other options. And the Constitution Center was a larger place, and that needed 900,000 square feet.

Mr. DENHAM. So, in your report, do you see any justification to go to a 900,000-square-foot building?

Mr. KOTZ. No, no. The numbers were wildly inflated. There was no basis for it. Even if you assumed, as you indicated, that the SEC was going to get all the money, there still wouldn't have been need for 900,000 square feet, no less an additional 500,000 square feet, as you indicated, which would be 1.4 million. It was completely fabricated. And we believe it was simply to be able to acquire beautiful space with fancy views, like you indicated on that slide show.

Mr. DENHAM. How about the current 1.3 million space that they currently occupy? Is that 100 percent utilized?

Mr. KOTZ. No. And, in fact, during that time there were open offices there. There continue to be some open offices. I think it is mostly utilized, but there still are open offices in Station Place.

Mr. DENHAM. So we've got 1.3 million in current space with availability. Went out to get 300,000 square feet, which inflated to 900,000 square feet, with an option of 500,000 square feet. Can you give me the timeline of that course of decisionmaking?

Mr. KOTZ. Sure. This is all within the period from June 2010 through July 2010. There was the briefing in June 2010, where there was discussion about 280,000 to 315,000 square feet. By July 2010 it turned into 900,000 square feet with the option for the additional 500. So it was 1 month.

Mr. DENHAM. Is that normal?

Mr. KOTZ. No, no. I mean it——

Mr. DENHAM. This is half-a-billion dollars. I mean I would think you would need congressional approval to spend a half-a-billion dollars, or certainly you would go through other agencies.

Probably this would rise to the level of the President, to say, you know, "I realize you are going to cut a lot of different programs this year that are very important to the people of this Nation. We are thinking about going out and getting enough square footage, and spending a half-a-billion dollars. Mr. President, what do you think about that?"

I mean the process of going out and getting this type of leased space, the sign-off?

Mr. KOTZ. Yes. I mean the negotiation was done, essentially, over a weekend. They got the OK to go forward on Friday. By Wednesday they had signed the deal. The process of coming up with the numbers was very, very quick. You know, not scientific, not thorough, you know, no program put forward, you know, no rational basis put forward, no approvals outside the SEC.

Mr. DENHAM. Thank you, Mr. Kotz. My time has expired. Mr. Walz?

Mr. WALZ. Well, thank you, Mr. Chairman and Ranking Member. This entire situation is troubling on many layers. I guess the school

teacher in me—the one good thing about this whole thing is is, Mr. Heslop, you have done what I didn't think was possible. You certainly brought us together in a bipartisan manner for a common cause. Because the frustration here is palatable. I associate myself with both my colleagues' remarks.

I often times sometimes laugh about the names of hearings. This one is serious, and I think it was appropriately named, and that is very frustrating to me, one, as a watchdog of the taxpayers' money, but two, as I think everyone in this room recognizes, is the incredible importance of the SEC, and the job that it does, and the importance now more than maybe any time in the last 75 years is on trial today, if you will, because of a stupid, possibly illegal, decisionmaking.

And I again associate, I think, with the chairman on this one is I can't imagine a private business just getting to decide they will get around to this when they decide, "It is OK, we will fix this," or whatever. That is not going to happen. They are going to have somebody hammering on them. And I am incredibly frustrated by that.

And this whole idea of leasing—and I don't like to pile on, Mr. Heslop, but we, as Members of Congress—I review my leases through GSA, and I follow those rules. We go out and look for space in Rochester, Minnesota, in Mankato, look for the best space, try and get the best dollar for it, negotiate a good deal, and I look it over to make sure it is legal. That is my responsibility, in addition to other responsibilities. So there is a frustration.

But I do think the good news is I am a huge fan of our IG programs, Mr. Kotz, on—and across the board. I spend a lot of time in the VA committee, and the inspector general in the VA returns about 12 to 1 in terms of what we give them for a budget. For every dollar they return 12 back to the taxpayer. Do you happen to know, in your Agency, what that number is, or could we get it?

Mr. KOTZ. Our office's budget?

Mr. WALZ. No, what you get on what we give to you.

Mr. KOTZ. Oh.

Mr. WALZ. I am going to come to that——

Mr. KOTZ. Oh.

Mr. WALZ [continuing]. On what we get, a return on the dollar in terms of stopping fraud, waste, and abuse, both internally and in private contractings. In the VA, that is the number they can come up with.

Mr. KOTZ. Yes, I don't know that we have calculated a specific number. I mean in each one of our semi-annual reports we identify cost savings. Routinely, those are in the millions.

Mr. WALZ. You get to count $500 million on this one. That will up the odds.

Mr. KOTZ. Right, right, yes.

Mr. WALZ. But it—but in all seriousness, I will move to the next question on this.

Yesterday's number from the Financial Services cut the budget for the SEC by 18.7 percent. You are probably going to take your share of the cut in that. My concern on this is all of us want to see good responsibility, I think, at this time in history. And for the importance of responsibility of enforcing new enforcement laws to

make sure we don't get a melt-down, it will be tragic to me if we are not able to give you the resources. Because as those resources go down—how does your office decide how you look at things, how you go after things? Because you are limited, I would assume.

Mr. KOTZ. Right. Well, you know, we get a lot of complaints. And where we get complaints—every complaint that comes in, we look at it in some way or another. We triage the process to determine how much resources we should put to a certain complaint. In this case, we got so many complaints about this leasing decision that it was very clear it would have to be looked at.

And then, many folks from that office, the Office of Administrative Services, came to us—many anonymously—with other concerns about that. So it was very clear that this one had to be looked at. But, you know, we strive to look at whatever we can. We do have a small staff, but we are very efficient, and we do produce a lot of work, because it is important for the taxpayer that there be a watchdog in place.

Mr. WALZ. In this case, would it be fair to say the system did work? We have an agency, we have the IG, the complaints came in, they were taken, they were investigated, you brought it to Congress.

And I will say "worked," because I get a very strong feeling here, Mr. Heslop, this thing will be resolved. I can be pretty certain of that. It will be resolved in a satisfactory manner to the taxpayer and to the system.

But would you think the system worked here, so far, at this point?

Mr. KOTZ. Yes, in that manner, certainly. I mean we identified the issues, we issued a report. We didn't pull any punches in that report. The Agency has accepted the report.

Now, the next stage, obviously, is to fix the problem and to engage in disciplinary action, as appropriate. But I do say, as of now, the system has worked, yes.

Mr. WALZ. Would it be possible—and I don't know if it's you, yourself, Mr. Kotz, or someone in your office—to see if you have that data, on return for the dollar, what you are doing?

I am very concerned, when I make the argument where we do have to cut—and the chairman is right about that, there is tough decisions to be made—as I said, I am a long-time fan of the IG because of what I think it saves and does what it's supposed to do for the taxpayer.

Could I get that information?

Mr. KOTZ. Sure, we would be happy to provide that to you.

Mr. WALZ. Thank you for that. I yield back, Mr. Chairman. Again, thank you for this hearing.

Mr. DENHAM. Thank you, Mr. Walz. Mr. Heslop, did the SEC leasing regulations and policies in July of 2010 require written approval by the chairman or commissioners of the SEC?

Mr. HESLOP. Not to my knowledge.

Mr. DENHAM. Not the chairman or the commissioners? A half-a-billion dollars, you go out and spend a half-a-billion, commission and chairman not needed?

Mr. HESLOP. To my knowledge, it was a delegated responsibility.

Mr. DENHAM. What approval process did they require?

Mr. CAHN. That responsibility, or the delegated responsibility for approval of leases, resided with the executive director of the Agency. And I do not know, at the time, what approval underneath him was required for him to execute an approval.

Mr. DENHAM. And what type of expenditures is the executive director authorized to make?

Mr. CAHN. I don't know the level of his approval. I don't know whether there is a particular cap. I just know with regard to leasing decisions, that was delegated from the chairman to the executive director at the time of this lease.

Mr. DENHAM. What is the largest expenditure that has been done in the past?

Mr. CAHN. I don't know the answer to that, but I would be happy to have that information pulled together and provided to the committee.

Mr. DENHAM. Do you have any idea? Ballpark?

Mr. CAHN. (No response.)

Mr. DENHAM. Is this the largest?

Mr. CAHN. I do not—I just—I do not know, I'm sorry.

Mr. DENHAM. Have you ever heard of the executive director spending $1 billion?

[No response.]

Mr. DENHAM. $1 trillion?

Mr. CAHN. No, no. I do not know how the size—these lease payments compare to the size, for instance, of the lease payments in connection with the Station Place headquarters location, which I believe is a larger footprint.

Obviously, the numbers we are talking about are the aggregate amount over the lifetime of the lease, as opposed to an annual expenditure. I do not know, with regard to particular line items, what is the largest expenditure in an—on an annual basis that the executive director has authority to approve. But I would be happy to get that information to you.

Mr. DENHAM. So are you saying, then, because it is over a term, that the SEC would look at this on an annual basis, and spending authority may have been less than the half-a-billion?

Mr. CAHN. No. You were asking about——

Mr. DENHAM. You are just saying you have no idea.

Mr. CAHN. You asked me what the largest expenditure was, whether half-a-billion, and it depended, I guess, on how you measured it, whether you measured it on what the annual impact was, or over the lifetime of the commitment. And I was just saying that I didn't know the answer to the question of what the largest one was that the executive director had approved, but we would be happy to get that information to you.

Mr. DENHAM. And approval process that is currently required?

Mr. CAHN. I believe right now, with regard to leases, that authority resides with Mr. Heslop.

Mr. DENHAM. And prior to this?

Mr. CAHN. Prior to the immediate—immediacy, I believe it resided with the executive director. Those authorities have been transferred to Mr. Heslop, so he now has the authority—all leases need to be approved by him.

Mr. DENHAM. So Mr. Heslop has the authority to commit our Federal Government to a half-a-billion dollars with no other authority at all?

Mr. HESLOP. Sir, as I stated, we are conducting, in process, as we speak, an independent——

Mr. DENHAM. Oh, I understand that there is a process that you are——

Mr. HESLOP [continuing]. Analysis of all of our——

Mr. DENHAM [continuing]. You are looking at going after——

Mr. HESLOP [continuing]. Of our policies——

Mr. DENHAM [continuing]. But I just want to know right now, today, do you have the authority to go out and spend a half-a-billion dollars?

Mr. HESLOP. I don't believe that I do, sir. But the policy that we typically follow is we have an annual budgeting process. That budgeting process is approved by our financial management oversight committee.

So, first of all, we are limited within the confines of the SEC's budget on an annual basis. And then, expenditures from within that are taken through a governance process of our financial management oversight committee. And as a rational man, sir, I would not take a decision of half-a-billion dollars independently. I would run it through the committee, and run it through the chairman.

Mr. DENHAM. And, as COO, you oversaw annual budgeting processes in the past. So this isn't something—an annual budget process is not something new you guys have just implemented in the last few weeks, is it?

Mr. HESLOP. No, sir.

Mr. DENHAM. OK. So you oversaw that as COO prior to this.

Mr. HESLOP. I did not last year, sir. I have just assumed these responsibilities within the last 7 weeks.

Mr. DENHAM. So the executive director went over the annual budget process.

Mr. HESLOP. The executive director previous to me was on top of the annual budgeting process, yes.

Mr. DENHAM. And, as COO, do you not look at the budget?

Mr. HESLOP. As COO, I looked at the budget as it related to those functions underneath my umbrella of responsibility. And at that time that did not include budget management. It did not include the Office of Administrative Services.

Mr. DENHAM. I just want to, for the record—COO does stand for chief operating officer, correct?

Mr. HESLOP. Sir, the Commission had a bifurcated approach to oversight of the back office functions in the past. It is a—it was a recommendation recently we had—as you know, Dodd-Frank requested an independent assessment of the Agency. The Dodd-Frank study recommended that those functions be consolidated under one head. It was consolidated under me, approximately 7 weeks ago.

Mr. DENHAM. OK. So, under your testimony, prior to your new duties you were not authorized to look at the annual budget.

Mr. HESLOP. I was certainly authorized to look at the annual budget——

Mr. DENHAM. You just chose not to.

Mr. HESLOP. I looked at it with respect to those functions that were under my tutelage: Office of Information Technology, Office of Freedom of Information Act, Privacy, and Records Management.

Mr. DENHAM. So was a half-a-billion dollars under last year's annual budget?

Mr. HESLOP. Again, sir, I don't know. I did not look at that component of it.

Mr. DENHAM. You missed that piece of it. How big is the annual budget?

Mr. HESLOP. I think we are at approximately $1.1 billion.

Mr. DENHAM. I would at least, as CEO, expect that you would—even if you chose not to look at the entire annual budget, that you at least looked at a top line. Would you not?

Mr. HESLOP. I reviewed the budget, sir. Yes, sir.

Mr. DENHAM. OK. So you said $1.1 billion is the annual budget?

Mr. HESLOP. Approximately, yes.

Mr. DENHAM. And we went out and spent a half-a-billion dollars. That did not even take a jump on the radar screen to say, "Wait a minute, this is—I must need to look into the budget further, because this is a big jump in what our annual budget authorizes."

Mr. HESLOP. Again, sir, I was not privy to any real estate decisions, this one in particular.

Mr. DENHAM. I just want to understand. You know, as CEO your decisionmaking process—obviously, if you have got to at least look at the top line—maybe you weren't inquisitive enough to look at the entire budget.

But if you are at least looking at the top line budget numbers, and your budget went from $1.1 billion to $1.6 billion, that somewhere there must be a big issue there. If you are looking across the Nation and we are making cuts, the President has made a decision that we are going to cut spending, or at least, at the time, freeze spending, and you, as chief operating officer, saw the top line budget, $1.1 billion increasing to a large amount, did you not think, as chief operating officer, that maybe you ought to look deeper into the budget and figure out where the discrepancy is?

Mr. CAHN. If I may?

Mr. DENHAM. Mr. Cahn, if he doesn't understand the question, maybe you can answer for him.

Mr. CAHN. Let me try, Chairman Denham. I mean I think that it is a very important question. I think the issue focuses on the Antideficiency Act issue, because the question, as I understand it presented by the Antideficiency Act, the issue is whether, as an agency with independent leasing authority, and authority to enter into multiyear leases, whether we are required, consistent with the Antideficiency Act, to obligate funds for the entire amount of the contract in the first year of the contract, or whether, consistent with the Antideficiency Act, we are permitted to obligate funds only on an annual basis for what amounts are due.

Certainly agencies, such as GSA, it is clear that they may obligate their long-term leases on an annual basis. We have understood since 1990, when we received independent leasing authority, that we could, consistent with the Antideficiency Act, obligate those funds on an annual basis, and that is something that hasn't been questioned by OMB or GAO in the course of their audits of us.

But, having said that, that is the question that the inspector general has legitimately raised in connection with his investigative report. And that is why we have submitted that question to the comptroller general. Because if, consistent with our interpretation of the Antideficiency Act, it is permissible to present in our budget our long-term leases on an annual basis, I think that answers your question.

Obviously, if the determination comes back——

Mr. DENHAM. It doesn't answer my question. It doesn't even scratch the surface. I am out of time right now.

But I am just—I am amazed that chief operating officer and his legal counsel, you know, whether it is over the course of a 10-year obligation—if you are at $1.1 billion and it jumps to $1.2 billion, or 1.1 to 1.15, somebody needs to be asking some questions. And if we don't have the right people in charge to be able to ask those questions, then we need to make some changes.

Ms. Norton?

Ms. NORTON. Thank you, Mr. Chairman. One of the problems we are experiencing here you need to really take into account. We see no energy for reform coming from these witnesses. We understand what the IG said.

That is befuddling to me. I don't know if you understand the gift you are giving to those who oppose Dodd-Frank, while many of us are up here trying to remind people that the way we got into this hole was, if you will excuse me, some of the problems that were raised at SEC and the problems that Dodd-Frank is meant to cure.

So, what—your failure to even want to remove an employee who has been named as the source of the abuse is like going to those who oppose Dodd-Frank and said, "Here is something further for you." It is befuddling to me.

And, Mr. Heslop, your testimony—you are big and bold. "Although the SEC is no longer pursuing space in Constitution Center, the Agency continues to believe that significant staff will be required to carry out the new responsibilities"—good luck, good luck getting it from this Congress—"assigned to the Agency under Dodd-Frank. To this end, the SEC will continue to assess its space needs"—"Congress, we are going to continue to look at our space needs"—"in the context of its current budget, and the overall resources available to the Agency."

I looked through your testimony. I didn't see anything in the testimony that says—and I will tell you what, Mr. Chairman, any resources we get will be devoted to the regional offices the way the chairwoman said it should, in the first place. Instead, you refer increasingly in your testimony—I have pulled it out to new responsibilities, need for space because you've got new responsibilities, continuing resolution didn't give you all the money you needed to carry out these responsibilities.

Nowhere do you indicate that the chair said you were to carry out those responsibilities in the regional office, so you probably won't need any more space in the District of Columbia. Isn't that the case?

Mr. HESLOP. Ma'am, as I mentioned earlier, the BCG study that was done as a result of the Dodd-Frank Reform Act required us to take a look—basically, do an independent assessment of the SEC.

And as a result of that study, one of the recommendations was to look at our regional strategy. And that is exactly what we are doing. That analysis——

Ms. NORTON. You don't mention that in your testimony. You don't mention in your testimony that any resources that you are lucky enough to get would go certainly not to a Washington, DC—now, this is my district, I always love to have people lease in my district, but I do have an oath to be a Member of Congress first, and responsible to taxpayers—you don't even say that no more space would be sought in the District of Columbia. Can you at least say that this morning?

Mr. HESLOP. It will be totally dependent, ma'am, on the level of resourcing that we get to execute the new responsibilities that we have been given under the Dodd-Frank Act.

Ms. NORTON. All right, Mr.—what you are saying is on the record and under oath.

Mr. HESLOP. Yes, ma'am.

Ms. NORTON. And that is going to be repeated back to you time and time again.

Mr. HESLOP. It is——

Ms. NORTON. Not only with respect to this issue, but with respect to your very important mission.

Now, I am—with—and when I say Congress would like to see, whenever we see a problem, that there is somebody who is gung-ho on fixing the problem. I don't see anything like that from anybody, except the IG, who can't fix it, because that's not his job.

I asked staff to pull up what leases were coming up. And that is one of the reasons why I think we have to, Mr. Chairman, do a bill. Because they have got some leases coming up in the very near term. And let's look at Atlanta, where they are 383 feet above the standard level of other Government employees. That is coming up—well, that is already done.

Would you—I want to—perhaps you don't have off the top of your head. I would like to know whether you—would you get to the chairman on whether or not you have renewed the Atlanta lease, which ran out on June 19, 2011, for 114 people for the same amount of space?

But let's move on. On 2012, January, Chicago. It is rented at—it is leased at 419 per person. At—and that is coming up in 2012. In Los Angeles you have got 336 per person. Understand we are talking about 200 square feet per person, and some law firms in this town are going down to 175 square feet per person, because they don't want to spend all their money, what they have left, on leasing. In Miami, 449 square feet per person. Your total regional offices are at 492, on the average, per square—square feet per person.

Now, let me ask this, in case—if you are left with leasing authority, would you agree today to draw down the utilization rate to the standard utilization rate of 200 square feet, or 230 square feet, so as to reduce your utilization rate in any new contracts you would be fortunate enough to make?

Mr. HESLOP. Yes, ma'am, we would certainly consider that figure.

Ms. NORTON. Seems to me that you will have some difficulty doing that if you are leasing—if you are renewing leases. But that is something that any competent real estate operator would be doing now, he would be renegotiating every single lease you have.

I think the chairman asked about are there other buildings with this kind of lease. I just want to record that you have made the top 10 of leased space ever in the District of Columbia.

Could I ask the IG whether you think, in light of your report, that Congress would be well advised to revoke the leasing authority of the SEC?

Mr. KOTZ. Yes, obviously it is something that requires serious consideration. I would say this. You know, looking at the way the leasing practices have been run to date, I would say there is no question that the leasing authority should be taken away.

If significant changes are made, if there is a complete cleaned house at the Office of Administrative Services, if everything is done differently going forward, then I think there would be a possibility to allow that to go forward. But certainly, from what we saw, I don't think that the SEC has done a capable job of exercising that leasing authority.

I would think that there would have to be a drastic and significant change in the way——

Ms. NORTON. Well, let me—all right. Let's consider this drastic change.

Mr. Heslop, in the present staff, who has had any background or experience in real estate transactions of the kind, for example, that GSA requires in the ordinary course of doing business? And what has that experience been?

Mr. HESLOP. There are a number of current staff that have actually had GSA experience. We have a lead realty specialist with 20 years of GSA realty contracting and policy experience, and has been at the SEC 2 years. We have a lead realty specialist with nearly 10 years of GSA realty contracting and policy experience. We have a realty specialist with 11 years of GSA realty contracting experience, and——

Ms. NORTON. Mr. Heslop, the IG—read the IG's report. The IG said that those with any real estate experience, those are fairly minor—those with fairly minor roles, even at GSA, were routinely ignored.

Does Sharon Sheehan have any significant real estate experience? And she is the woman in charge, and the person the IG finds was deeply involved in these abuses. Has she any real estate experience?

Mr. HESLOP. I am not aware of what her professional history and how deep it is——

Ms. NORTON. Would you see to it that the chairman receives her resume?

Mr. HESLOP. Sure.

Ms. NORTON. Within the next 10 days. Let me ask about the status of Constitution Center. I have toured Constitution Center. It is an extraordinary facility. This is a facility that was apparently built for—as a secure facility, recognizing that, after 9/11, the Government would be looking for secure facilities for certain kinds of agencies. Is the SEC classified as a secure facility?

[No response.]

Ms. NORTON. Are you like the Defense Department? Are you like the Department of Homeland Security?

Mr. HESLOP. I am not aware of the classification system that——

Ms. NORTON. What kinds of employees would have or are now in Constitution Center from the SEC? What are their duties?

Mr. HESLOP. I am not aware of any employees in Constitution Center at the moment, ma'am.

Ms. NORTON. All of the employees are out?

Mr. HESLOP. Yes, ma'am.

Ms. NORTON. What kinds of employees were housed there before you got GSA to help you try to find others for this space?

Mr. CAHN. Congresswoman Norton, I don't believe any SEC employees have been at Constitution Center at any time.

Ms. NORTON. So nobody ever made it into Constitution Center?

Mr. CAHN. That is correct.

Mr. DENHAM. And I would like to follow up on the same round of questioning. What was the intent? Is there a specific reason why this building was picked? Does the SEC have specific requirements that would require a secure building?

Mr. HESLOP. Not to my knowledge. The way the Department of Defense—you know, a specific type that the Department of Defense organization might have. Based on my two decades of experience in the military, I don't believe the SEC has the kinds of requirements that you might find with several of the DOD-type activities.

Mr. DENHAM. Let me switch the line of questioning back again, Mr. Heslop. Last week you and Mr. Cahn, you met with my staff, subcommittee staff. When we requested the SEC provide the subcommittee with an unredacted copy of the IG report, committee staff was informed "a formal written request should be made so that the SEC commissioners could review the request and approve it."

What types of administrative decisions do the commissioners review and approve, and why are leasing actions, especially one binding the Federal Government to a half-a-billion dollars, not included among them?

Mr. CAHN. Chairman Denham, as I mentioned, the—well, as you know, we have produced the unredacted report and exhibits to the committee in connection——

Mr. DENHAM. Well, I understand. And my concern is, for a simple report, before you come before a congressional committee to testify, you required a written notification to go to the commissioners, so the commissioners could vote on whether or not you just were going to provide a simple piece of paper that should be open to the public.

Now, if you have got to go to the commission to ask for approval and a vote to give Congress some information, but you don't have to go to the commission for a half-a-billion dollars, I would assume there is something wrong with the approval process there, or your priorities are deeply skewed.

Mr. CAHN. I appreciate that, Chairman. And I think certainly, going forward, we need to look at whether we need a process that involves going to the commission, as opposed to the delegated authority that we have now. The delegation to the executive director

is in accordance with the manner in which certain administrative functions, as opposed to adjudicative and other functions, are delegated within the commission.

But I think you obviously raise a very significant point, and one that we are currently evaluating right now.

Mr. DENHAM. You are evaluating a lot of things with no answers.

You know, we had invited Commissioner Shapiro to be here to testify today. I understand that she is wrapping up her testimony in Financial Services. Mr. Manley, I would ask you to go over to Financial Services, and if she wraps up her testimony, maybe she can come here and provide some answers and some greater detail.

I know you are new, Mr. Heslop, with some new duties, but some of these questions are pretty basic questions. If somebody in my company answered these questions in the manner that you guys are, there would be a lot of people fired. I mean this is just amazing, that half-a-billion dollars—you want us to go back to the commission just in asking for the unredacted copy of the IG report and take a vote by the commissioners, but the commission doesn't require you to go to them with a half-a-billion dollars? And, Mr. Heslop, you oversee the annual budget, but you don't notice when a large expenditure like this is being proposed? That's amazing.

Ms. Clancy, in your testimony you provide an overview of how GSA normally reviews and approves leases. During GSA's process, does GSA keep track of necessary approvals orally, or do you get approvals in written documentation?

Ms. CLANCY. Our process is fairly extensive, and we actually have a formal written process that tracks those, both electronically as well as through a paper process which gets input later on into our electronic system. So it's two—at two levels.

Mr. DENHAM. Mr. Heslop, in your testimony you mentioned that the SEC has worked with the landlord of Constitution Center to find other Federal tenants to release "part of our obligation under the lease." You also indicate the SEC is working with GSA on filling the remaining space. Can we assume, then, that the SEC has concluded that the lease obligation is a valid one?

Mr. HESLOP. [No response.]

Mr. DENHAM. Are you obligated to the lease?

Mr. HESLOP. Yes. Yes, it is——

Mr. DENHAM. Somebody signed it.

Mr. HESLOP. It is a valid lease.

Mr. DENHAM. OK. So, the Federal Government is on the hook for this long-term lease. Where are we, as far as getting out of that obligation, or releasing that to others?

Mr. CAHN. Right, we are—we have been working closely and we are working closely with GSA and other entities, and we are hopeful that we can do that. And I would defer to the GSA to be able to respond more to the——

Mr. DENHAM. You are hopeful? Where are we in the process?

Mr. CAHN. We have been in discussions with them, and we are——

Mr. DENHAM. When did you realize this was a problem? Was it before the IG report came out, or——

Mr. CAHN. We have been in discussions with GSA, I think, going back to the fall, yes. So we have been——

Mr. DENHAM. OK. So you have been working on it since the fall. Where are we?

Mr. CAHN. We are still working with them. I think it is a matter of them——

Mr. DENHAM. You are working with them. That is the best answer you can give us today? How far are you working with them? Do you have any—are there any proposals out there? Are there any signed agreements? Do we have anybody under lease today?

Mr. CAHN. With regard to the remaining space, there isn't anyone yet that is under obligation to take that remaining space.

Mr. DENHAM. So we were able, over a weekend, to approve a half-a-billion dollars of taxpayers' money without any authority from the commission, from Congress, from the President. We were able to, over a weekend, go out and secure half-a-billion dollars worth of space, and over the course of a year we have not been able to get out of that lease or find anybody else who was willing to lease that property.

Mr. CAHN. I think, as Mr. Heslop's testimony mentioned, we were able to identify two tenants to take the majority of the space. There is still a balance, you are correct, and——

Mr. DENHAM. You have identified, or they are under new contract?

Mr. CAHN. They are under new contract for the—for most of the space. There is about 340,000 square feet that remains that we are working with GSA on.

Mr. DENHAM. And who are those new tenants?

Mr. CAHN. FHFA and OCC.

Mr. DENHAM. And GSA? Have they already—each of those agencies already gone out for proposal on new space?

Ms. CLANCY. I believe—we were not involved in either one of those leases for OCC or FHFA. I believe that both of those agencies have their own leasing authority. And so those leases, to my understanding, were negotiated directly with the landlord.

Mr. DENHAM. The landlord being?

Ms. CLANCY. The landlord at the Constitution Center.

Mr. DENHAM. But had to renegotiate. Now we are subleasing this space. SEC is subleasing this space to two other Government agencies that also have their own leasing authority to help come in and fix the problem.

Mr. CAHN. My understanding is that we released the space, so they are in direct—they have a direct lease agreement with the landlord. So we are not subleasing that space to FHFA and OCC.

Mr. DENHAM. But SEC——

Mr. CAHN. I can confirm that.

Mr. DENHAM [continuing]. Is still on the hook for the rest of the lease.

Mr. CAHN. Yes, sir.

Mr. DENHAM. Thank you. Mr. Walz?

Mr. WALZ. Thank you, Mr. Chairman. Mr. Heslop, I want to get back at something just a little bit here, trying to understand this on how something like this happens. It is going to be—the details are going to come out, as I said, and we will get it all right.

You come to this job with private sector experience. I want to go back to where—you were at Capital One, is that correct?

Mr. HESLOP. That is correct.

Mr. WALZ. And Capital One is the thirteenth largest financial institution in the United States?

Mr. HESLOP. I believe that is correct, sir.

Mr. WALZ. OK. And you were there about 12 years?

Mr. HESLOP. Yes, sir.

Mr. WALZ. So you got a chance to understand their internal culture and how things work and how they would go about leasing, expanding, and those decisions?

Mr. HESLOP. I was very familiar with the risk management internal controls component during my tenure at Capital One. I did have some small degree of leasing interface, as well. It was not huge.

Mr. WALZ. For the critics that are always there—and in this case it looks like rightfully so—that Government can't get things right, would Capital One have made a mistake like this?

Mr. HESLOP. I can't speculate as to whether they would have made one.

Mr. WALZ. Would there have been safeguards, culturally, that would have prevented it from happening, in your opinion?

Mr. HESLOP. It is actually an interesting question. I believe when I first got there, there was not a strong culture of internal controls and process and rigorous discipline. One of my roles, while I was there during my tenure, was to implement, on a global basis, a very strong disciplined internal control program, which, over time, you know, was instituted into the culture, and became very successful.

So, I would say the answer to your question would be early on it could well have happened. Later on, toward the end of my tenure, I think we had a rigorous control environment in place.

Mr. WALZ. And I know that the—and it comes with the nature of leadership—you are going to take a lot of responsibility for things, one way or another, and that is the way it should work, to a certain degree.

My questions are that I often times see inside of Government agencies is sometimes a career staff there, maybe working at cross purposes to the person who is put in into the leadership position. Do you feel there is a problem at SEC, in terms of management and your ability to be able to dictate, or at least oversee, if that's a better term?

Mr. HESLOP. I would not characterize it as a problem. I would say that there is an opportunity to change the culture, as it relates to, you know, a more disciplined approach to controls, in general. I think that with the IG we have been making good strides in that direction, and we have evidence of that in some specific areas over the course of the last year. We have more to go. The OAS organization is one of those, which is now under my tutelage, and I very much intend to bring that organization under control as well, with specific—specifically focused around the leasing of facility space.

Mr. WALZ. Do you share the chairman's frustration on—that it is not moving faster? I understand there is a relative amount of time—the one thing I think I see, and I think the public gets a frustration with—and I think it's a valid concern—even large bureaucratic—which I think you could argue Capital One is big

enough to have some of that—they seem to be more nimble at times on being able to do that.

Are we still hampered with not moving at the pace of the way the world moves now inside our agencies? Because I don't know how long this takes. I am not—I don't have a best practices that says how long it should take GSA and everyone to work on this. My intuitive sense tells me, like the chairman is saying, it should move a hell of a lot faster.

And I want to know. How do we determine that? Or how do we make sure that is happening? And that is something where you and leadership could implement, I would think.

Mr. HESLOP. I think I would definitely agree with you, that I would like to see it move faster. There are a number of constraints that one faces in an organization like this that you don't face necessarily on the private sector that impede progress along a more rapid glide path. We are trying to work, you know, as effectively and efficiently as possible, tackle those obstacles, and move the ball down the path.

Mr. WALZ. Well, I think that is our charge right now, that those of us—and, as I said, I am going to be fighting for a proper amount of funding, making sure it is used right, making sure the IG has their ability, making sure you have the ability to oversee what I think was reckless disregard for the public welfare and the economy that collapsed this economy. But right now I think the ranking member is right. We have given them—not only teed it up, we have given them a damn beach ball to hit over center field that "These guys are reckless, can't do anything right, how dare they oversee us in the private sector?"

So, I am looking for you or someone to stand up, the director, whoever it is, to stand up and say, "We are going to implement these things, we are going to move faster, we are going to take these IG recommendations from some experts, we are going to look at them and see if we can implement it," and then come back to us if this is the case.

And I know that there is no one, other than the ranking member, no one in Congress, that cares more about due process, but her frustration with employees—we don't—we are not just going to jack somebody, move them out, and not give them due process or whatever. But I think if someone has made such a gross error, there has got to be ability to, if you will, move her to the corner and sharpen pencils until we figure this out. That should be able to happen.

Is that true? I mean don't you think—come to us if we are hampering you with some of those. Come to us and say, "We need the ability to have more flexibility to move some of this stuff."

So I just—I offer that to you. I want—as I said, you are going to take your lumps on this. You are experienced, you have been in the private sector and done this. But I think what the chairman is looking for, too, is, yes, a fix of this initial problem. Certainly what I am looking for is what we are going to do, moving forward.

And this economic difficulties we are having presents golden opportunities to streamline our operations and make it work better.

And so, with that, I yield back.

Mr. DENHAM. Thank you, Mr. Walz. I have just been informed by Mr. Manley that the commissioner is still testifying, she is going

to be unable to come back after our votes. We have been called to votes now.

So, I made the determination we are going to be having a second hearing. There are just too many unanswered questions here. But in this next hearing I will expect to know who has been fired during this whole process. If we can all agree that there has been some wrongdoing done here, which—I would at least hope that we could agree to that—I would expect to see who is being held accountable on this.

I also want to know the budget oversight process, because this seems like a gross abuse of taxpayer dollars.

And I also know that the Agency would not make available Ms. Sheehan to testify. And before we close the hearing, I have got a couple of documents that we are going to show. But I will just inform this panel, as well as the SEC, that this committee does plan on using its subpoena authority. We will have people here, and we will demand answers for the taxpayers.

With that, I know that Ms. Norton is on a tough time schedule, so I would like to recognize her for a brief statement.

Ms. NORTON. I thank you, Mr. Chairman, for your indulgence. What I regret is that you have infected your important mission here, and we really don't need that up here. You've got to separate out these two missions, and you've got to do it very quickly.

I want to just clarify the IG's statement. He had said, well, if they had—you know, perhaps they could carry on such activities if, you know, they changed everything. Let me ask you whether—two things, whether they could carry it on with the same person in charge, and whether you think that, in light of their core mission, they would be better off devoting most of their time or all of their time to their core mission.

Mr. KOTZ. Certainly with respect to the first question, no. They would need to have new people in charge. I think if the same people were in place, they wouldn't be able to carry on in an appropriate way.

In terms of their overall mission, I think that is a very valid point, that obviously, what the SEC is trying to do is enforcement, other matters related to the financial system. And certainly, time spent dealing with these issues is not productive to their mission.

You know, in terms of how that would come out, that is really up to Congress to decide.

Ms. NORTON. Thank you very much. Those were definitive enough responses.

Mr. DENHAM. Thank you, Ms. Norton. Mr. Kotz, your investigation found that the dates on the signature page of the justification for sole-source procurement was misleading, to say the least.

Put the slides up here.

[Slide.]

Mr. DENHAM. On the screen is a copy of the signature page. Can you explain what the issues are, and why they are significant?

Mr. KOTZ. Sure. If you can see on the signature page, the signatures are dated August 2nd. However, the document was not finalized on August 2nd. It was signed, and then revised substantially. It was not finalized until September 2nd. And, in fact, one of the

signatures that was written, it was signed on August 31st, but they wrote in "August 27th."

But then, when they saw that the other signatures were August 2nd, they whited out the 7 so it would appear like it's August 2nd. And you can see there is a space. You can see there is a space under that second signature from the bottom, where it is pretty clear that there was a 7 or another number there, and that was whited out to make it appear that they were all signed on the same day.

In fact, the document was not finalized until a month later.

Mr. DENHAM. Mr. Heslop, have you seen these documents before?

Mr. HESLOP. I have.

Mr. DENHAM. Can you at least recognize that there is an issue here?

Mr. HESLOP. Absolutely. We do not condone back-dating of documents. We are managing the disciplinary action process aggressively, and we will take appropriate action, upon completion of the recommendations to me.

Mr. DENHAM. What type of recommendations are you waiting for?

Mr. HESLOP. I am waiting for the general counsel and the Office of Human Resources to provide me recommendations as to appropriate disciplinary action with respect to each of the individuals named.

[Pause.]

Mr. DENHAM. You know, I am not somebody who is normally at a loss for words. But I got to tell you, this is amazing. It is a complete gross abuse of taxpayer dollars.

Mr. Heslop, I am—quite frankly, I am amazed at your testimony today. You are the COO of a very large agency with a very large budget, huge responsibilities. I would assume you are a pretty bright individual to be able to sit in this spot.

I am—I will look forward to our next hearing, and I will expect some answers. We will give the SEC plenty of notice, we will give you plenty of time. But I will expect everybody that we send an invitation to to not only respond to that invitation and make sure their schedules are available, but we will subpoena them. We will bring them in. But we expect accountability. And the answers that we have received today are just completely unsatisfactory. We have votes taking place on the floor right now.

I would like to thank each of our witnesses for their testimony, or lack thereof. We will be following up with questions for the record. And I would ask that you provide your responses in a timely manner.

I ask unanimous consent that the record of today's hearing remain open until such time as our witnesses have provided answers to any questions that may be submitted to them in writing, and unanimous consent that the record remain open for 15 days for additional comments and information submitted by Members or witnesses to be included in the record of today's hearing.

[No response.]

Mr. DENHAM. Without objection, so ordered. If no other Members have anything to add, this subcommittee stands adjourned.

[Whereupon, at 11:51 a.m., the subcommittee was adjourned.]

Eleanor Holmes Norton

STATEMENT OF
THE HONORABLE ELEANOR HOLMES NORTON
SUBCOMMITTEE ON ECONOMIC DEVELOPMENT, PUBLIC BUILDINGS
AND EMERGENCY MANAGEMENT
TRANSPORTATION AND INFRASTRUCTURE COMMITTEE

HEARING ON
"The Securities and Exchange Commission's $500 Million Fleecing of America"

June 16, 2011

Welcome to today's hearing on the Securities and Exchange Commission (SEC) Inspector General's (IG) May 16, 2011, report on the SEC leasing deal for the Constitution Center building located in Southwest Washington, D.C. The shocking findings by the IG on a leasing agreement for more than $500 million paints an outrageous picture of an agency that was not competent to engage in real estate transactions and, consequently, developed a culture that allowed bureaucrats to make major, unsupported financial commitments on behalf of the agency, using outright deceit and possibly fraud.

In the aftermath of the financial crisis, the Dodd-Frank regulatory reform legislation provided the SEC with new responsibilities to oversee our nation's financial system and authorized it to hire a large number of employees. Although no appropriation was made to hire these new employees, on July 28, 2010, the SEC entered into a sole-source procurement for 900,000 square feet of space, with an option to lease 500,000 additional square feet at Constitution Center to accommodate these new employees. In early October 2010, the SEC informed the building owners that it did not need approximately 600,000 of the 900,000 square feet and would not need the additional 500,000 square feet either. The SEC and Constitution Center are currently in a dispute over the SEC's obligation to pay approximately $94 million under the agreement for the leased space it longer needs.

The IG findings are so serious that they point toward criminal violations by federal employees in the course of their official activities leading to the execution of the lease. According to the IG, several SEC employees worked in concert to repeatedly subvert the direction provided by the SEC chairman on the placement of new employees, made false representations, and doctored documents to justify a sole-source procurement. SEC employees relied on the self-delusion that Congress would appropriate all the authorized funds under the Dodd-Frank regulatory reform legislation, although the notion that the SEC would receive an appropriation equal to the full authorization level for new employees was inconsistent with the history of the SEC appropriations, and flies in the face of the simple fact that authorized discretionary funding does not guarantee an appropriation of such funds. More importantly, the notion that all of the new employees would be housed at the SEC headquarters was found to be completely unsupported by, and even at odds with, the express direction of the SEC chairman that most of the employee growth should be concentrated in regional offices.

The abuse did not end there. Contrary to the General Services Administration (GSA) standard of 230 square feet of building space per person, the SEC Office of Administrative

Services (OAS) estimated a need for 400 square feet per person, nearly double the GSA standard. This overly generous standard was later inflated by 49 percent for auxiliary staff, even though the 400 square feet per person estimate was actually meant to accommodate the auxiliary staff. The IG concluded that this inflation by the SEC OAS "employed a series of unfounded, egregiously flawed, and irresponsible projections to derive the purported need to lease 900,000 square feet." Even if the SEC had received all funds authorized by Dodd-Frank legislation, the SEC would have needed, at most, an additional 300,000 square feet, only one third of the 900,000 the agency eventually leased. Why did the SEC lease 900,000 square feet? The answer provided by the IG is that a few SEC OAS officials had "grandiose plans" to lease the upscale Constitution Center. Having set the target square footage, the SEC OAS officials worked backwards using a "deeply flawed and unsound analysis" to justify the lease, according to the IG.

To compound the damage, the $556 million lease was a sole-source contract procurement "negotiated" over only three days. Only after the contract was signed did the SEC prepare a Justification and Approval for Other than Full and Open Competition. According to the IG, the Justification and Approval was "inadequate, not properly reviewed, and backdated..." and was prepared well past the regulatory deadline for such contracts. The IG also has raised the serious concern the contract violated the Anti-Deficiency Act that, amongst other things, prohibits officers or employees from expanding or obligating an amount exceeding an appropriations, and from involving the government in a contract or obligation for the payment of money before an appropriation unless authorized by laws.

Astonishingly, this transaction represents a pattern since the SEC was granted leasing authority in 1990. The agency has made repeated missteps, from the build, to, suit lease for the SEC headquarters located behind Union Station, which lead to $48 million in construction overages, and to the mishandling of leases in San Francisco and New York, to only forming a leasing division 19 years after receiving leasing authority. The SEC was granted its own leasing authority with the expectation that such authority would be "...exercised vigorously by the Commission to achieve cost savings and to increase the Commission's productivity and efficiency." Sadly, the opposite has been the case, which calls into serious question the grant of leasing authority to the SEC or any federal entity other than the GSA.

This subcommittee has an obligation to taxpayers to understand the steps that led to the Constitution Center lease, to take corrective measures to ensure that the SEC can no longer engage in leasing activities, and to ensure that appropriate action is taken regarding the employees involved. Notably, several employees implicated in this leasing transaction have refused the subcommittee's invitation to testify, and at least one of the principal players named in the IG report still has oversight of the SEC leasing program. The SEC leadership is on notice that if there is retaliation against the employees who provided testimony and tips to the SEC IG, we will respond immediately.

I appreciate the testimony that has been prepared, and I look forward to hearing from today's witnesses.

U.S. General Services Administration

Elaine Clancy
Director of Leasing
National Capital Region

Committee on Transportation & Infrastructure
United States House of Representatives
U.S. Securities and Exchange Commission
Lease at Constitution Center
June 16, 2011

Good morning Chairman Denham, Ranking Member Norton, and Members of the Committee. I appreciate being invited here today to discuss the U.S. General Services Administration's (GSA) approach to the acquisition of leased space for Federal agencies.

GSA searches for the most effective ways to provide space for Federal agencies that help them achieve their missions, while protecting the public's interest. In order to accomplish these goals, GSA implements a deliberate and comprehensive process that ensures adequate competition and takes into account other public interests, including placement in central business districts or facilities which are close to public transportation.

GSA currently has an inventory of over 370 million square feet of space, approximately half of which is spread among nearly 9,000 leases across the country. GSA effectively manages its leased space. In FY2010, leased space vacancy was only 0.8 percent. GSA leases space for most Federal agencies including, but not limited, to offices, laboratories, warehouses, and clinics. Leases are located according to the client agency's mission requirements in urban, suburban, and rural areas and in accordance with established location laws and policies.

Space Planning with Agencies

A potential leasing action begins when a Federal agency brings a space request to GSA. These requests can range from replacement leases, expansion space, or more effective space for an agency's mission. In all cases, we first determine if federally owned or leased space is already available that could meet the agency's requirements. If unavailable, GSA evaluates the appropriateness of a potential leasing action.

GSA's inventory includes approximately 9,000 leases. GSA tailors its approach to space requests based on the size and complexity of the identified need. Leases under the current prospectus threshold (i.e., a net annual rent less than $2.79 million for FY2011) represent approximately 98 percent our leases and 73 percent of the leased square footage. Prospectus-level leases with annual rent exceeding $2.79 million represent 2 percent of leases transacted and 33 percent of the annual rent payments that GSA makes to lessors.

The requirements-development, review, and evaluation process of prospectus-level leases is more extensive due to the size and cost of these leases. Consistent with broader Administration policy for real property, GSA strives to ensure that prospectus level lease actions reflect the best and most cost effective approach to providing the Federal government with necessary space. Specifically, GSA seeks to ensure that space is efficiently utilized, including the emerging approaches for office space configurations, identification of specialized space necessary to meet mission requirements, and

availability of space in subject markets. Additionally, these large leases require review and clearance by both GSA's Central Office and the Office of Management and Budget (OMB) prior to submission to Congress. While ensuring that proposed leases comply with all criteria governing lease scoring treatment under OMB Circular A-11, OMB also reviews the leases to ensure that the proposed action is consistent with personnel and resource estimates in the President's budget and anticipated in the outyears.

The lease prospectus discussion involving GSA, the customer agency and OMB, is the opportunity for the three parties to discuss the relationships among requirements, costs, and availability of resources leading to sound decisions that meet Government needs in a manner consistent with taxpayer interests.

GSA's Leasing Process

Once GSA has worked with an agency to carefully define and scope their requirements and ensure that the space they need is based on accurate projections and reflects available funds, GSA's lease acquisition process runs through a carefully sequenced set of steps to ensure adequate competition and a fair rental rate for taxpayers.

One of GSA's fundamental, key strategies is to promote competition by attempting to maximize the number of potential qualified offerors for a lease solicitation. By improving communication with the commercial real estate sector, GSA's presence in the market is strengthened and a sense of partnership with leasing industry practitioners emerges, resulting in increased competition for GSA leases.

GSA follows a sequenced and efficient leasing acquisition process, which includes market advertising and surveying, assessments, evaluations, negotiations, and contract execution. The details of this process are highlighted below.

Advertisement: If the space requirement is greater than 10,000 square feet, GSA advertises requirements for space on the Federal Business Opportunities website at www.fedbizopps.gov, or in the local newspaper where appropriate, in order to obtain maximum competition from the private sector. While advertising is not required for smaller space requirements, GSA often does so in order to promote competition.

Market Survey: Based on agency requirements, GSA conducts a market survey with agency representatives to identify properties that meet the agency's requirements. This is a critical step in the procurement process. If GSA determines during the market survey that there is insufficient competition in the area, GSA will work with the client agency to expand the area of consideration or refine their space requirements before soliciting the local commercial real estate market.

The Request for Lease Proposal (RLP): GSA develops the RLP package (previously known as a Solicitation for Offers (SFO), a standard document tailored to the requirements of each particular solicitation, and sends it to all prospective offerors identified during the market survey. The RLP is available upon request to any party.

Negotiations and Evaluation: Once offers are received and evaluated, GSA begins negotiations. GSA internally establishes negotiation objectives (acceptable ranges for rental rates, costs for tenant improvements, and cost ranges for additional requirements) and conducts discussions with potential lessors in the competitive range.

Final Proposal Revisions: Once negotiations are completed, GSA requests Final Proposal Revisions, where offerors are requested to submit their "best and final offer" to the Government.

Final Evaluation and Award: After submission of final revisions, GSA reviews and evaluates offers and makes an award determination. Award is made based on price or price and other factors explained in the RLP. Most leases are awarded to the offeror who meets the Government's minimum requirements at the lowest price. For more complex requirements, such as prospectus level leases, GSA may conduct "best value" procurements, which allows for a balance between the technical merits of the proposal and the cost.

Contract Execution: GSA compiles and sends an executable lease document with all negotiated terms and conditions to the apparent successful offeror for signature. Upon return of the signed lease from the apparent successful offeror, the GSA Lease Contracting Officer awards the lease by executing the lease contract.

Build-out and Acceptance: The lessor completes the build-out of the space in accordance with the requirements of the lease and GSA inspects and accepts the space when completed. Following GSA's acceptance of space as substantially complete, the Government starts payment of rent to the lessor.

Move-in: Concurrent with GSA's acceptance of space from the lessor, we assist our tenants in occupying the space, at which time their payment of rent to GSA begins pursuant to an Occupancy Agreement between GSA and the tenant agency which sets forth the terms and conditions related to their occupancy. This step completes the lease acquisition process.

Improving and Streamlining the Leasing Process

While these controls are important, GSA constantly looks for ways to streamline, standardize, and simplify our leasing processes to minimize the costs associated with acquiring a lease. We also continually assess our performance against other rental rates in the markets in which we lease space through a Lease Cost Relative to Market measure. GSA is committed to adapting its internal processes to mirror leasing in the private sector, and to fully utilizing the market leverage that results from the Federal government being a reliable tenant.

Consultation with the private sector leasing and lending community inspired GSA to undertake many improvements, such as aligning a simplified lease acquisition threshold and space terminology with private sector practices, introducing a succeeding lease model for situations where relocation is not cost-effective, streamlining the acquisition process by creating a nationwide standardized template for use by GSA's regional offices, and redeveloping FedBizOpps advertisements for greater consistency and easier accessibility.

U.S. Securities and Exchange Commission Lease at Constitution Center

In regards to the lease SEC procured at Constitution Center in Washington, DC, SEC has recently reached out to GSA to request our assistance in filling the remaining vacant space. GSA is gathering additional details pertaining to this contract and the conditions under which SEC procured the lease. To the extent we can responsibly assist in protecting the public's interest and meeting the space needs of other agencies, we will consider doing so.

Conclusion

GSA's approach to leasing Federal space allows agencies to achieve their mission effectively and works to protect the public's interest in ensuring that space is acquired at a fair rate, while being flexible to ensure that the highest levels of control are placed on the largest potential leasing actions. In addition, we aim to constantly improve our processes to attract further competition from the private sector and minimize costs to taxpayers.

Thank you for inviting me to appear before you today. I appreciate the opportunity to discuss GSA's leasing practices and expertise, and I welcome your questions.

Testimony on the Lease of Constitution Center
by
Jeffery Heslop
Chief Operating Officer, U.S. Securities and Exchange Commission

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

June 16, 2011

Chairman Denham, Ranking Member Norton, Members of the Subcommittee:

My name is Jeff Heslop, Chief Operating Officer (COO) and Acting Executive Director of the U.S. Securities and Exchange Commission. I appreciate the opportunity to testify on behalf of the Commission with respect to the agency's lease of office space at the Constitution Center building in Washington, D.C., and to share with you information on the actions that the SEC is taking in response to the May 16, 2011 report of the Commission's Office of Inspector General (OIG), Report No. OIG-553, concerning that lease.

The OIG report on the leasing of Constitution Center revealed a number of flaws in the SEC's leasing process. Although the SEC has not paid any rent and is no longer obligated for a majority of the original space, it is clear that this leasing decision lacked the rigor and attention to detail demanded for decisions of this magnitude. As such, we are committed to implementing whatever changes are needed to improve that process, starting with the retention of outside experts to conduct a comprehensive assessment of our entire leasing organization.

I joined the SEC in May 2010 as its first-ever COO.[1] Upon joining the SEC, my responsibilities were focused on overseeing the operations of the Office of Information

[1] Immediately prior to that, I worked for 12 years at Capital One Bank, including as Managing Vice President of Information Risk Management, Chief of Staff for the Chief Information Officer, and as Director of the company's Information Technology University. Prior to joining Capital One, I was a Lieutenant Colonel in the United States Army, where I served for 22 years, including as Assistant Director of the Army Pentagon Staff and Battalion Commander at the University of Richmond ROTC Program.

Technology (OIT), the finance and accounting functions of the Office of Financial Management (OFM), and the Office of FOIA, Privacy, and Records Management. In April of this year, Chairman Schapiro asked me to take over responsibilities of the departing Executive Director (ED), who was responsible for overseeing the Office of Administrative Services (OAS), which manages the agency's real property leasing activities.[2]

My charge from the Chairman is to address the issues identified in the OIG report and improve the agency's leasing processes. I can assure you that the SEC is committed to taking all necessary and appropriate actions to ensure that the SEC makes efficient and economical use of its office space, produces accurate and reliable data to support leasing decisions, and holds agency staff – from senior executives on down – accountable.

We have taken – and are continuing to take – steps to minimize the future impact of this leasing decision. The SEC has worked with the landlord to identify substitute tenants, and recently two other agencies took the majority of the space allotted to the SEC. The SEC's releases that enabled the landlord to lease the space to the other federal tenants were conditioned upon the SEC being released from all obligations for that space. SEC staff currently is working with the General Services Administration to identify other federal government agencies to fill the remaining space.

Beyond this, as described in more detail below, the SEC is actively at work to strengthen the agency's real property leasing program. In addition, we are endeavoring to ensure that any new controls and procedures we are putting in place regarding the agency's leasing decisions address the issues raised in the OIG report.

[2] At the present time, the SEC is taking steps to consolidate the COO and ED positions.

My testimony will describe the SEC's leasing program, the impact of recent statutory changes on the SEC's workforce needs, and the changes we are making to improve future leasing decisions.

The SEC's Real Property Leasing Program

The SEC currently employs approximately 3,900 permanent staff and more than 700 contractors. Approximately 60 percent of the SEC's permanent staff work at the agency's headquarters, principally the Station Place buildings located in northeast Washington, D.C. adjacent to Union Station. Additionally, certain back-office functions are staffed from the agency's Operations Center in Alexandria, Virginia. The SEC's remaining approximately 1,500 employees – principally enforcement and examinations staff – work in the agency's 11 regional offices located in New York City, Chicago, Los Angeles, Boston, Philadelphia, San Francisco, Fort Worth, Miami, Denver, Atlanta, and Salt Lake City.

The SEC does not own any of its facilities, and instead enters into commercial leases for its office space. These leases provide office space for the agency's permanent staff, temporary staff (*e.g.*, interns and fellows), and contractors, as well as space for public meeting rooms, hearing and testimony rooms, files and records storage, and information technology, including the agency's data center and alternate data center. The SEC currently maintains approximately 2.5 million square feet of leasehold interests, which includes office space in each of the cities previously mentioned. In the current fiscal year, the agency will make total lease payments of approximately $100 million, which represents about 8 percent of the agency's annual budget.

The SEC's real property leasing program is managed by OAS, specifically, its Real Property and Leasing Branch. Leasing authority is centralized within OAS, meaning that the SEC's regional offices do not have separate authority to enter into their own real property leases.

Several other OAS components have responsibilities that impact the SEC's real estate leasing program, including the Security, Construction, Space Management, and Facilities Branches, as well as the Office of Acquisitions. Other SEC offices that have significant interaction with the real property leasing program include: OIT, which equips offices with telephones, computers, and other IT equipment; OFM, which is a source of information on agency-wide budgets and resource needs; and the Office of General Counsel, which provides legal advice in connection with various leasing and acquisition issues. The Director of OAS serves as the SEC's Senior Procurement Executive and appoints a Realty Contracting Officer, who has delegated, express written authority for realty leasing on a contracting officer's warrant.

Impact of the Dodd-Frank Act

In addition to carrying out our longstanding core responsibilities, last year's enactment of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act or the Act) added significantly to the SEC's workload. The law assigns the SEC considerable new responsibilities, including establishing a new regulatory regime for the multi-trillion dollar over-the-counter derivatives market; registration of hedge fund and other private fund advisers, municipal advisors and security-based swap market participants; enhanced supervision of credit rating agencies and clearing agencies; heightened regulation of asset-backed securities; and creation of a new whistleblower program. The Act mandated an aggressive timetable for rulemaking and implementation of the statute and doubled the agency's funding authorization over five years.

These new responsibilities, when coupled with those previously existing, required the hiring of additional staff. The Continuing Resolution in place for the first six months of this fiscal year significantly limited our ability to do that. As such, if resources sufficient to carry out

our new market protection responsibilities are provided, the SEC will have a need to hire and house an expanded workforce in the future.

Constitution Center

On July 28, 2010, the SEC entered into an agreement to lease approximately 900,000 rentable square feet of office space at Constitution Center,[3] an office building located at 400 Seventh Street in southwest Washington D.C, to house new staff necessitated by the Dodd-Frank Act and to address the facilities needs created by expiring leases in Alexandria for its back office operations. The SEC's agreement contained a 10-year term, and envisioned space being delivered to the SEC in phases, with the first piece expected to be made available at the beginning of fiscal year (FY) 2012. To date, the SEC has not taken occupancy of the building, and has not paid any rent on the property.

In the fall of 2010, when it became apparent that the SEC would be limited by the Continuing Resolution and would not be receiving further funding for FY 2011 to hire additional staff – and in light of significant uncertainty regarding the agency's budget for FY 2012 – the agency's leasing branch worked with the Constitution Center landlord to identify two non-appropriated financial regulatory agencies – the Office of the Comptroller of the Currency and the Federal Housing Finance Agency – that were able to take the majority of the space allotted to the SEC, a total of approximately 558,000 square feet. The SEC's releases that enabled the landlord to lease space to the other federal tenants were conditioned upon the SEC being released from all obligations for the space.[4]

With respect to the remaining space (approximately 342,000 square feet), the SEC earlier this year determined that the uncertainty of the agency's budget for FY 2012 and beyond

[3] Constitution Center was the former headquarters of the U.S. Department of Transportation.

[4] As noted in the OIG report, the agency does not believe any damages are owed to the landlord.

counsels against retaining any space at Constitution Center. To this end, SEC staff currently is working with the General Services Administration to help identify another federal government agency to fill the space.

Although the SEC is no longer pursuing any space in Constitution Center, the agency continues to believe that significant additional staff will be required to carry out the new responsibilities assigned to the agency under the Dodd-Frank Act. To this end, the SEC will continue to assess its space needs in the context of its current budget and the overall resources available to the agency.

The OIG's Report and the SEC's Responsive Actions

The SEC's OIG recently reviewed the agency's leasing process for Constitution Center, issuing a report on May 16, 2011. The report provides a thorough discussion of the OIG's findings and recommendations, and clearly reveals significant flaws in the process by which SEC leasing decisions were made. As recommended by the OIG, the Chairman directed that I carefully review the report's findings. Based on the findings of the report, we are moving to implement the report's recommendations.

Shortly before receiving the report, the Chairman reassigned to me the authority to oversee the OAS. In addition, the Chairman submitted a reprogramming request to the House and Senate Appropriations Committees requesting approval to formally reorganize the SEC to reflect this transfer of authority for overseeing OAS operations. Additionally, the agency has taken, or is in the process of taking, a number of other steps to improve our leasing program and enhance the governance of leasing operations, including:

- Conducting a comprehensive assessment of OAS operations. The SEC is in the process of retaining the assistance of outside experts to conduct a comprehensive assessment of our entire OAS organization, with specific focus on the real property leasing and acquisitions programs. The assessment will examine:

- OAS's organizational structure, including decision-making processes, reporting relationships, quality controls, and staffing levels;
- workforce knowledge, skills, and abilities;
- business processes to identify improvement opportunities, including efficiency, cost reduction, and internal controls;
- policies and procedures to ensure compliance with regulatory requirements and identify risks or impediments to optimal performance; and
- real estate and leasing governance structures to ensure strict compliance and quality controls and ensure appropriate decision-making and approval authorities.

In addition, a risk assessment will be performed to better identify key risks at the operational, process, and activity levels and recommend improvements and cost-beneficial controls. We anticipate that the assessment will be completed by the fall of 2011.

- Requiring future leasing decisions to be approved by the COO. Determinations of where to house agency staff are among the most significant financial decisions the agency makes. To ensure these decisions are fully informed and carefully considered, I have directed that all future real property leasing decisions be submitted and approved by me as COO before any leases are signed.

- Creating a senior executive-level facilities management oversight committee for leasing decisions. Going forward, no leasing obligations will be incurred or recommended for approval without consultation with a senior executive-level facilities management committee we are in the process of creating. This cross-organizational committee will provide oversight and guidance to the SEC leasing process, and will serve as a forum for executive-level discussion of the agency's leasing decisions. In addition, we separately have initiated a review, led by the directors of our national enforcement and examination programs, of the SEC's regional office presence, which will include an assessment of the agency's location strategy and associated office space needs.

- Reducing the square footage allotted to contractors who require office space. Allocation of office space to the SEC's contractors contributes significantly to the agency's overall use of space. Earlier this year, we undertook an effort to re-assess the design and allocation of office space to contractors at the SEC's Washington, D.C. area facilities, and concluded that we could make more economical use of space. We since have taken aggressive action to reduce the square footage allotted to contractors and to consolidate contractor use of space. In some cases, we have assigned five or more contractors to an office that previously might have otherwise been occupied by only one person. These actions have reduced the agency's overall need for space, and have helped free up space for higher priority uses.

- Acquiring a system that automates space planning to enable more strategic occupancy planning and more efficient use of space. With a workforce that includes more than 4,000 staff and contractors spread among 12 major metropolitan areas around the

country, it is essential that we improve our ability to manage and support facilities management throughout its entire lifecycle, from planning to acquisition to operations. To this end, earlier this year the SEC initiated efforts to acquire an integrated workplace management system, *i.e.*, information technology software that will permit us to automate and provide more efficient space planning, move management, and asset management. Such systems, available on an off-the-shelf basis and commonly used in private industry as a best practice, should provide managers with significantly more timely and accurate analysis and planning to deliver efficient space utilization at all office locations.

- Hiring a new Leasing Branch Chief. The Chief of OAS's Real Property and Leasing Branch, the position most directly accountable for procurement and administration of the agency's real property leasing, recently left the SEC. I have made it a top priority to fill this critical position with an experienced realty expert and manager who will work with me to reform and improve the agency's lease-related decision-making process.

- Developing a more clearly defined leasing policy and associated process. We are in the process of developing a new leasing project approval process that will address, among other things:

  - estimation accuracy;
  - the approval process for non-competitive (*i.e.*, sole-source) leasing acquisitions;
  - cost/benefit and business case analysis;
  - authorized funding availability;
  - clear identification of hiring needs with the requisite geographic match; and
  - external government agency requirements.

  We also will develop and use a "rentable square foot" per-employee space standard that is benchmarked to government agencies and private organizations with comparable missions and needs. Additionally, efforts are underway to develop appropriate performance goals and performance metrics for the real property leasing program.

In addition, the OIG report recommends that the agency, upon a careful review of the report's findings and a comprehensive assessment of our OAS operations, consider whether disciplinary action should be taken against certain current staff members. The SEC has begun this review in accordance with federal personnel law. At present, the Office of Human Resources and Office of General Counsel are analyzing the investigative report and record and, if warranted, the Director of the Office of Human Resources will recommend appropriate disciplinary action to me. I would then decide any appropriate disciplinary action that should be taken.

Conclusion

In conclusion, the SEC is actively at work on a number of fronts to strengthen the agency's real property leasing program. Although the SEC has paid no rent on the space and has worked with the landlord to identify substitute tenants, the OIG report identified flaws in the leasing process in need of correction. We are endeavoring to take all necessary and appropriate steps, including implementing new controls and procedures, to ensure that we address the significant issues identified in the OIG's report.

I would be happy to answer any questions you may have.

Written Testimony of H. David Kotz
Inspector General of the
Securities and Exchange Commission

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

Thursday, June 16, 2011
10:00 a.m.

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.

I would like to begin my remarks by briefly discussing the role of my Office and the oversight efforts we have undertaken during the past few years. The mission of the OIG is to promote the integrity, efficiency and effectiveness of the critical programs and operations of the SEC. The SEC OIG includes the positions of the Inspector General, Deputy Inspector General, Counsel to the Inspector General, and has staff in two major areas: Audits and Investigations.

Our audit unit conducts, coordinates, and supervises independent audits and evaluations related to the Commission's internal programs and operations. The primary purpose of conducting an audit is to review past events with a view toward ensuring compliance with applicable laws, rules, and regulations and improving future performance. Upon completion of an audit or evaluation, the OIG issues an independent report that identifies any deficiencies in Commission operations, programs, activities, or functions and makes recommendations for improvements in existing controls and procedures.

The Office's investigations unit responds to allegations of violations of statutes, rules, and regulations, and other misconduct by Commission staff and contractors. We carefully review and analyze the complaints we receive and, if warranted, conduct a preliminary inquiry or full investigation into a matter. The misconduct investigated ranges from fraud and other types of criminal conduct to violations of Commission rules and policies and the Government-wide conduct standards. The investigations unit conducts thorough and independent investigations in accordance with the applicable Quality Standards for Investigations. Where allegations of criminal conduct are involved, we notify and work with the Department of Justice and the Federal Bureau of Investigation, as appropriate.

Audit Reports

Over the past three and one-half years since I became the Inspector General of the SEC, our audit unit has issued numerous reports involving matters critical to SEC programs and operations and the investing public. These reports have included an examination of the Commission's oversight of the Bear Stearns Companies, Inc. and the factors that led to its collapse, an audit of the Division of Enforcement's (Enforcement) practices related to naked short selling complaints and referrals, 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. In addition, in March 2009, we conducted a review of an agency restacking project in which over $3 million was expended to relocate approximately 1,750 SEC

employees in its headquarters building and, in September 2010, we completed an audit of the SEC's real property and leasing procurement process.

Investigative Reports

The Office's investigations unit has conducted numerous comprehensive investigations into significant failures by the SEC in accomplishing its regulatory mission, as well as investigations of allegations of violations of statutes, rules, and regulations, and other misconduct by Commission staff members and contractors. Several of these investigations involved senior-level Commission staff and represent matters of great concern to the Commission, Members of Congress, and the general public. Where appropriate, we have reported evidence of improper conduct and made recommendations for disciplinary actions, including removal of employees from the federal service, as well as recommendations for improvements in agency policies, procedures, and practices.

Specifically, we have issued investigative reports regarding a myriad of allegations, including claims of failures by Enforcement to pursue investigations vigorously or in a timely manner, improper securities trading by Commission employees, conflicts of interest by Commission staff members, post-employment violations, unauthorized disclosure of nonpublic information, procurement violations, preferential treatment given to prominent persons, retaliatory termination, perjury by supervisory Commission attorneys, failure of SEC attorneys to maintain active bar status, falsification of federal documents and compensatory time for travel, abusive conduct, and the misuse of official position and government resources.

In August 2009, we issued a 457-page report of investigation analyzing the reasons why the SEC failed to uncover Bernard Madoff's $50 billion Ponzi scheme. In March 2010, we issued a 151-page report of investigation regarding the history of the SEC's examinations and investigations of Robert Allen Stanford's $8 billion alleged Ponzi scheme. Most recently, on May 16, 2011, we issued a comprehensive and thorough report of investigation 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, which is the subject of this hearing.

Commencement and Conduct of the OIG's Leasing Investigation

On November 16, 2010, the OIG opened our investigation 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.

As part of our investigative efforts, we made numerous requests to the SEC's Office of Information Technology (OIT) for the e-mails of current and former SEC employees for various periods of time pertinent to the investigation. The e-mails were received, loaded onto computers with specialized search tools, and searched on a continuous basis throughout the course of our investigation. In all, OIT provided e-mails for a total of 27 current and former SEC employees for various time periods pertinent to the investigation. We estimate that we obtained and searched over 1.5 million e-mails during the course of the investigation.

We also made several requests to the SEC's Office of Administrative Services (OAS), which oversees the SEC's leasing function, for documents relating to its leasing practices. We carefully reviewed and analyzed the information we received as a result of our document requests. These documents included all records relating to the Constitution Center lease, as well as documents relating to the leasing of additional office space by the SEC for the past several years.

We took the sworn testimony of 18 witnesses in the investigation and interviewed 11 other individuals with knowledge of facts or circumstances surrounding the SEC's leasing activities.

Issuance of Comprehensive Report of Investigation in Leasing Matter

On May 16, 2011, we issued to the Chairman of the SEC a comprehensive report of our investigation in the leasing matter that contained over 90 pages of analysis and more than 150 exhibits. The report of investigation detailed all of the SEC's recent leasing-related decisions and analyzed all of the facts and circumstances that led to the SEC's decision to lease space at Constitution Center.

Results of the OIG's Leasing Investigation

The OIG investigation 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 OIG 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, 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. 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.

The OIG investigation also found that OAS prepared a faulty Justification and Approval document to support entering into the lease for the Constitution Center facility without competition. This Justification and Approval document was prepared after the SEC had already signed the contract to lease the Constitution Center facility. Further, 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. In actuality, the Justification and Approval was not finalized until a month later.

A brief summary of our specific findings is set forth as follows. In 1990, Congress provided the SEC with independent leasing authority, which exempted the SEC from General Services Administration (GSA) regulations and directives. See 15 U.S.C. § 78d(b)(3). The House Conference Report for this legislation expressed the clear intention that "the authority granted the Commission to lease its own office space directly will be exercised vigorously by the Commission to achieve actual cost savings and to increase the Commission's productivity and efficiency." H.R. Conf. Rep. 101-924, 101st Cong, 2d Sess. 1990 at 20.

Subsequent to Congress's granting of independent leasing authority to the SEC, several expensive missteps related to the SEC's leasing actions and management of its

space have occurred. For example, in May 2005, the SEC disclosed to a House Subcommittee that it had identified unbudgeted costs of approximately $48 million attributable to misestimates and omissions of costs associated with the construction of its headquarters facilities near Union Station, known as Station Place One and Two. In 2007, merely a year after moving into its new headquarters, the SEC embarked on a major "restacking" project pursuant to which various SEC employees were shuffled to different office spaces in the same buildings at a cost of over $3 million. An OIG audit of that project found that there was no record of a cost-benefit analysis having been conducted before this undertaking. An OIG survey found that an overwhelming majority of Commission staff affected by the restacking project had been satisfied with the location of their workspace before that project was initiated, and did not believe the project's benefits were worth the cost and time of construction, packing, moving, and unpacking.

The OIG investigation further found that, as a result of a mistaken belief that the SEC would receive significant additional funding, OAS made grandiose plans to lease an upscale facility at Constitution Center. On May 14, 2010, the SEC submitted an authorization request to the Chairman of the U.S. Senate Committee on Banking, Housing, and Urban Affairs, requesting $1.507 billion for Fiscal Year (FY) 2012 to fund an increase of 800 new staff positions. On May 20, 2010, the U.S. Senate passed a version of the financial regulatory reform bill that eventually became Dodd-Frank (the U.S. House of Representatives had passed a version of the legislation on December 11, 2009). The SEC estimated that it would need to add another 800 positions in FY 2011 and FY 2012 to implement Dodd-Frank. After the reconciliation process between the

two versions of the financial regulatory reform bills, Dodd-Frank became law on July 21, 2010.

Authorization of funding for an executive agency like the SEC does not guarantee that the agency will be appropriated the funds. An authorization request is the first step in the SEC's lengthy budget process. Under that process, an authorization request is submitted to Congress in May of the fiscal year two years prior to the fiscal year for which the authorization is requested (*e.g.*, the FY 2012 authorization request takes place in May 2010). The following September, several months after the authorization request is made, the SEC submits a proposed budget request to the Office of Management and Budget (OMB). In November, the next step of the budget request process takes place: OMB replies to the SEC with a "pass-back," and the SEC and OMB then usually negotiate the amount of the budget request. Several months later, the President formally submits a budget proposal to Congress. Once the President makes the budget request to Congress, Congress then begins the decision-making process as to how much money to appropriate to the SEC and other agencies. SEC employees interviewed in connection with the OIG's leasing investigation acknowledged that an authorization may indicate an intention for Congress to provide funding, but circumstances frequently change and, therefore, federal agencies understand that until funds are appropriated, they cannot count on receiving those funds.

Notwithstanding the uncertainty of actually being appropriated the amount requested through the budget process, in May 2010, OAS began planning for an expansion at SEC Headquarters based on the agency's FY 2012 budget request. Initially, the SEC's Associate Executive Director of OAS, Sharon Sheehan, and the former Chief

of OAS's Leasing Branch decided that the agency needed to lease approximately 300,000 square feet of space to accommodate the SEC's needs through FY 2012. As of May 2010, the Chief of the Leasing Branch's plan was to solicit offers from three properties within walking distance of Station Place to meet the SEC's additional space needs. However, on June 2, 2010, the Chief of the Leasing Branch received an e-mail from the real estate broker for a facility at Constitution Center, located on 7th and D Streets, SW, approximately two miles from the SEC's Station Place facility near Union Station, regarding Constitution Center's availability and some of its features.

The 1.4 million square foot Constitution Center had just been renovated in "one of the largest office redevelopment projects in Washington, DC," according to promotional literature. One of the more attractive features of the Constitution Center facility was its 5,000 square foot lobby with spacious accommodations for a guard desk(s), security screening room, shuttle elevator lobby, and display space, as well as Jerusalem limestone floors, marble walls, wood and metal paneling, decorative lighting and a floor-to-ceiling glass wall facing the landscaped courtyard. The facility promised abundant daylighting, panoramic views of the city and surrounding region, and an open plaza area that contained a one-acre private garden.

Almost immediately after being contacted by the broker for Constitution Center, OAS decided to expand the previous delineated locality of consideration to add Constitution Center to the other three buildings that would be included in the solicitation for offers for approximately 300,000 square feet of space.

On June 17, 2010, OAS briefed SEC Chairman Mary Schapiro on its immediate expansion plans at SEC Headquarters. At that briefing, the Chief of the Leasing Branch

informed the Chairman that the SEC needed to lease immediately 280,000 to 315,000 square feet of office space in Washington, D.C., and identified on a map specific locations for that expansion, including Constitution Center. Both Chairman Schapiro and her former Deputy Chief of Staff, Kayla Gillan, recalled the Chairman expressing clear preference for the locations that were within walking distance of Station Place, as opposed to the Constitution Center facility. Chairman Schapiro also questioned whether the SEC needed 300,000 additional square feet, given that she believed the SEC should concentrate its growth in the agency's regional offices.

The OIG investigation found notwithstanding Chairman Schapiro's expressions in mid-June 2010 of her preference for a facility closer to Station Place and her questioning of why the SEC needed as much as 300,000 square feet of space, by mid-July, OAS came back to the Chairman with an urgent recommendation that the SEC immediately lease 900,000 square feet of space with the only available option being the Constitution Center facility. The OIG investigation found that the analysis OAS performed to justify the need for three times its original estimate of necessary square footage, and its determination that the Constitution Center facility was the only available option, was deeply flawed and based on unfounded and unsupportable projections. We found that, as a consequence of its flawed analysis, OAS grossly overestimated the amount of space needed at SEC Headquarters for the SEC's projected expansion.

Specifically, the OIG investigation found that OAS erroneously assumed that all of the new positions projected for FY 2011 and FY 2012 would be allocated to SEC Headquarters and that none of those new positions would be allocated to the SEC's regional offices. This assumption was contrary to the position the Chairman had

communicated to OAS at the June 17, 2010 meeting that as much as possible of the SEC's future growth should occur in the regional offices, not at Headquarters. We found that although the need for a calculation reflecting the allocation of a number of the new positions to the regions was discussed, none was ever prepared. Sheehan testified that "OAS had difficulty getting the breakout," and acknowledged that, assuming all of the new positions would be located at Headquarters would "inflate the number."

We also found that OAS conducted its analysis of the SEC's space needs by using a standard of 400 square feet per person when calculating how much space would be needed for the additional positions it believed it would gain as a result of Dodd-Frank and associated increases in the SEC's budget. A Realty Specialist in OAS explained to the OIG that the Chief of the Leasing Branch and she developed the 400 square feet standard by dividing the square footage of office space by the number of people the SEC had authority to hire for the offices in that space at Headquarters and several of the SEC's regional offices. The Realty Specialist described the standard as a "WAG" (wild-assed guess) and a "back of the envelope" calculation, and acknowledged in her OIG testimony that OAS "didn't do this scientifically." OAS's 400 square feet per-person standard was an "all-inclusive number" that included common spaces and amenities. It also included an additional 10 percent for contractors, 10 percent for interns and temporary staff, and five percent for future growth. Notwithstanding this "all-inclusive" number, we found that when OAS later performed its calculations to justify the Constitution Center lease, it added even more unnecessary space by double-counting contractors, interns and temporary staff and by improperly incorporating future growth into the projections of

space needed. We also found that each one of these estimates was wildly inflated and unsupported by the data OAS was using.

The OIG investigation found that the OAS inflated its estimate of new positions that would require space by including an estimate of the number of contractors who would be hired in addition to the number of SEC employees. In early June 2010, OAS Associate Executive Director Sheehan asked the OAS Branch Chief for Space Management & Mail Operations to obtain information about the number of contractors in the agency. On June 12, 2010, the Branch Chief reported back, "Right now, based on the Contractor numbers I have at [Station Place], I can justify us using a 10%, Contractor to Position, factor." The Branch Chief later learned that OAS needed the numbers to be larger. He testified as follows regarding his understanding of why the Chief of the Leasing Branch needed the number to be larger: "[W]hat I understand she was trying to do was to make sure that whatever size lease she entered into was enough to meet our needs. And I think that in this case, if we were going to take the whole building, the numbers needed to be larger." Ultimately, OAS ignored the data that had been gathered during the first two weeks of June 2010, which indicated the correct contractor ratio was 10 percent, and inflated its calculation of space by adding contractors using a completely arbitrary 20 percent ratio.

In addition, we found that OAS's estimate of new positions that would need space included an estimate of the number of interns and temporary staff who would be hired, in addition to new employees. OAS's estimate of interns and temporary staff to be hired assumed a ratio of 16.5 percent (9 percent for interns and 7.5 percent for temporary staff). However, the OIG found that OAS's estimate of intern and temporary staff positions was

significantly higher than the estimate in the data it had received. On July 16, 2010, a management program analyst in the SEC's Office of Human Resources provided OAS with "the [peak] numbers [for interns and temporary staff]," which ranged from approximately 4 to 7 percent for the six fiscal years of data analyzed.

Further, the OIG investigation found that OAS's calculations increased the amount of space required for every person to be hired in FY 2011 and FY 2012 by 10 percent for "inventory" representing "vacant offices you have for expansion and unanticipated growth, that kind of thing," according to an OAS Assistant Director. However, as was the case with the estimate for contractors, temporary staff and interns, an inventory factor had already been incorporated into the calculation of the 400 square foot standard. Moreover, the 10 percent inventory factor added was double the 5 percent factor previously determined to be appropriate.

We also found that OAS's estimate of new positions that would need space included an assumption not only about FY 2011 and FY 2012, but also reflected an assumption that, in FY 2013, Congress would increase the SEC's appropriation by 50 percent of the assumed FY 2012 increase. We found that the assumption of 50 percent growth in 2013 was arbitrary and unsupported. Based on the assumed FY 2013 growth, OAS calculated that the SEC would add another 295 positions in that year and again assumed that all of those positions would be allocated to SEC Headquarters. We found that this estimate was not based upon any firm numbers or projections and was contrary to the SEC's planning and budget process, which does not project growth more than two years into the future.

The OIG investigation found that OAS used the above-described overinflated estimates to calculate a space need of 934,000 square feet. On Friday, July 23, 2010, Executive Director Diego Ruiz met with Chairman Schapiro, Chief of Staff Didem Nisanci, and then-Deputy Chief of Staff Gillan to recommend that the SEC lease 900,000 square feet of space at Constitution Center. Gillan recalled the July 23, 2010 meeting with Ruiz, and stated that Ruiz had come to her "and said that he needed to see Mary [Schapiro] quickly because he needed to make a quick decision on Constitution Center. That the other possible space opportunities had evaporated, gone to others, were no longer available. And that this one was really all that was left and that we needed to act quickly."

Chairman Schapiro testified as follows regarding the July 23rd meeting with Ruiz:

> I remember explicitly being told there really wasn't any other space available that could fulfill our needs and that there was a time – a sense of we were about to lose this. We had lost other space that we had apparently indicated an interest in and that we were about to lose this. So there was a sense of urgency on their part.

Gillan testified that Ruiz did not explain in the July 23, 2010 meeting, or at any other time, that the assertion that SEC Headquarters needed an additional 900,000 square feet was predicated, in part, on the assumption that all of the agency's new positions in FY 2011 and FY 2012 would be allocated to Headquarters. Gillan testified, "[I]n fact, that's inconsistent with what I had understood, because … [Chairman Schapiro] specifically said that, to the extent possible, she wanted new hires to go to the regions." Gillan also testified that Ruiz did not explain in the July 23, 2010 meeting, or at any other time, that the assertion that SEC Headquarters needed an additional 900,000 square feet was predicated, in part, on OAS's projections of significant growth in FY 2013.

On July 23, 2010, Ruiz sent an e-mail to Sheehan and others stating, "Met with Chairman this morning, and we have her approval to move forward." The OIG investigation found that the SEC negotiated the contract for 900,000 square feet at Constitution Center in three business days, signing the contract on July 28, 2010. On July 27, 2010, the SEC staff involved in that negotiation discussed the fact that they had "no bargaining power" because "Sharon [Sheehan] wants this signed tomorrow." Internal e-mails show that OAS feared losing the building to the National Aeronautics and Space Administration, which had also expressed an interest in the facility.

On July 28, 2010, the SEC executed a Letter Contract committing the SEC to lease approximately 900,000 square feet of space at Constitution Center. The contract established a multiphase delivery schedule, in which Phase 1, approximately 350,000 square feet, would be delivered no later than September 2011, and Phase 2, approximately 550,000 square feet, would be delivered no later than September 2012. The contract stated that "the SEC's interests require that [the owner] be given a binding commitment so that the space required will be committed to the SEC and initial build out for the Phase 1 space can commence immediately ...." The lease term in the contract was ten years. The Chief of the Leasing Branch estimated the costs associated with the SEC's leasing and occupying Constitution Center would be $556,811,589.

The Letter Contract also granted the SEC the right of first refusal for the remaining approximately 500,000 square feet of space at Constitution Center until December 15, 2010. If the SEC had exercised this option, it would have leased the entire 1.4 million square feet of space at Constitution Center. The Chief of the Leasing Branch testified that OAS wanted a right of first refusal on all of the remaining space at

Constitution Center "because the Congress was throwing money at us" and "Sharon [Sheehan] was always hoping that we wouldn't have anybody else in the building. That we would be able to ultimately justify the need for the whole building or something."

After the SEC committed itself to the ten-year lease term at a cost of $556,811,589, it entered into a Justification and Approval for Other than Full and Open Competition, which is required by the Federal Acquisition Regulation (FAR) when an agency decides not to allow for full and open competition on a procurement or lease. The FAR permits other than full and open competition "when the agency's need for the supplies or services is of such an unusual and compelling urgency that the Government would be **seriously injured** unless the agency is permitted to limit the number of sources from which it solicits bids or proposals." 48 C.F.R. § 6.302-2 (emphasis added).

The OIG investigation found that the Justification and Approval to lease space at Constitution Center without competition was inadequate, not properly reviewed, and backdated. The Justification and Approval provided as follows:

> To fulfill these new responsibilities it is necessary to significantly increase full-time staff and supporting contractors by approximately 2,335 personnel to be located at the SEC's headquarters in Washington, DC. However, the SEC's current headquarters is full. Accordingly the SEC has a requirement of an unusual and compelling urgency to obtain approximately 900,000 rentable square feet (r.s.f.) of additional headquarters space in the Washington, D.C. Central Business District, as this is the amount of space required to accommodate the approximately 2,335 new staff and contractors in headquarters.

The Justification and Approval asserted that the 900,000 square feet "must be in a single building or integrated facility to support the SEC's functional requirements and operational efficiency."

An OAS Management and Program Analyst signed the Justification and Approval as the SEC's Competition Advocate. She testified that she did not take any steps to verify that the information in the Justification and Approval was accurate, "[o]ther than asking the contracting officer, you know, just general questions, 'Is this indeed urgent and compelling[?].'" She further testified that when she signed the Justification and Approval, she was not aware that funding for the projected growth had not been appropriated. She also did not have an understanding of when the projected 2,335 personnel were expected to be hired. Further, she acknowledged in testimony that the SEC would, in fact, not be "seriously injured" if it lost the opportunity to rent one contiguous building and had to rent multiple buildings to fill its space needs.

The FAR also requires that a Justification and Approval for Other than Full and Open Competition be posted publicly "within 30 days after contract award." The Letter Contract was signed on July 28, 2010. Accordingly, the deadline for publication of the Justification and Approval was August 27, 2010. On September 3, 2010, the SEC publicly posted the Justification and Approval on the Federal Business Opportunities website. The document was signed by four individuals, with all four signatures dated August 2, 2010.

However, the OIG investigation found that the Justification and Approval was not finalized until September 2, 2010, and substantial revisions were being made up to that date. We found that three of the four signatories executed the signature page on August

2, 2010, before a draft even remotely close to the final version existed. The OIG found that the SEC's Competition Advocate executed the signature page on August 31, 2010, and initially backdated her signature to August 27, 2010, but subsequently whited-out the "7" on the date to make it appear that she also had signed the document on August 2, 2010. The actions of the signatories to the Justification and Approval gave the public the false impression that the document was finalized a few days after the Letter Contract was signed, and there was only a delay in its publication.

The OIG investigation also found that there is significant uncertainty among the SEC staff regarding important requirements in connection with government leasing and there are serious questions as to whether the SEC complied with several of those requirements in connection with its leasing of Constitution Center. Appendix B of OMB Circular No. A-11 states, "Agencies are required to submit to OMB representatives the following types of leasing and other non-routine financing proposals for review of the scoring impact: Any proposed lease of a capital asset where total Government payments over the full term of the lease would exceed $50 million." Although the evidence showed the SEC initially contemplated providing OMB with the written notification and senior agency officials believed that OMB had been formally notified, no written notification to OMB was provided.

In addition, we found that there is a possibility that the SEC violated the Antideficiency Act in connection with its lease of Constitution Center. The Antideficiency Act prohibits officers or employees of the government from involving the government "in a contract or obligation for the payment of money before an appropriation is made unless authorized by law." 31 U.S.C. § 1341(a)(1)(B). The

incurring of an obligation in excess or advance of appropriations violates the Antideficiency Act. Notwithstanding its July 28, 2010 commitment to a ten-year lease at Constitution Center, the SEC did not obligate the entire amount of rent payments due under the lease. Although the SEC has been granted independent leasing authority statutorily and is generally granted authority to enter into multiyear leases in its annual appropriations, the U.S. Government Accountability Office (GAO) has found that "[t]he existence of multiyear leasing authority by itself does not necessarily tell [an agency] how to record obligations under a lease." GAO has distinguished agencies that have "specific statutory direction" to obligate funds for multiyear leases one year a time, such as the GSA, from agencies such as the Federal Emergency Management Agency (FEMA), which do not have such explicit direction. Because the SEC, like FEMA, does not have specific statutory direction to obligate funds for its multiyear leases on an annual basis, its lease obligations may have to be obligated in their entirety at the time they are incurred. Thus, SEC may have violated the Antideficiency Act in connection with its commitment to lease space at Constitution Center.

In early October 2010, the SEC informed the owner of the building that it could not use approximately 600,000 of the 900,000 square feet of space it had contracted for at Constitution Center and asked for the owner's assistance in finding other tenants for that space. In November 2010, the owner of the building began negotiations with the Federal Housing Finance Agency (FHFA) and the Office of the Comptroller of the Currency (OCC) to lease portions of Constitution Center. In January 2011, OCC and FHFA entered into contracts for space at Constitution Center, leaving approximately 350,000 square feet to which the SEC remains committed. On January 18, 2011, counsel for the

building owner sent a demand letter to the SEC, asserting that the SEC's actions had caused him to incur $93,979,493 in costs at Constitution Center.

The OIG investigation further found that a "closed" and "rigid" atmosphere within OAS may have contributed to the irresponsible decisions made with respect to the Constitution Center lease. In the course of this OIG investigation, several witnesses who sought to remain anonymous came forward to the OIG to provide information concerning the environment and the decision-making processes within OAS. These witnesses described an environment in which inexperienced senior management make unwise decisions without any input from employees who have significant knowledge and experience. We found that questioning of upper management decisions by the staff is "not allowed" and that OAS Executive Director Sheehan surrounds herself with "yes-men" and "does not want to hear what [experienced staff] will tell her." These individuals testified that upon learning of the SEC's decision to lease 900,000 square feet of space at Constitution Center, they "just couldn't understand how [OAS] could justify that amount of space ..." and were "flabbergasted" by the decisions. One experienced employee testified that OAS management had "grandiose plans" and was significantly influenced by the upscale nature of the facility.

Recommendations of the OIG's Report of Investigation

We provided our Report of Investigation to the SEC with the recommendation that the newly-appointed Chief Operating Officer/Executive Director carefully review the report's findings and conduct a thorough and comprehensive review and assessment of all matters currently under the purview of OAS. We further recommend that the Chief Operating Officer/Executive Director, upon conclusion of such review and assessment,

determine the appropriate disciplinary and/or performance-based action to be taken for matters that relate to subject of the report of investigation, including, at a minimum, consideration of disciplinary action against two individuals, up to and including dismissal, and consideration of disciplinary action against a third individual.

We also recommended that the SEC 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.

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.

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.

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