U.S. SECURITIES AND EXCHANGE COMMISSION

Agency Financial Report

FISCAL YEAR 2017

PROTECTING INVESTORS

MAINTAINING FAIR, ORDERLY, AND EFFICIENT MARKETS

FACILITATING CAPITAL FORMATION

MESSAGE FROM THE CHAIRMAN

Since joining the U.S. Securities and Exchange Commission (SEC) in May 2017, I've seen first-hand the commitment and dedication of the agency's 4,600 employees to carry out our important three-part mission—to protect investors, maintain fair, orderly, and efficient markets, and facilitate capital formation. Through their efforts, the SEC serves the American public and seeks to sustain our nation's continuing prosperity and importance in an ever-changing, interconnected global economy.

The Agency Financial Report describes the SEC's results over the past fiscal year. It presents the agency's financial statements, and provides the opinion of our independent auditor, the Government Accountability Office, with respect to the financial statements and the effectiveness of our internal control systems. The report also includes the perspective of the SEC's Inspector General on the agency's key management and performance challenges, and reports on our plans for meeting these and other emerging challenges in the years ahead.

I am pleased to report that, while global competition and the fast-moving pace of technology present new challenges to effective oversight and enforcement, the SEC is facing those challenges head on. We are committed to leveraging our precious resources efficiently and effectively. In doing so, we will endeavor to increase opportunities for Main Street investors and entrepreneurs in their pursuit of financial security and their share of the American dream.

JAY CLAYTON
Chairman
November 13, 2017

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AGA

Certificate of Excellence in Accountability Reporting®

presented to the

U.S. Securities and Exchange Commission

in recognition of outstanding effort in preparing the Agency Financial Report for the fiscal year ending September 30, 2016.

Diane L. Dudley, CGFM, CPA
Chair, CAFR Board

Ann M. Ellerson, MS, PMP
Chief Executive Officer, AGA

CERTIFICATE OF EXCELLENCE IN ACCOUNTABILITY REPORTING

The SEC's Fiscal Year 2016 Agency Financial Report received the Certificate of Excellence in Accountability Reporting from the Association of Government Accountants. This was the 11th year in a row that the SEC has won this award, which is presented to federal government agencies whose annual reports achieve the highest standards in demonstrating accountability and communicating results.

INTRODUCTION

Each Fiscal Year (FY), the SEC publishes an Agency Financial Report (AFR) that provides detailed financial performance results. The information presented in the FY 2017 AFR enables the President, Congress, and the public to assess the agency's accomplishments and understand its financial and operational picture. This report also satisfies the requirements contained in the Office of Management and Budget (OMB) Circular A-136, *Financial Reporting Requirements*.

The agency is producing an AFR that primarily focuses on financial results and an Annual Performance Report (APR) that provides a more in-depth review of strategic goals and performance results in lieu of a combined Performance and Accountability Report. The FY 2017 APR will be included in the FY 2019 Congressional Budget Justification Report available in 2018 at www.sec.gov/about/secreports.shtml.

This report contains three main sections and supplemental appendices.

Management's Discussion and Analysis

Provides a high-level overview of the SEC—its history, mission, and organizational structure—and the agency's FY 2017 overall performance as related to its strategic goals and primary objectives. Also in this section are management's assurances on internal controls and the agency's forward-looking information.

Financial Section

Contains audited financial statements, accompanying notes, and required supplementary information, as well as the independent auditor's report on these statements and management's response to that report. Also included are comparative financial statements and accompanying notes for the Investor Protection Fund.

Other Information

Details the agency's compliance with, and commitment to, specific regulations. Included in this section are performance and management analyses and recommendations from the Office of Inspector General and the SEC's response to that information in accordance with the Reports Consolidation Act of 2000; a detailed explanation of any significant erroneous payments and overpayments recaptured as required by the Improper Payments Information Act of 2002, as amended; and a table displaying recent inflationary adjustments made to civil monetary penalties in accordance with the Federal Civil Penalties Inflation Adjustment Act of 1990, as amended.

Appendices

Offers additional resources related to the agency and this report: a glossary of terms, frequently used acronyms and abbreviations, biographies, and contact information.

Electronic copies of this AFR and prior year reports are available at www.sec.gov/about/secreports.shtml.

IN GOD WE TRUST
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MANAGEMENT'S DISCUSSION AND ANALYSIS

This section provides a high-level overview of the agency and its FY 2017 program and financial performance.

About Us

Mission, Vision, Values, and Goals
Explains the SEC's mission, vision, values, and four strategic goals, as set forth in the agency's strategic plan.

History and Purpose
Provides background on the SEC and its responsibility to oversee the nation's securities markets and certain primary participants.

Organizational Structure and Resources
Lists the SEC's office locations, organizational structure, employment statistics, and summarizes the 10 major programs by responsible divisions and offices.

Year in Review
Summarizes efforts made by the SEC in pursuit of its strategic goals in FY 2017.

Looking Forward
Details specific actions on which the SEC will continue to focus as part of its regulatory and oversight responsibilities.

Financial Highlights
Provides an overview of the SEC's financial information, including an analysis of the financial data presented in the audited financial statements, the limitations of the financial statements, and the sources and uses of the SEC's funds.

Performance Highlights
Explains the SEC's strategic and performance planning framework, discusses the process used to verify and validate the performance results contained in the AFR, displays FY 2017 operating costs by strategic goal, summarizes FY 2017 performance results by strategic goal, and highlights key performance accomplishments.

Management Assurances and Compliance with Other Laws
Provides management's assessment and assurances on the SEC's internal controls under the Federal Managers' Financial Integrity Act of 1982, and on the compliance of the SEC's financial systems with federal requirements under the Federal Financial Management Improvement Act of 1996. This section also addresses the SEC's compliance with the Federal Information Security Management Act of 2002 and other laws and regulations.

ABOUT US

Mission

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

Vision

The SEC strives to promote a securities market that is worthy of the public's trust and characterized by:

- Transparent disclosure to investors of the risks of particular investments;
- Oversight of key market participants, including exchanges, brokers and dealers, investment advisers, and others;
- Focus on strengthening market structure and systems;
- Promotion of disclosure of market-related information;
- Protection against fraud and abuse; and
- Evaluation, development, and maintenance of appropriate rules and regulations.

Values

Integrity: As the SEC is the independent federal agency entrusted with regulating and conducting enforcement for the U.S. securities markets, each member of the Commission's workforce has a responsibility to demonstrate the highest ethical standards to inspire confidence and trust.

Excellence: The SEC is committed to the highest standards of excellence in pursuit of its mission. The investing public and the U.S. securities markets deserve nothing less.

Accountability: The SEC embraces the responsibility with which it is charged. In carrying out its mission, SEC employees hold themselves accountable to the public and take responsibility for achieving the goals of the SEC.

Effectiveness: The SEC strives to work creatively, proactively, and effectively in assessing and addressing risks to the securities markets, the public, and other market participants. The staff is committed to finding innovative and flexible approaches to the SEC's work and using independent judgment to explore new ways to fulfill the SEC's mission in the most efficient and effective manner possible.

Teamwork: The SEC recognizes that its success depends on a diverse, coordinated team committed to the highest standards of trust, hard work, cooperation, and communication. The staff is committed to working together and coordinating effectively with investors, business, governments, and other organizations in the U.S. and abroad.

Fairness: The SEC treats investors, market participants, and others fairly and in accordance with the law. As an employer, the SEC seeks to hire and to retain a skilled and diverse workforce, and to ensure that all decisions affecting employees and applicants are fair and ethical.

Strategic Goals and Strategic Objectives

Strategic Goal 1: Establish and maintain an effective regulatory environment

Strategic Objective 1.1: The SEC establishes and maintains a regulatory environment that promotes high-quality disclosure, financial reporting, and governance, and that prevents abusive practices by registrants, financial intermediaries, and other market participants.

Strategic Objective 1.2: The SEC promotes capital markets that operate in a fair, efficient, transparent, and competitive manner, fostering capital formation and useful innovation.

Strategic Objective 1.3: The SEC adopts and administers regulations and rules that are informed by robust economic analysis and public comment and that enable market participants to understand clearly their obligations under the securities laws.

Strategic Objective 1.4: The SEC engages with a multitude of stakeholders to inform and enhance regulatory activities domestically and internationally.

Strategic Goal 2: Foster and enforce compliance with the federal securities laws

Strategic Objective 2.1: The SEC fosters compliance with the federal securities laws.

Strategic Objective 2.2: The SEC promptly detects and deters violations of the federal securities laws.

Strategic Objective 2.3: The SEC prosecutes violations of federal securities laws and holds violators accountable through appropriate sanctions and remedies.

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

Strategic Objective 3.1: The SEC works to ensure that investors have access to high-quality disclosure materials that facilitate informed investment decision-making.

Strategic Objective 3.2: The SEC works to understand investor needs and educate investors so they are better prepared to make informed investment decisions.

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

Strategic Objective 4.1: The SEC promotes a results-oriented work environment that attracts, engages, and retains a technically proficient and diverse workforce, including leaders who provide motivation and strategic direction.

Strategic Objective 4.2: The SEC encourages a collaborative environment across divisions and offices and leverages technology and data to fulfill its mission more effectively and efficiently.

Strategic Objective 4.3: The SEC maximizes the use of agency resources by continually improving agency operations and bolstering internal controls.

History

During the peak of the Great Depression, Congress passed the Securities Act of 1933[1] (Securities Act) and the Securities Exchange Act of 1934[2] (Securities Exchange Act), which established the SEC.

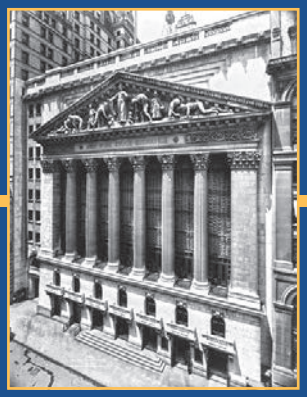
> We have sought to put forward the rule of fair play in finance and industry.
>
> —Former President Franklin D. Roosevelt during a speech to Congress two days after signing the Securities Exchange Act of 1934

These laws were designed to regulate the financial markets and restore investor confidence in U.S. capital markets by providing investors and the markets with reliable information and clear rules to ensure honest dealings. The main purpose of these laws was to ensure the following:

- Companies that publicly offer securities for investment dollars are forthcoming and transparent about their businesses, the securities they are selling, and the risks involved with investing; and
- People who sell and trade securities—brokers, dealers, and exchanges—treat investors fairly and honestly.

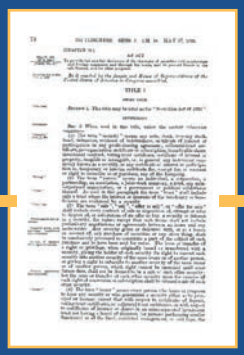
THE ORIGIN OF THE SEC

MAY 17, 1792
A group of stockbrokers and merchants sign the Buttonwood Agreement, which creates the New York Stock & Exchange Board.



APRIL 22, 1903
The New York Stock Exchange floor opens at 18 Broad Street.

OCTOBER 29, 1929
The stock market crashes, launching the Great Depression.



MAY 27, 1933
Congress approves the Securities Act of 1933, the first federal law to regulate the issuance of securities.

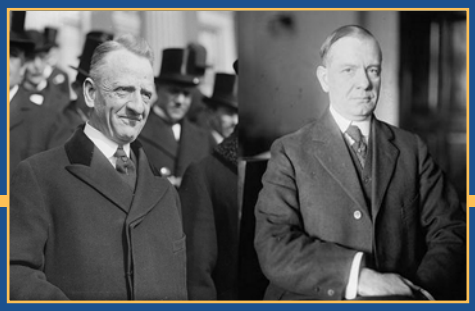
Purpose

The SEC is responsible for overseeing the nation's securities markets and certain primary participants, including broker-dealers, investment companies, investment advisers, clearing agencies, transfer agents, credit rating agencies, and securities exchanges, as well as organizations such as the Financial Industry Regulatory Authority, Municipal Securities Rulemaking Board, and the Public Company Accounting Oversight Board. Under the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010[3] (Dodd-Frank Act), the agency's jurisdiction was expanded to include certain participants in the derivatives markets, private fund advisers, and municipal advisors.

Each year, the SEC brings hundreds of civil enforcement actions against individuals and companies for violation of securities laws. Examples of infractions are insider trading, accounting fraud, market manipulation, and providing false or misleading information about securities and/or the issuing companies.

1 More information about the Securities Act of 1933 can be found at www.sec.gov/about/laws/sa33.pdf
2 More information about the Securities Exchange Act of 1934 can be found at www.sec.gov/about/laws/sea34.pdf
3 More information about the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 can be found at www.sec.gov/about/laws/wallstreetreform-cpa.pdf

JUNE 16, 1933
Congress approves the U.S. Banking Act of 1933 (or Glass-Steagall Act), which limits affiliations between banks and securities firms and establishes the FDIC.



Sen. Carter Glass (D–Va.) and Rep. Henry B. Steagall (D–Ala.), the co-sponsors of the Glass–Steagall Act

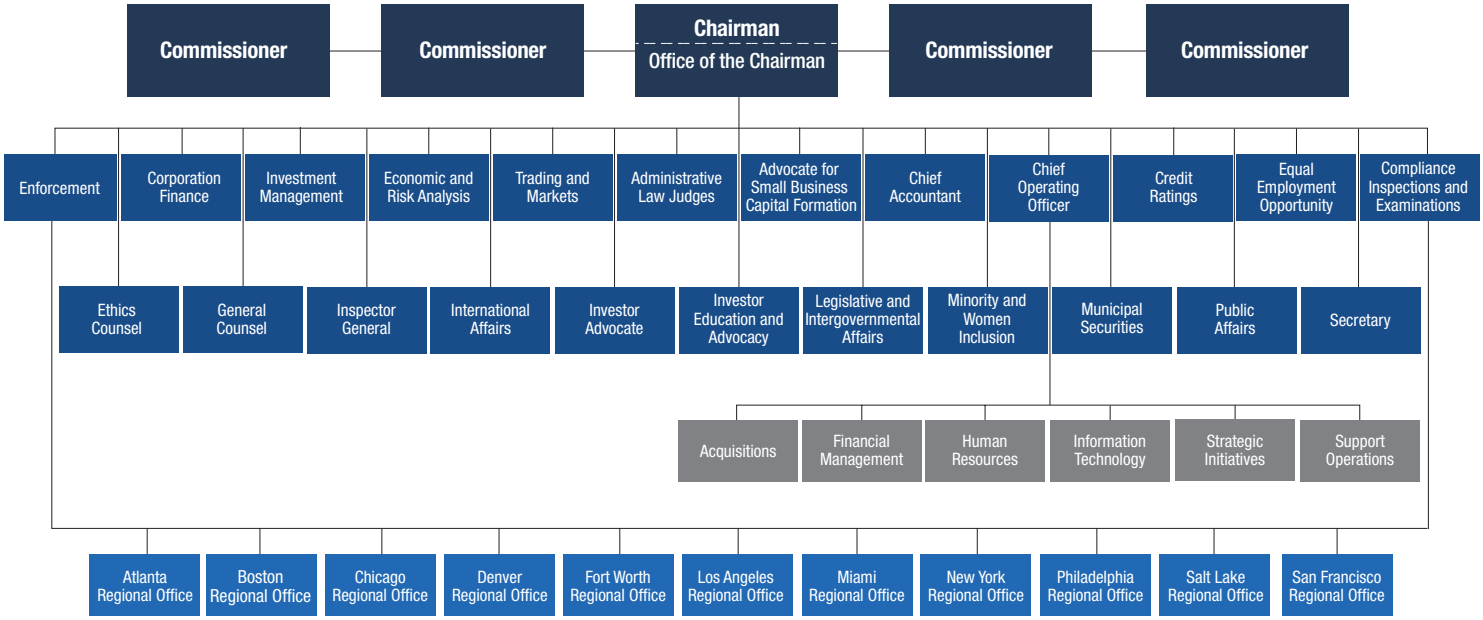
JUNE 1934
President Roosevelt appoints the inaugural Commission of the SEC, naming Joseph P. Kennedy as the agency's first Chairman.

(clockwise from top left) George C. Mathews, Robert E. Healy, James M. Landis, Joseph P. Kennedy, and Ferdinand Pecora

JUNE 6, 1934
Congress approves the Securities Exchange Act of 1934. The SEC is established to enforce and regulate this legislation.

Image credit: SEC Historical Society (www.sechistorical.org)

Chart 1.1 | SEC Organization Chart



Organizational Structure

The SEC is an independent federal agency led by a bipartisan, five-member Commission—one of whom is designated as the Chairman—with staggered five-year terms. As of September 30, 2017, there were two vacant Commissioner positions.

Each member of the Commission is appointed by the President and confirmed by the Senate (see *Appendix A: Chairman and Commissioner Biographies*). The Chairman serves as the chief executive and by law, no more than three of the Commissioners may belong to the same political party.

The Commission convenes on a regular basis, and meetings are open to the public and the news media unless the discussion pertains to a confidential subject, such as whether to begin an enforcement investigation.

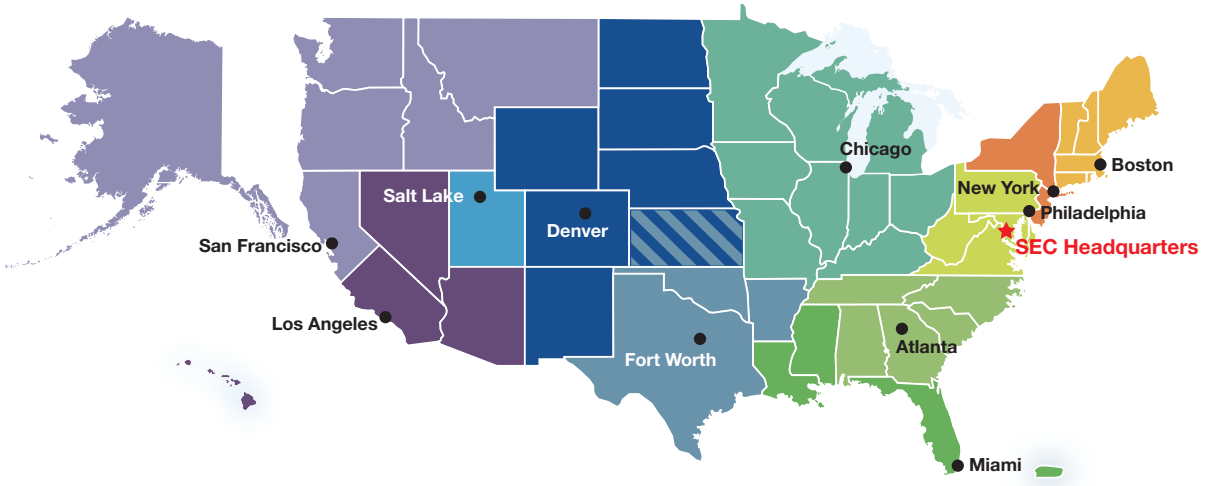
The agency's functional responsibilities are organized into five divisions and 25 offices. In FY 2017, the SEC employed 4,794 full-time equivalents (FTE), including 4,672 permanent and 122 other than permanent FTEs.

The organization chart above is accurate as of September 30, 2017.

Office Locations

The SEC's headquarters are in Washington, DC, and the agency has 11 regional offices located throughout the country. The regional offices are responsible for investigating and litigating potential violations of the securities laws. The regional offices also have enforcement and examination staff to inspect regulated entities such as investment advisers, investment companies, and broker-dealers. The following chart illustrates the locations of, and specific areas within, each of the regional offices.

Chart 1.2 | SEC Headquarters and Regional Office Locations



- ★ **SEC Headquarters**
- **Atlanta Regional Office**
  Georgia, North Carolina, South Carolina, Tennessee, Alabama
- **Boston Regional Office**
  Connecticut, Maine, Massachusetts, New Hampshire, Vermont, Rhode Island
- **Chicago Regional Office**
  Illinois, Indiana, Iowa, Kentucky, Michigan, Minnesota, Missouri, Ohio, Wisconsin
- **Denver Regional Office**
  Colorado, Kansas, Nebraska, New Mexico, North Dakota, South Dakota, Wyoming
- **Fort Worth Regional Office**
  Texas, Oklahoma, Arkansas, Kansas (except for the exam program which is administered by the Denver Regional Office)
- **Los Angeles Regional Office**
  Arizona, Hawaii, Guam, Nevada, Southern California (zip codes 93599 and below, except for 93200-93299)
- **Miami Regional Office**
  Florida, Mississippi, Louisiana, U.S. Virgin Islands, Puerto Rico
- **New York Regional Office**
  New York, New Jersey
- **Philadelphia Regional Office**
  Delaware, Maryland, Pennsylvania, Virginia, West Virginia, District of Columbia
- **Salt Lake Regional Office**
  Utah
- **San Francisco Regional Office**
  Washington, Oregon, Alaska, Montana, Idaho, Northern California (zip codes 93600 and up, plus 93200-93299)

SEC Programs

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

Table 1.1 | SEC Programs and Program Descriptions

ENFORCEMENT	
Division of Enforcement	Investigates and brings civil charges in federal district court or in administrative proceedings based on violations of the federal securities laws. An integral part of this program's function is seeking penalties and the disgorgement of ill-gotten gains in order to return funds to harmed investors. Also within this program is the Office of the Whistleblower, which rewards individuals who provide the agency with tips that lead to successful enforcement actions.
COMPLIANCE INSPECTIONS AND EXAMINATIONS	
Office of Compliance Inspections and Examinations	Conducts examinations of registrants such as investment advisers, investment companies, broker-dealers, self-regulatory organizations (SRO), transfer agents, and clearing agencies.
CORPORATION FINANCE	
Division of Corporation Finance	Helps investors gain access to materially complete and accurate information about companies and the securities they offer and sell, to facilitate capital formation and to deter fraud and misrepresentation in the public offering, trading, voting, and tendering of securities.
TRADING AND MARKETS	
Division of Trading and Markets	Supervises major market participants and conducts activities to maintain fair, orderly, and efficient standards that foster investor protection and confidence in the markets.
INVESTMENT MANAGEMENT	
Division of Investment Management	Seeks to minimize the financial risks to investors from fraud, mismanagement, self-dealing, and misleading or incomplete disclosure in the investment company and investment adviser segments of the financial services industry.
ECONOMIC AND RISK ANALYSIS	
Division of Economic and Risk Analysis	Provides economic analyses as part of the Commission's rulemaking process and supports its rule review, examination, and enforcement programs with data-driven, risk-based analytical methods.
GENERAL COUNSEL	
Office of the General Counsel	Serves as the chief legal officer of the Commission and provides independent legal analysis and advice to the Chairman, Commissioners, and operating divisions on all aspects of Commission activities. This office also defends the Commission in federal district courts.

Table 1.1 | *Continued from previous page*

OTHER PROGRAM OFFICES	
Office of the Chief Accountant	Establishes accounting and auditing policies, and works to improve the professional performance of public company auditors to ensure that financial statements used for investment decisions are presented fairly and have credibility.
Office of Investor Education and Advocacy	Serves investors who complain to the SEC about investment fraud or the mishandling of their investments by securities professionals; ensures the views of retail investors inform the Commission's regulatory policies and disclosure programs; and works to improve investors' financial literacy.
Office of International Affairs	Advances international regulatory, supervisory, and enforcement cooperation; promotes converged high regulatory standards worldwide; and facilitates technical assistance programs in foreign countries.
Office of Administrative Law Judges	Conducts public hearings throughout the United States in a manner similar to non-jury trials in the federal district courts. As independent adjudicators, administrative law judges issue initial decisions on allegations set out in Commission Orders Instituting Proceedings, issue subpoenas, hold prehearing conferences, and rule on motions and the admissibility of evidence.
Office of the Investor Advocate	Helps investors resolve significant problems with the SEC or with SROs, and identifies areas in which investors would benefit from changes to federal laws or to SEC regulations or SRO rules.
Office of Credit Ratings	Administers the rules of the Commission with respect to the practices of nationally recognized statistical rating organizations (NRSRO) in determining ratings; protects the users of credit ratings; promotes accuracy in credit ratings issued by NRSROs; and ensures that such ratings are not unduly influenced by conflicts of interest.
Office of Municipal Securities	Oversees the municipal securities market and administers the agency's rules pertaining to municipal securities brokers and dealers, advisors, investors, and issuers. This office also coordinates with the Municipal Securities Rulemaking Board on rulemaking and enforcement actions.
Office of the Advocate for Small Business Capital Formation	Helps small businesses and investors resolve significant problems incurred with the SEC or SROs, and analyzes the potential impact of current and proposed regulations.
AGENCY DIRECTION AND ADMINISTRATIVE SUPPORT	
Office of the Chairman	Oversees all aspects of agency operations. The Chairman and Commissioners are responsible for reviewing and approving enforcement cases and formal orders of investigation, as well as overseeing the development, consideration, and execution of policies and rules.
Office of Legislative and Intergovernmental Affairs	Serves as the liaison between the SEC and Congress, and is responsible for responding to requests from Congress for information related to agency programs and legislation affecting the SEC or its mission.
Office of the Chief Operating Officer	Provides strategic leadership and operational oversight of the SEC's core mission support activities and compliance with administrative requirements from Congress and the Executive Branch.
Office of the Ethics Counsel	Administers the Commission's Ethics Program and interprets the SEC's Supplemental Ethics Rules as well as government-wide ethics laws, rules, and regulations.
Office of Minority and Women Inclusion	Develops standards for all agency matters relating to diversity in management, employment, and business activities.
Office of Equal Employment Opportunity	Strives to enhance access to employment opportunities for the best and brightest talent, and to foster a fair and equitable work environment in compliance with federal laws and SEC standards.

Table 1.1 | *Continued from previous page*

AGENCY DIRECTION AND ADMINISTRATIVE SUPPORT *(CONTINUED)*	
Office of Public Affairs	Assists the Commission in making the work of the SEC is accessible to the public, understandable to investors, and accountable to taxpayers.
Office of the Secretary	Reviews all documents issued by the Commission; schedules and coordinates Commission meetings; prepares and maintains records of Commission actions; and receives and tracks filings in administrative proceedings.
Office of Financial Management	Oversees the agency's financial systems and prepares financial statements and reports; manages the formulation and execution of the SEC's annual budget; coordinates the agency's performance and cost reporting; and oversees internal controls over financial reporting.
Office of Information Technology	Maintains responsibility for the Commission's infrastructure operations and engineering, user support, program management, capital planning, cybersecurity, and enterprise architecture.
Office of Strategic Initiatives	Oversees the Electronic Data Gathering, Analysis, and Retrieval (EDGAR) program, including by serving as the EDGAR system's business owner; leads the redesign of the EDGAR system; and manages the agency's data and information services.
Office of Human Resources	Assists with recruitment, staffing, organizational development, leadership and employee development, compensation and benefits administration, position classification, workforce planning, and labor relations.
Office of Acquisitions	Provides advice on acquisition planning, development, and sourcing; awarding contracts and interagency agreements; and ensures contract terms and conditions are met through timely contract closeouts and de-obligation of funds.
Office of Support Operations	Processes requests under the Freedom of Information and Privacy Acts; maintains all agency records in accordance with the Federal Records Act; oversees the security and safety of SEC facilities; and manages property, equipment, and overall building operations.
INSPECTOR GENERAL	
Office of Inspector General	Conducts audits of the SEC's and investigates allegations of misconduct by staff or contractors in an effort to detect fraud, waste, and abuse, as well as promote integrity, economy, efficiency, and effectiveness throughout the agency's programs and overall operations. This is an independent office.

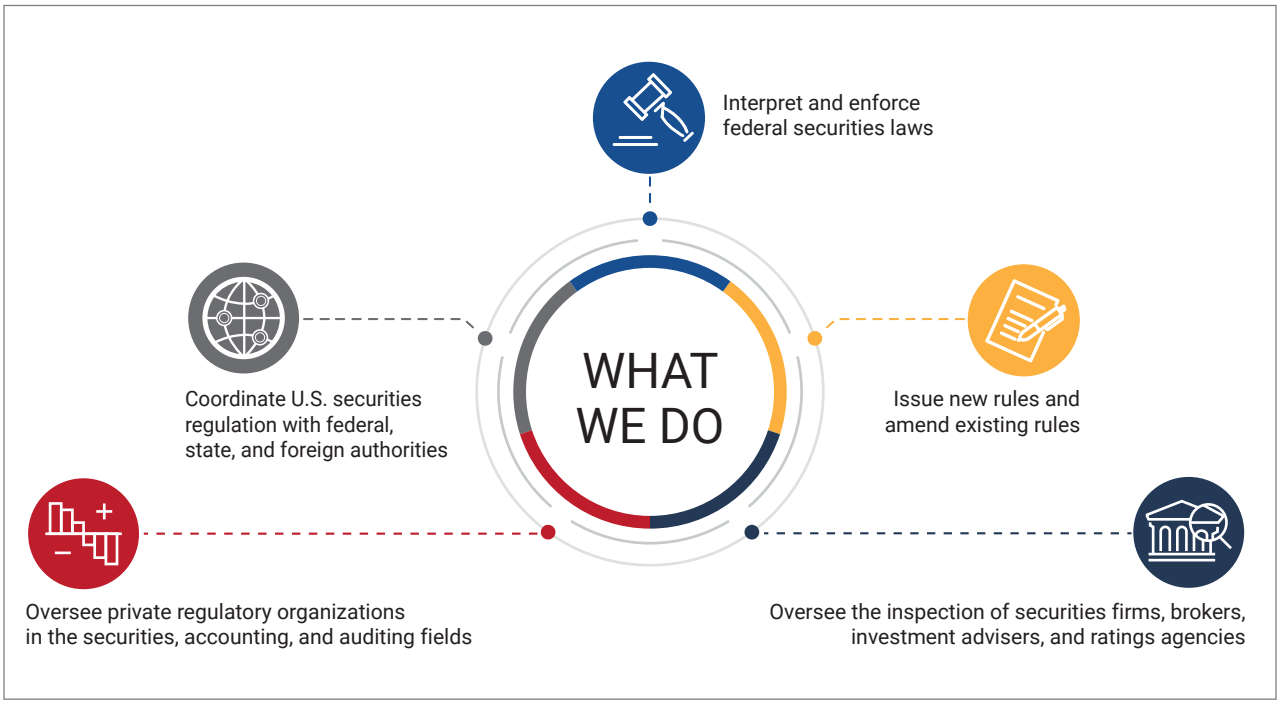
As shown in the Statements of Net Cost on page 65, the SEC presents its costs of operations by the programs outlined above, consistent with the presentation used by the agency in submitting its budget requests.

YEAR IN REVIEW

FY 2017 was a year of transition at the SEC. In January 2017, Mary Jo White stepped down as the SEC's Chair after nearly four years of service. Between January and May 2017, Michael Piwowar, a current Commissioner, served as Acting SEC Chairman. And on May 4, 2017, following his nomination by the President and confirmation by the U.S. Senate, Jay Clayton began work as SEC Chairman. Throughout FY 2017, the agency's capable and experienced career staff—approximately 4,600 personnel—worked vigorously to execute the SEC's mission. Their efforts provided a strong measure of continuity and facilitated a smooth and orderly leadership transition.

As a result, FY 2017 was a significant year for the SEC. During FY 2017, the agency and our staff oversaw, among other things, approximately $72 trillion in securities trading on U.S. equity markets; the disclosures of 4,300 exchange listed public companies; and the activities of over 26,000 registered market participants including investment advisers, mutual funds, exchange-traded funds (ETF), broker-dealers, and transfer agents. We also engaged and interacted with the investing public on a daily basis through a number of activities ranging from our investor education programs to alerts on our www.sec.gov portal to disclosure documents filed on our Electronic Data Gathering, Analysis, and Retrieval (EDGAR) system.

The following sections, organized based on our strategic goals, summarize a number of notable actions taken in FY 2017. Additional details on these, and other significant, agency actions are available on the agency's website, www.sec.gov.



STRATEGIC GOAL 1: Establish and maintain an effective regulatory environment

The U.S. capital markets have long been among the deepest, most dynamic, and most fluid in the world. They provide businesses with the opportunity to grow, create jobs, and furnish diverse opportunities for investors, including retail investors and pension funds. Our markets also have provided the United States with a competitive advantage in capital formation and American Main Street investors with better investment opportunities than comparable investors in other jurisdictions. In its work, the SEC strives to maintain and enhance these complementary positions, including being mindful of emerging trends and related risks.

Effective Oversight of Changing Markets

Technological advancements and commercial developments are leading to significant changes in the way our markets operate—and requiring the SEC to remain vigilant and continuously examine its regulation of U.S. markets. During FY 2017, the SEC devoted significant attention to its monitoring, oversight, and regulatory functions to ensure that the securities markets provide vibrant, efficient, and fair mechanisms for facilitating the transfer of capital, as explained below.

In March 2017, the Commission adopted rules to shorten the standard settlement cycle for most securities transactions from three to two business days. This change, implemented in September 2017, represents a significant milestone for the securities markets. The last time the standard settlement cycle was amended was 1995, when the Commission reduced it from five to three business days. The SEC's economic analysis concluded that the shortened two-day settlement cycle will reduce credit, market, and liquidity risk in the clearance and settlement process, while enhancing the efficiency of securities transactions.

In October 2016, in response to a June 2014 Commission directive, the self-regulatory organizations (SRO) began a pilot program under the National Market System to test the impact of wider tick sizes on the trading of stocks of certain smaller capitalization companies. This "Tick Size Pilot" will be in effect for two years. Preliminary analyses of the pilot data indicate that the impact of the wider tick sizes on market quality has been mixed. For many covered securities, quoted spreads and depth of book have increased, and volatility has decreased. Trading center data became publicly available in August 2017 and is enabling more robust analysis.

Facilitating Capital Formation

The SEC undertook significant efforts during FY 2017 to facilitate capital formation, especially in the public markets. In particular, staff attorneys and accountants in the Division of Corporation Finance (CF) assisted over 400 companies through an initial public offering (IPO) and nearly 100 companies as they entered the periodic reporting system. Other accomplishments achieved in FY 2017 are listed in the following paragraphs.

In July 2017, the division began accepting and reviewing, on a non-public basis, voluntary draft registration statement submissions for all IPOs, follow-on offerings within 12 months after an IPO, and companies registering securities for the first time under the Securities Exchange Act. This expanded policy, which builds on the confidential submission process established in response to the Jumpstart Our Business Startups (JOBS) Act, has provided meaningful new benefits to companies and investors, and a number of companies have already pursued this path. In August 2017, the division also clarified that companies may omit from draft registration statements interim financial information that otherwise will not be required when a company files its registration statement. This saves costs for companies, yet investors continue to benefit from the full financial information required when a company publicly files its registration statement.

The SEC also held five meetings during the year of our Advisory Committee on Small and Emerging Companies, a group of outside experts chartered by the agency for the purpose of obtaining advice regarding capital-raising by small and emerging companies. Their insights continue to prove valuable to the SEC and our Main Street investors.

Protecting Retail Investors

In recent decades, the share of Americans' retirement savings held in Individual Retirement Accounts (IRA), 401(k) retirement savings plans, and other defined contribution plans has grown considerably. With more Main Street investors directly responsible for making key decisions about their retirement savings, the SEC during FY 2017 devoted significant attention to revising or updating various rules focused on protecting retail investors. We provide many avenues to provide and enhance protections for retail investors, including enforcement, examination of financial intermediaries, and investor education. Transparency also protects investors both in facilitating better decision-making and providing a means for detecting and pursuing misconduct. Examples of our accomplishments are listed below.

In March 2017, the Commission voted to propose rule amendments to improve investor protection and enhance transparency in the municipal securities market. The revisions to Exchange Act Rule 15c2-12 seek to provide municipal bond investors with timely access to important information regarding certain financial obligations incurred by issuers and obligated persons that could impact such entities' liquidity and overall creditworthiness.

In September 2017, the SEC announced the formation of a new group within the Division of Enforcement (Enforcement)—the Retail Strategy Task Force—to develop proactive, targeted initiatives to identify misconduct impacting retail investors. The task force is focused on applying lessons learned from past frauds and leveraging data analytics and technology to identify large-scale misconduct affecting retail investors. The task force includes enforcement personnel from around the country, and in carrying out its work also collaborates with staff across the SEC, including from the SEC's National Exam Program and the Office of Investor Education and Advocacy (OIEA).

robo-adviser /rō-bō-əd-vī-zər / ▸n.
an automated adviser that utilizes algorithmic-based programs to provide financial advice and services with little or no human intervention

The SEC also held three meetings during the year of our Investor Advisory Committee, an external group chartered by the agency for the purpose of obtaining advice regarding initiatives to protect investor interests. The committee's work was supplemented by the important work of the SEC's Office of Investor Advocate, established in 2014 to be a voice for investors by, among other things, analyzing the impact of proposed regulatory changes on investors and recommending changes to regulations for the benefit of investors.

Other notable investor protection initiatives accomplished in FY 2017 include the issuance of guidance clarifying the legal responsibilities of fast-growing "robo-advisers" that typically provide advice through online algorithmic-based programs. And, as discussed below, the agency brought a significant number of enforcement cases involving retail investor fraud.

Retrospective Reviews

The SEC and the public benefitted from a number of studies by economists within the Division of Economic Research and Analysis (DERA) that aimed to inform agency staff and the public, including studies that look at the impact of its rulemaking actions after rule adoption. For instance, in December 2016, DERA issued a white paper that analyzed the market for Regulation A offerings after adoption of new Commission rules. Another DERA white paper, in February 2017, examined offering activity in the securities-based crowdfunding market following adoption of new Commission rules.

STRATEGIC GOAL 2: Foster and enforce compliance with the federal securities laws

At the heart of the SEC's work to protect investors, facilitate capital formation, and maintain the integrity of the securities markets is our work to foster and enforce compliance with the federal securities laws and our rules. In FY 2017, the SEC invested more than half of our budgetary resources in the agency's enforcement and examination programs which are focused, among other things, on rooting out fraud and wrongdoing in our financial system and ensuring that broker-dealers and investment advisers comply with investor protection rules.

Enforcement Program Highlights

Enforcement, the agency's largest program, conducts investigations into possible violations of the federal securities laws, and oversees the Commission's civil suits in the federal courts as well as its administrative proceedings. Through these efforts, the SEC pursues significant cases that bring securities law violators to justice, return money to harmed investors, and send important messages of deterrence.

disgorgement /dis-gȯrj-ment / ▸ n. the act of returning or repaying ill-gotten gains obtained from fraudulent activities

During FY 2017, acting on recommendations by enforcement staff, the Commission authorized 446 stand-alone enforcement actions, 196 follow-on proceedings and 112 delinquent filing proceedings. The SEC obtained judgments and orders for over $3.8 billion in penalties and disgorgement, returned a record $1.0 billion to harmed investors, ordered over $50 million in payments to whistleblowers, suspended trading in the securities of 309 issuers to combat market manipulation and microcap fraud, and obtained favorable verdicts in federal district court. The SEC's enforcement actions during the year spanned the entire spectrum of the securities industry.

Retail Investor Fraud. The SEC in FY 2017 filed numerous enforcement cases targeting securities registration violations, offering frauds, and Ponzi schemes targeted at retail investors. Among the more high-profile cases, the SEC disrupted two schemes involving businesses purportedly created to purchase and resell tickets to high-demand concerts and shows, and also brought charges against the alleged orchestrators of a "boiler room" scheme who solicited investments in a business purportedly facilitating online and cell phone sales of lottery tickets. The SEC also brought cases interdicting frauds targeting senior citizens, such as filing fraud charges against individuals allegedly involved in two cold-calling scams that bilked more than 100 victims out of more than $10 million through high-pressure sales tactics and lies about penny stocks. The SEC in FY 2017 also issued an investigative report cautioning market participants that offers and sales of digital assets by "virtual" organizations—such as "Initial Coin Offerings"—are subject to the requirements of the federal securities laws, and that persons participating in unregistered offerings may be liable for violations of those laws.

Investment Professional Misconduct. The SEC took significant actions during the year to halt misconduct by investment professionals. Through its enforcement program, the SEC secured settlements from Barclays Capital (to pay more than $97 million to refund clients who were overcharged); Pacific Investment Management Company (to pay nearly $20 million to settle charges that it misled investors about the performance of an actively managed ETF); and Morgan Stanley Smith Barney (to pay $8 million and admit wrongdoing related to the sale of certain unsuitable investments to advisory clients). The SEC also filed fraud charges against the founder of Platinum Partners and two of its flagship hedge fund advisory firms for conducting a fraudulent scheme to inflate asset values and illicitly move investor money to cover losses and liquidity problems.

Cyber-Based Fraud. Using a technology- and data-driven approach, the SEC during the year targeted and brought enforcement actions against a variety of cyber-based financial schemes. Among others, the SEC filed charges against a Virginia-based mechanical engineer accused of scheming to manipulate the price of Fitbit stock by making a phony regulatory filing, and also brought charges against three Chinese traders for racking up almost $3 million in illegal profits by trading on hacked nonpublic market-moving information stolen from two prominent law firms.

Financial Fraud. The SEC was successful during the year in identifying and rooting out numerous financial and disclosure frauds. Among others, the SEC filed financial fraud charges against a Canada-based oil and gas company and three of its former top finance executives for their roles in an alleged extensive accounting fraud; a global financial services company, which agreed to pay $90 million and admit wrongdoing for misrepresentation of how it determined a key performance metric; and a Mexico-based homebuilding company for allegedly reporting fake sales of more than 100,000 homes to boost revenues in its financial statements.

Gatekeeper Misconduct. The SEC continued to focus on potential legal violations by gatekeepers who are well positioned to detect and prevent compliance breakdowns and fraudulent schemes that cause investor harm. During FY 2017, the SEC successfully brought enforcement actions against Ernst & Young LLP (who agreed to pay more than $11 million to settle charges related to failed audits of an oil services company that used deceptive income tax accounting to inflate earnings) and KPMG (who agreed to pay more than $6 million to settle charges that it failed to properly audit the financial statements of an oil and gas company resulting in investors being misinformed about the company's value).

COMMON INVESTMENT SCHEMES

Boiler Room
Using high-pressure sales tactics

Ponzi
Providing returns to established investors with funds from new investors rather than from profits

Pump-and-Dump
Touting a company's stock (typically microcap companies) through false and misleading statements

Pyramid
Recruiting new participants by promising sky-high returns in a short period of time for doing nothing more than handing over money

Insider Trading. The SEC charged 100 parties in insider trading actions, sending a strong message of deterrence to would-be violators. Notable examples include enforcement actions against a partner at a Hong Kong-based private equity firm who allegedly amassed more than $29 million in illegal profits by trading in advance of Comcast's acquisition of DreamWorks Animation; the former chief executive officer of a Silicon Valley-based fiber optics company who allegedly generated more than $2 million in illicit profits and losses avoided by trading on nonpublic information and tipping his brother ahead of two negative earnings announcements and the company's merger; a former government employee-turned-political intelligence consultant involving alleged tips of nonpublic information about government plans to cut Medicare reimbursement rates; and seven individuals who allegedly generated millions of dollars in illegal profits by trading on confidential information regarding dozens of impending mergers and acquisitions.

Foreign Corrupt Practices Act (FCPA) Violations. The SEC continues to be a vigorous enforcer of the FCPA, which generally prohibits the payment of bribes to foreign officials to assist in obtaining or retaining business. Among the more notable FCPA victories during the year are a $965 million settlement with Swedish telecommunications provider Telia Company AB (to resolve claims involving efforts to win business in Uzbekistan); a $957 million settlement with petrochemical manufacturer Braskem S.A. (to settle claims involving millions of dollars in illicit bribes paid to Brazilian government officials to win business); a $519 million settlement with Teva Pharmaceutical Industries (to settle charges that it paid bribes to government officials in Russia, Ukraine, and Mexico); a $205 million settlement with aircraft manufacturer Embraer S.A. (to settle charges that it violated the FCPA to win business in the Dominican Republic, Saudi Arabia, Mozambique, and India); and a $130 million settlement with JPMorgan Chase & Co. (for claims arising from its hiring practices in the Asia-Pacific region). The SEC's FCPA cases typically entail substantial coordination with the U.S. Department of Justice and foreign authorities.

Whistleblower Awards. The Dodd-Frank Act authorized the SEC to provide monetary awards to eligible whistleblowers who come forward with high-quality original information that leads to SEC enforcement actions resulting in sanctions of more than $1 million. During FY 2017, the SEC awarded nearly $50 million to 12 whistleblowers. The SEC also during the year charged several companies—Neustar Inc., SandRidge Energy Inc., BlackRock Inc., and HomeStreet Inc.—for taking action to impede potential whistleblowers from communicating with the SEC about possible securities law violations.

Jury Trial Victories. The SEC's experienced trial attorneys secured favorable jury verdicts during the year against a drug company employee and his friend who were found liable for insider trading that earned over $1 million in illegal profits; the former chairman of a public company who was found liable for fraudulently obtaining millions of dollars in loans from his brokerage firm; and an individual who was found liable for insider trading before an upcoming merger between a pharmaceutical company and medical products manufacturer.

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retail investor /rē-tāl-in-vest-ər / ▸ n.
an individual who buys securities for personal benefit (e.g., to purchase a home, save for retirement, send a child to college) rather than the benefit of an organization

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Examinations Program Highlights

During the year, the SEC conducted thousands of examinations of registered entities—including broker-dealers, investment advisers, investment companies, municipal advisors, national securities exchanges, clearing agencies, transfer agents, and the Financial Industry Regulatory Authority (FINRA)—to promote compliance and monitor risks to retail investors. The SEC during the year focused its examination program on a number of priority areas, including those listed below.

Expanded Coverage of Investment Advisers. Given the significant growth in assets under management by registered investment advisers, the SEC in recent years has been shifting more resources to investment adviser exams. In FY 2017, the SEC achieved examination coverage of approximately 15 percent of all investment advisers, up from 8 percent just five years ago. In addition, the SEC continued to leverage data analysis to analyze and identify potentially problematic activities and firms and to use this information to make decisions concerning which firms to examine and how best to scope those examinations.

Retail Investors. The SEC during the year had a strong focus on risks to retail investors seeking information, advice, products, and services. This included examining investment advisers and broker-dealers to assess the services they provided to investors with retirement accounts, focusing on the reasonable basis for recommendations made to investors, conflicts of interest, supervision, compliance controls, and marketing and disclosure practices. The SEC also conducted examinations focused on conflicts of interest that may have influenced recommendations to invest in particular mutual fund share classes with higher loads or distribution fees. The SEC also conducted exams of firms that employed representatives with a record of misconduct to ensure that those representatives were adequately supervised when dealing with retail investors. Yet another area of retail focus was the examination of market makers and broker-dealers that serve retail customers to assess how they were complying with their duty of best execution when routing customer orders for execution.

Market-Wide Risk. The SEC during the year conducted 64 examinations focused on compliance with Regulation SCI, a 2014 Commission regulation designed to strengthen the technology infrastructure of the U.S. securities markets, including against cyber-attacks. Through the SEC's CyberWatch program, the agency also monitored for significant cyber events and outages affecting critical securities market infrastructure. Another examination initiative for FY 2017 focused on evaluating money market funds' compliance with the new fund structure rules that took effect in October 2016.

Credit Rating Agencies. Through its Office of Credit Ratings, the SEC in FY 2017 conducted examinations of all registered nationally recognized statistical rating organizations (NRSRO) to assess and promote compliance with regulatory requirements. During FY 2017, the SEC expanded the quantitative, information technology, and cybersecurity components of its NRSRO examinations.

market maker / mär-kət-mā-kər / ▸ n.
a firm that stands ready to buy and sell a particular stock on a regular and continuous basis at a publicly quoted price

FINRA Oversight. Given FINRA's status as the largest self-regulatory organization in the securities industry and its front-line responsibility to regulate broker-dealers, conducting inspections of FINRA operations and regulatory programs remained a key SEC priority for FY 2017. During the year, the SEC conducted targeted risk-based reviews of several FINRA programs and assessed the quality of FINRA's examinations of broker-dealers to ensure that its programs protect retail investors.

STRATEGIC GOAL 3: Facilitate access to the information investors need to make informed investment decisions

Because an educated and informed investor ultimately provides the best defense against fraud and costly mistakes, the federal securities laws require that companies, mutual funds, and other entities provide investors with timely and meaningful information about, among other things, their operations and financial condition. The SEC took a variety of actions during the year to advance the agency's disclosure interests.

Modernizing Disclosure Requirements

The SEC continued during FY 2017 to advance efforts to modernize and simplify public company disclosure requirements. During the year, CF developed and submitted to the Commission a proposal to revise Regulation S-K, the overarching regulation that sets forth the disclosure requirements for registration statements and ongoing reporting requirements for public companies. The aim of the Regulation S-K revisions, as articulated in November 2016 staff report on the topic, is to modernize and simplify disclosure requirements and improve the readability and the navigability of disclosure. In October 2017, the Commission voted to approve the division's rule proposal and expose it to public comment.

In March 2017, the Commission voted to propose amendments to require use of Inline eXtensible Business Reporting Language (XBRL) as a way to improve the quality and accessibility of data submitted by public companies and mutual funds, while also reducing the time and cost of preparing filings. Inline XBRL is a technology that allows filers to embed XBRL data directly into their EDGAR filings instead of as attachments, which is anticipated to reduce the likelihood of inconsistencies. The rule proposal was developed in collaboration with economists and data experts in DERA.

Improving Corporate Disclosures

The SEC promotes informed investment decisions by requiring that investors be given accurate, adequate, and timely public access to disclosure materials that are easily understood and analyzed. To help companies comply with these requirements, CF and the Division of Investment Management (IM) devote significant staff resources to reviewing, on a regular and systematic basis, the periodic reports of public companies and mutual funds to monitor and enhance compliance with the applicable disclosure and accounting requirements.

liquidity / li-kwi-də-tē / ▸ n. also referred to as marketability, this is a measure of the relative ease and speed with which a security can be bought or sold in a secondary market

During FY 2017, CF reviewed and, as appropriate, issued comments on the annual reports and financial statements of nearly 4,200 public companies. Similarly, IM reviewed more than 5,000 investment company annual reports. In these filing reviews, SEC staff concentrate on critical disclosures that appear to conflict with Commission rules or the applicable accounting standards and on disclosure that appears to be materially deficient in explanation or clarity. After completing a review, staff may send the company a comment letter requesting additional information or to elicit better compliance with applicable requirements. To increase the transparency of the review process, when the agency completes a filing review, it makes its comment letters (and company responses to those comment letters) public on the SEC's EDGAR system.

The Investor's Advocate and Investor Education

The SEC promotes informed investment decisions through education initiatives aimed at giving investors a better understanding of the operations of the nation's securities markets. During FY 2017, the agency continued our "Before You Invest, Investor.gov" public service campaign intended to encourage investors to research the background of their investment professional. As a result of the public service campaign and other investor education initiatives, a record 2.2 million new users visited Investor.gov, an increase of 18 percent compared to FY 2016. The SEC also participated in 70 events focused on military personnel and their families as part of our Military Financial Literacy Campaign.

OIEA also issued a variety of investor alerts and bulletins during the year to warn investors of possible fraudulent schemes, and educate them on investment-related matters. During the year, the agency issued bulletins on a number of timely topics, including robo-advisers; the risks of microcap stock investing; and initial coin offerings. We also published a new guide for investors on mutual funds and ETFs. In addition, the SEC assisted thousands of investors with investment-related complaints and answered questions from individual investors needing assistance.

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

We are committed to maintaining a work environment that promotes information-sharing and collaboration across the agency and leverages technology and data analysis to fulfill our mission more effectively and efficiently. The work of the SEC's many mission-facing attorneys, accountants, examiners, and economists is made possible thanks to the important behind-the-scenes work of the agency's administrative and operations personnel, including within the centralized support offices under the chief operating officer and in a division or office's internal business operations. The agency's numerous supervisors and program managers also play a critical role in ensuring effective and efficient operations and activities. The following paragraphs detail key areas of focus during FY 2017.

Cybersecurity

Cybersecurity is vitally important to us, especially given the increased use of and dependence on data and electronic communications, greater complexity of technologies present in the financial marketplace, and continually evolving threats from a variety of sources. In September 2017, Chairman Clayton issued a Statement on Cybersecurity detailing the agency's approach to cybersecurity as an organization and as a regulatory body. In addition to providing an overview of the Commission's collection and use of data and discussing key cyber risks faced by the agency, the statement discussed the incorporation of cybersecurity considerations in disclosure-based and supervisory efforts, coordination with other government entities, and enforcement of the federal securities laws against cyber threat actors and market participants that do not meet their disclosure obligations.

The statement and accompanying press release also publicly disclosed that the SEC had been the subject of an intrusion into the test filing portion of the agency's EDGAR system in 2016. The statement, together with an update provided by Chairman Clayton in October 2017, described the various workstreams in place to assess the scope of the 2016 intrusion and to assess and uplift the agency's cybersecurity profile with respect to EDGAR and more broadly with respect to systems used across the agency. The SEC during FY 2017 increased its investment in tools, technologies, and services to protect the security of the agency's network, systems, and sensitive data. Overall, by promoting effective cybersecurity practices in connection with both our internal operations and external regulatory oversight efforts, we aim to contribute substantively to a financial market system that recognizes and addresses cybersecurity risks and, in circumstances in which these risks materialize, exhibits strong mitigation and resiliency.

Strengthening EDGAR

The EDGAR system is central to the agency's mission and critical to the functioning of the capital markets. On a typical day, investors and other market participants view or download more than 50 million disclosure documents filed on EDGAR.

As noted above, the agency has instituted an operational review of, and as necessary or appropriate, uplift of the EDGAR system, with a focus on cybersecurity. In this regard, the agency created an EDGAR Program Office to improve EDGAR governance, accountability, and expertise through the creation of the EDGAR Program Office. This new office consolidated the agency's various EDGAR filer support functions into a single office to provide better customer service and organizational clarity to EDGAR filers. By serving as EDGAR's business owner, the office also will coordinate and rationalize the agency's enhancements and investments related to EDGAR, including modifications to conform with changes to Commission rules.

Because EDGAR is a critical component of our disclosure-based market system and accepts filings virtually continuously during the week, it is a priority to maintain the system's security and day-to-day operational capabilities. The SEC is engaged in a focused, operational review of EDGAR's security, including to assess the types of data we take in through the EDGAR system and whether EDGAR is the appropriate mechanism to obtain that data. As appropriate, we plan to take actions to strengthen EDGAR's security.

Leveraging Technology, Data, and Analytics

Apart from cybersecurity, the SEC's Office of Information Technology (OIT) has identified enhancing data management and advanced analytic capabilities as one of the agency's top IT strategic priorities. By enabling staff to harness the data available to them—for instance, by spotting patterns and relationships that might warrant further inquiry—the SEC's information technology investments enable the delivery of new mission capabilities and drive productivity gains across the agency. During FY 2017, OIT completed a comprehensive IT Strategic Plan for 2018–2020 that details how the agency plans to use and approach information technology over the next three years. In addition to advancing cybersecurity protections and enhancing data and analytic capabilities, the plan's other key priorities include: providing more agile approaches to technology delivery; and providing a high level of system and infrastructure reliability.

Improving Agency Operations

The SEC in FY 2017 pursued a number of initiatives to find efficiencies in internal operations, including through automation, streamlined internal processes and better use of data. We continue to develop and leverage our capabilities for risk analysis to inform our

decision making, including how most efficiently to use staff resources. Other internal improvement initiatives include combining the agency's various communications-related functions, crafting proposals to reduce the use of paper documents, and exploring ways to better apply and schedule examination staff resources.

Continuing to Make the SEC a Great Place to Work

Maintaining a high level of staff engagement and morale is critical to our ability to execute our mission. In FY 2017, nearly 80 percent of the SEC's eligible workforce completed the Office of Personnel Management's annual Federal Employee Viewpoint Survey (FEVS)—a record level of participation. This year's FEVS results showed notable increases in employee engagement, overall satisfaction and leader effectiveness indices, and also identified areas where continued management focus is needed to strengthen engagement with our workforce. While the SEC still has progress to make, the FEVS survey results show the agency is headed in the right direction, as evidenced by the fact that the SEC's global employee satisfaction scores were the highest of all mid-sized government agencies who participated in the survey.

During FY 2017, the SEC received recognition for its improved employee satisfaction scores. In 2017, the SEC's rating on the Partnership for Public Service *Best Places to Work* improved to 76 percent, up 20 percentage points since 2012. The SEC was also singled out as the "most improved" mid-sized federal agency, which resulted in the SEC's chief human capital officer being asked to testify in April 2017 before the House Oversight and Government Reform Committee on the agency's progress. We aim to continue building upon these 2017 results in the years to come.

LOOKING FORWARD

The SEC's tripartite mission—to protect investors; maintain fair, orderly, and efficient markets; and facilitate capital formation—remains our touchstone. The core principles we have applied over the past 80 years to carry out this mission are just as valuable and timeless today: relying on material disclosures to facilitate informed investment decision-making, placing heightened responsibilities on central or active securities market participants, and using our anti-fraud regime as a back-stop to our disclosure rules and oversight systems.

In the nearly 10 years since the global financial crisis, the SEC has undertaken significant efforts to respond to the lessons learned from that crisis, including to reinvigorate how we do our work, strengthen our core oversight and regulatory programs, and implement improvements to make our markets stronger and more resilient. Of course, the SEC's work does not just involve looking back to the causes of past crises. An equally important part of the agency's work is looking ahead to meet new and emerging challenges facing our markets.

As Markets Evolve, So Must the SEC

Our securities markets and the technologies that support those markets and our internal operations are evolving and innovating at a fast pace, presenting numerous benefits as well as challenges. Given the pace of change in today's world, it is important that the SEC be efficient and nimble and direct attention where it is needed most. Taking stock of lessons learned from past regulatory challenges and successes, the SEC has undertaken a variety of initiatives in recent years to improve the agency's capability to be more strategic and forward-looking. In FY 2018 and the future, we intend to build on this progress and deepen these essential capabilities.

Expanding Capabilities to Assess and Respond to Market Risk. The SEC has made it a priority to hire staff to strengthen the agency's foundation of market knowledge and trends, its capability to perform high-quality economic and statistical analysis, and its ability to develop and leverage analytic tools that sort through market and disclosure data to detect risks. Since the 2009 creation of the DERA to integrate financial economics and rigorous data analytics into the core mission of the SEC, its staffing level has tripled, from about 50 staff positions to more than 150 staff today.

A number of key mission-facing offices have also formed new units to deepen their risk assessment and data analysis capabilities. For instance, in FY 2017, Enforcement announced two new initiatives to build on its ongoing efforts to address cyber-based threats and protect retail investors. The division's Cyber Unit will focus on targeting cyber-related misconduct, and its Retail Strategy Task Force is charged with developing proactive, targeted initiatives to identify misconduct impacting retail investors. In addition, in 2010, Enforcement created the Office of Market Intelligence to oversee the analysis of tips and complaints including to look for trends. Other new offices created in recent years include: the Office of Compliance Inspections and Examinations' Office of Risk and Strategy; the Division of Trading and Markets' Office of Research and Analytics; IM's Risk and Examinations Office; Enforcement's Center for Risk and Qualitative Analytics; and CF's Disclosure Standards Office.

The staff in these offices interact regularly to share information arising from data-enabled risk analysis and to monitor emerging risks in the market that may significantly impact registrants, the markets, or the agency's regulatory oversight responsibilities. This expertise is enabling us to gain better insight

PRINCIPLES IN PRACTICE

01	The SEC's mission is our touchstone.
02	Our analysis starts and ends with the long-term interests of the Main Street investor.
03	The SEC's historic approach to regulation is sound.
04	Regulatory actions drive change, and change can have lasting effects.
05	As markets evolve, so must the SEC.
06	Effective rulemaking does not end with rule adoption.
07	The costs of a rule now often include the cost of demonstrating compliance.
08	Coordination is key.

into emerging risks so that the agency can adjust its regulatory mission as necessary, whether through writing new rules, better targeting staff exams, reviews, or investigations, and applying staff resources where they can have the most impact. As resources permit, the SEC intends to continue to develop and expand these programs in the years to come.

Maturing Internal Control and Risk Assessment Capabilities. The SEC has undertaken significant efforts in recent years to develop more mature operational risk assessment and internal control programs. The agency has continued to bolster its internal controls and financial reporting program under the Federal Manager Financial Integrity Act (FMFIA). Beginning in 2010, the SEC now also conducts an annual assessment and report on the adequacy of the internal supervisory controls that govern key mission-facing programs—the reviews of corporate financial securities filings, enforcement investigations, and examinations of registered entities. In 2013, the SEC formalized an operational risk management program, overseen by a Risk Management Oversight Committee comprised of senior executives from across the agency. Through this program, the agency monitors the operational risk environment and provides direction to risk owners for mitigating operational risks that may adversely affect the SEC's ability to achieve its goals.

The agency plans to further mature these functions during FY 2018 and future years to further expand and strengthen the agency's internal enterprise risk capabilities. Most notably, the SEC has already announced plans to establish a new chief risk officer role—a senior executive focused full-time on assessing, coordinating, and spearheading the agency's various risk management efforts.

Preparing for the Future

The SEC is currently developing a Strategic Plan, to be published in early 2018 for public comment, that will lay out the agency's vision for the next five years. It will sketch out what we view as the key challenges and trends facing our markets and regulatory programs, articulate the agency's most important strategic priorities, and identify the initiatives we are pursuing to help us attain those goals.

In 2018, the SEC has a number of initiatives underway that are resulting from our ongoing work to identify and respond to internal and external challenges and trends. We have highlighted a number of these ongoing areas of focus below. In addition, the SEC's Office of Inspector General (OIG) has shared with agency management its insight and perspective—gained through its ongoing work to audit and evaluate agency programs and operations—on the most significant management and performance challenges facing the agency. A detailed discussion of the challenges identified by the OIG, including information on the SEC's progress in addressing them, is provided in the "Other Information" section of this report.

Cybersecurity. Data collection, storage, analysis, availability and protection (including security, validation and recovery) have become fundamental to our capital markets, the individuals and entities that participate in those markets, and the SEC. The scope and severity of risks that cyber threats present have increased dramatically, and constant vigilance is required to protect against intrusions. The SEC is focused on identifying and managing cybersecurity risks and ensuring that market participants—including issuers, intermediaries, investors, and government authorities—are actively and effectively engaged in this effort and are appropriately informing investors and other market participants of these risks.

We recognize that even the most diligent cybersecurity efforts will not address all cyber risks that enterprises face. Malicious attacks and intrusion efforts are continuous and evolving, and in certain cases they have been successful at the most robust institutions, including at the SEC itself. Cybersecurity efforts must include, in addition to assessment, prevention and mitigation, resilience and recovery.

In May 2017, the SEC initiated an assessment of our internal cybersecurity risk profile and our approach to cybersecurity from a regulatory and oversight perspective. Components of this initiative build on prior agency efforts in this area and include establishing a senior-level cybersecurity working group to coordinate information sharing, risk monitoring, and incident response efforts throughout the agency. We have also several workstreams in place to review the 2016 EDGAR intrusion and assess and uplift the security of EDGAR and our other systems more broadly. As mentioned above, Chairman Clayton also issued a press release and Cybersecurity Statement in September 2017, and an update in October 2017 on our ongoing review of the 2016 EDGAR intrusion, as part of our effort to improve and communicate our work in this area to market participants and the American public.

We must remain on top of evolving threats when it comes to securing our own networks and systems against intrusion. This is especially true when protecting systems dealing with sensitive market data and data involving personally identifiable information (PII). This means regularly evaluating progress, pursuing improvements, and making it a priority to invest sufficient resources so our systems keep up with the fast-changing threat environment.

cybersecurity /sī-bər-si-kyu̇r-ə-tē / ▸n.
the steps taken to protect illegal or unauthorized access to a computer system or network

Looking forward, the SEC in FY 2018 is hiring additional staff and outside technology consultants to aid in our efforts to protect the security of the agency's network, systems, and data. The SEC is also taking a number of steps designed to strengthen our cybersecurity risk profile, with an initial focus on EDGAR. This effort includes assessing the types of data we take in through the EDGAR system, and whether EDGAR is the appropriate mechanism to obtain that data. Another part of this effort is reviewing the security systems, processes, and controls we have in place to protect data submitted through EDGAR. The SEC is also conducting similar reviews of other systems we use, assessing the types of data we keep and the related security systems, processes and controls. We are working to enhance our escalation protocols for cybersecurity incidents in order to enable greater agency-wide visibility and understanding of potential cyber vulnerabilities and attacks. More broadly, we are evaluating our cybersecurity risk governance structure, which has included the establishment of our senior-level cybersecurity working group and may include additional enhancements to promote the management and oversight of cybersecurity risk across the SEC's divisions and offices.

Consolidated Audit Trail (CAT) Implementation. Currently, trading activity occurs in a number of venues and no single system tracks orders as they are routed and executed. Pursuant to Commission rule, the securities exchanges and FINRA have developed a National Market System (NMS) Plan to establish a single, comprehensive database—a consolidated audit trail—that will track trading activity in the U.S. equity and options markets. The CAT data repository is currently being developed by a private, third-party plan processor (Thesys), under the direction of the securities exchanges and FINRA. Once implemented, the CAT will provide these SROs and the Commission with consolidated cross-market data that is more complete, accurate, accessible, and timely than the data currently available to regulators.

Of paramount concern to the SEC is the protection of sensitive CAT data, given that the data repository will contain extensive information on trading activity in the securities markets. The SEC therefore is focused on issues of data security with respect to CAT. We expect that the roll-out of the various components of CAT data reporting (wherein the SROs will report data to the central repository), will reflect an ongoing assessment of the sensitivity of the data reported and related security concerns and protections.

Among the defenses built into the CAT NMS Plan are requirements for the plan processor to develop a comprehensive information security program that addresses the security and confidentiality of all information within the CAT data repository and associated operational risks. And the SROs, which have direct oversight of the plan processor, are obligated to monitor the information security program to ensure that it is consistent with the highest industry standards for the protection of data. For the subset of data that may be extracted from the CAT data repository, the SROs and the SEC have independent obligations to protect any such data. With respect to the SEC specifically, we have committed to review regularly the effectiveness of our confidentiality and data use procedures in connection with our access to the CAT.

Technology and Innovation Are Changing How Markets Work and Investors Transact. Advances in technology have driven significant changes in securities markets. Today, companies support human decision-making with automated algorithms, which ingest massive amounts of unstructured data to make trading decisions. Investors are using innovative platforms to conduct transactions and research investments. Firms solicit investors through sophisticated, multichannel communications. The SEC recognizes that technology and innovation are constantly disrupting the manner in which markets work and investors transact, and strives to ensure that our rules and operations reflect the realities of our capital markets. We need to take into account new tensions, risks, uncertainties, and conflicts, and continuously examine and reassess our regulatory market structure.

While this dynamic atmosphere presents challenges, it also provides opportunities for improvements and efficiencies. It is our job as regulators to find these. Technology is not just the province of those we regulate. The SEC has the capability to develop and utilize it, too. We apply sophisticated analytic strategies to detect companies and individuals engaging in suspicious behavior. We are adapting machine learning and artificial intelligence to new functions, such as analyzing regulatory filings.

As the SEC evolves alongside the markets, however, we must remember that implementing regulatory change has costs. Companies spend significant resources building systems of compliance, hiring personnel to operate those systems, seeking legal advice concerning the design and effectiveness of those systems, and adapting the systems as regulations change. Shareholders and customers bear these costs, which is something that should not be taken lightly, lest we lose our credibility as regulators.

Because technology and markets are changing so rapidly, being able to stay current with market trends and developments is essential to the SEC's ability to remain an effective regulator. For this reason, in FY 2018 and future years the agency seeks to maintain and, within the constraints of available resources, expand its depth of expertise in vital areas such as market insight and analysis, clearing agencies, broker-dealer operations, electronic trading, and fixed income markets.

Individuals Are Increasingly Directly Responsible for Retirement Investment Decision-Making. Over the last four decades, the share of Americans' retirement savings held in IRAs, 401(k) retirement savings plans, and other defined contribution plans has grown from 20 percent to 58 percent, according to the Brookings Institution. With more and more Main Street investors directly responsible for making key decisions about their retirement savings, this makes the SEC's work to protect retail investors more important than ever.

This significant growth in IRA and 401(k) investors provides added urgency and importance to the SEC's ongoing evaluation of the standards of conduct that investment professionals must follow in providing advice to investors. With the U.S. Department of Labor's (DOL) Fiduciary Rule now partially in effect, the SEC must make all reasonable efforts to bring clarity and consistency to this area. We hope to act in concert with our colleagues at the DOL in a way that best serves the long-term interests of all Main Street investors, including those who have an IRA or 401(k).

While there is a lot of work to do, and this issue is complex, the SEC plans to move forward in FY 2018. In June 2017, the SEC Chairman issued a statement seeking public input on standards of conduct for investment advisers and broker-dealers. The robust public comments that have been received will help us evaluate potential regulatory actions in light of current market activities and risks. Any action will need to be carefully constructed, so it provides appropriate and meaningful protections but does not result in Main Street investors being deprived of affordable investment advice or products.

Decline in U.S.-Listed Public Companies. Over the last two decades, there has been a roughly 50 percent decline in the total number of U.S.-listed public companies. As an added data point, over this period, studies show the median word-count for SEC filings has more than doubled, yet readability of those documents is at an all-time low. While there are many factors that drive the decision of whether to be a public company, increased disclosure and other burdens may render alternatives for raising capital, such as the private markets, increasingly attractive to companies that only a decade ago would have been all but certain candidates for the public markets. Fewer small and medium-sized public companies may mean less liquid trading markets for those types of companies that remain public. And to the extent companies are eschewing our public markets, the vast majority of Main Street investors will be unable to efficiently participate in their growth.

In FY 2018, the SEC will be evaluating and developing a range of proposals designed to make our public capital markets more attractive to growing businesses than in the recent past. A key focus for the agency is to work to bring into better sync the reporting, compliance and oversight dynamic between private and public markets. This includes gaining better insight into the costs—ranging from direct compliance costs to the consumption of management and employee bandwidth—of being a public company, including for smaller and medium-sized companies. This must be done without adversely affecting, and with an eye toward enhancing, investor protection.

Additionally, during FY 2018, the SEC plans to staff a new Office of the Advocate for Small Business Capital Formation and establish a new Advisory Committee on Small Business Capital Formation, as required by

Congress in the SEC Small Business Advocate Act of 2016. Among other statutorily-mandated functions, the advocate will identify areas in which small businesses and small business investors would benefit from changes in Commission regulations or SRO rules. The advocate also will work to identify problems that small businesses have securing access to capital, including any unique challenges to minority- and women-owned businesses.

401(k) /fȯr-ō-wən-kā / ▸n. an employer-sponsored retirement savings plan that gives the employee a choice of investment options

Growing Importance of Fixed Income Markets. The Baby Boomers, born between 1946 and 1964, are heading into retirement in droves—about 10,000 a day, according to the Social Security Administration. As waves of retirees seek stable, income-producing investment options, fixed income products will attract more and more Main Street investors. While such products are viewed as a stable place to store hard earned money, many investors may not appreciate that fixed income products differ significantly from the better known equities products.

To help assess and address the challenges and market impact posed by these changing demographics, the SEC plans in FY 2018 to launch a new initiative to evaluate and take appropriate measures to enhance the efficiency, transparency, and effectiveness of fixed income markets. Specifically, the SEC has announced plans to establish a new Fixed Income Market Structure Advisory Committee tasked with examining and making recommendations with respect to the efficiency, transparency, and effectiveness of the fixed income markets. The committee is anticipated to be formally established and to begin meeting in early FY 2018. We expect that this committee initially will focus on the structure and operation of the U.S. corporate bond market and may also assess the extent to which any corporate bond market recommendations might also be relevant for the municipal bond market.

Globally Interconnected Financial Markets. At the same time that the SEC's domestic responsibilities are expanding, our regulatory activities increasingly have international implications. Traders in today's global financial markets can move billions of dollars thousands of miles away in a fraction of a second; issuers can explore a whole world of choices as they decide where to list and raise new capital; and investor portfolios are more diverse and global than ever before. Engagement and appropriate coordination with foreign regulators, both bilaterally and multilaterally, on everything from enforcement strategies to swaps regulation, are necessary for the SEC to oversee today's markets, to combat fraud, and to identify global risks that could impact U.S. securities markets.

Internationally, the SEC in FY 2018 will be closely monitoring the impact for U.S. investors and U.S. markets of market-wide regulatory changes in Europe. This includes the European Union's revised Markets in Financial Instruments Directive, which takes effect in January 2018, and the anticipated exit of the United Kingdom from the European Union in FY 2019. In addition, the SEC continues to build strong relationships with foreign counterparts to advance the agency's policy objectives in the international cooperation and assistance area. This includes promoting best practices, overcoming obstacles with respect to sharing cross-border enforcement-related information, and assisting and advising foreign authorities with their investigations.

Leveraging Technology To Be Smarter and More Efficient. In recent years we have seen an extraordinary increase in the volume and velocity of data available to the securities industry, investors, and the SEC. The ever-increasing volume of data demands advanced analytics tools and best-in-class infrastructure that is dynamic, scalable, and secure. Similarly, demand from the public for SEC information has never been

higher. Last year, www.sec.gov received 10.4 billion page views—double from just two years ago—and the public downloaded more than 2.6 petabytes of data. The information the SEC provides is driving the marketplace, and helping companies attract funding, grow, and create jobs.

All of these shifts require the SEC to expand our own technology capabilities and increase our efficiency. The SEC through its budget requests seeks sufficient resources to stay on top of these critical developments and promote our mission in an evolving landscape. The SEC has made progress in modernizing our technology systems, with the benefits of increasing our use of data analytics, increasing program effectiveness, and streamlining operations. The SEC's IT investment priorities for FY 2018 and beyond include:

- Increasing investments in information security to address, as a top priority, the ability to monitor and protect against advanced persistent threats, and to improve overall risk management and monitoring;
- Expanding data analytics tools to integrate and analyze the large and ever-increasing volume of financial data we receive, enabling us to detect potential fraud or suspicious behavior earlier and allocate resources more effectively;
- Improving our examination program through advanced risk assessment and surveillance tools that help identify high-risk areas for further examination;
- Enhancing systems that support our enforcement program, including applying sophisticated algorithms that foster the detection of potential insider trading and manipulation;
- Streamlining public access to our EDGAR system; and
- Investing further in business process automation and enhancements, including the retirement of legacy systems, which will drive cost efficiencies and improve security across the agency.

Internal Staff Collaboration and Communication. The SEC continues to place a high priority on fostering intra-agency communication and collaboration to facilitate the execution of our mission. There is extensive interaction among divisions and offices for nearly every significant action the SEC undertakes, including rulemakings, enforcement actions, and other policy initiatives. Additionally, there are numerous formal and informal mechanisms for cross-agency coordination, such as intra-agency governance committees and working groups related to operational issues, identification of key risks, technology and data, and more.

In FY 2018, the SEC plans to continue to identify and work on operational improvements that facilitate better communication and collaboration throughout the agency, as well as those that optimize our organizational structure and generate efficiencies and cost savings. We intend to use the results of the most recent FEVS as an indicator to identify potential areas for further improvement.

Covering a Wide-Range of Important Activities with Finite Resources. As highlighted earlier, the SEC's broad mission requires us to cover a lot of ground—from the oversight of securities trading on U.S. equity markets, to the disclosures of public companies, to the activities of registered market participants, and interactions with the investing public including through our www.sec.gov portal. Our ability to execute our mission is inherently dependent upon the SEC obtaining sufficient resources to keep pace with the growing size and complexity of the securities markets and our broad oversight and enforcement responsibilities. The SEC submits an annual budget request which outlines the funding it is seeking and the intended use of such funding. The SEC's funding is deficit-neutral. The appropriation that the SEC receives is fully offset by securities transaction fees and, accordingly, the SEC's funding is not borne by taxpayers. Budgetary constraints will impact the ability of the SEC to fulfill its goals and objectives as outlined in this section.

FINANCIAL HIGHLIGHTS

This section provides an analysis of the financial position, results of operations, and the underlying causes for significant changes in balances presented in the SEC's FY 2017 financial statements.

As described further below, the SEC's finances have several main components:

- An annual appropriation from Congress;
- Securities transaction fees, charged in accordance with Section 31 of the Securities Exchange Act, which offset the agency's annual appropriation;
- Securities registration, tender offer and merger fees (also called filing fees), of which $50 million is deposited into the SEC's Reserve Fund each year. The Reserve Fund may provide resources up to $100 million to pay for SEC expenses, and are not subject to annual appropriation or apportionment;
- Disgorgement and penalties ordered and collected from violators of the securities laws, some of which are then returned to harmed investors and the balances are transferred to the Treasury; and
- The SEC Investor Protection Fund, which is funded through disgorgement and penalties not distributed to harmed investors, and which is used to make payments to whistleblowers who give tips to aid the SEC's enforcement efforts in certain circumstances, as well as to cover the expenses of the SEC's OIG Employee Suggestion Program.

Sequestration Order for FY 2017

On March 1, 2013, the President issued the Sequestration Order for FY 2013, which reduced FY 2013 budget authority.

As determined by the Office of Management and Budget (OMB), for FY 2017, the sequestration order was applicable to mandatory appropriations, which included the Reserve Fund and the Investor Protection Fund, of the SEC as follows:

Reserve Fund

The budget authority of $75 million was reduced by 6.9 percent, or $5.2 million.

Investor Protection Fund

The budget authority of $3.9 million was reduced by 6.9 percent, or $310 thousand.

Rescission for FY 2017

On May 5, 2017, Congress passed the Consolidated Appropriations Act, 2017. Within the appropriation language, a $25 million rescission was applied to the unobligated balance of the Reserve Fund.

Overview of Financial Position

Assets. At September 30, 2017, the SEC's total assets were $10.8 billion, a decrease of $877 million or eight percent below FY 2016.

Fund Balance with Treasury decreased by $125 million between FY 2017 and FY 2016—a result of a decrease in custodial Disgorgement and Penalty cash of $77 million and Salaries and Expenses activity of $60 million.

Accounts Receivable, Net decreased by $663 million due to the collections of Disgorgement and Penalty receivables established prior to FY 2017 for three large cases.

Chart 1.3 | FY 2017 Assets by Type

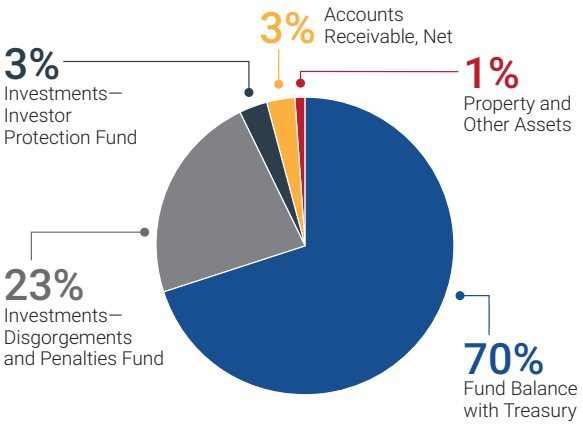


Table 1.2 | Assets as of September 30, 2017 and 2016

(DOLLARS IN MILLIONS)	2017	2016
Fund Balance with Treasury	$ 7,505	$ 7,630
Investments – Disgorgement and Penalty Fund	2,471	2,506
Investments – Investor Protection Fund	292	350
Accounts Receivable, Net	365	1,028
Property and Equipment, Net	131	126
Other Assets	11	12
Total Assets	**$ 10,775**	**$ 11,652**

Liabilities. At September 30, 2017 the SEC's total liabilities were $3.4 billion, a decrease of $569 million or 14 percent below FY 2016.

For the assets received resulting from enforcement judgments, the SEC recognizes a corresponding liability, which is either custodial if the collections are transferred to the U.S. Treasury General Fund or the Investor Protection Fund, or governmental if the collections are held pending distribution to harmed investors.

The decrease of $290 million in Liability for Disgorgement and Penalties reflects the distributions to harmed investors recorded between October 1, 2016 and September 30, 2017.

Custodial Liability decreased $492 million, reflecting a decrease in Disgorgement and Penalty receivables established prior to FY 2017 due to collections on two large cases.

The SEC recognized a contingent liability for the year ended September 30, 2017 of $221 million, which represents a recognized liability for estimated whistleblower awards where the payment is considered probable.

Ending Net Position. The SEC's net position, comprised of both unexpended appropriations and the cumulative results of operations, decreased by $308 million between September 30, 2017 and 2016.

Chart 1.4 | FY 2017 Liabilities by Type

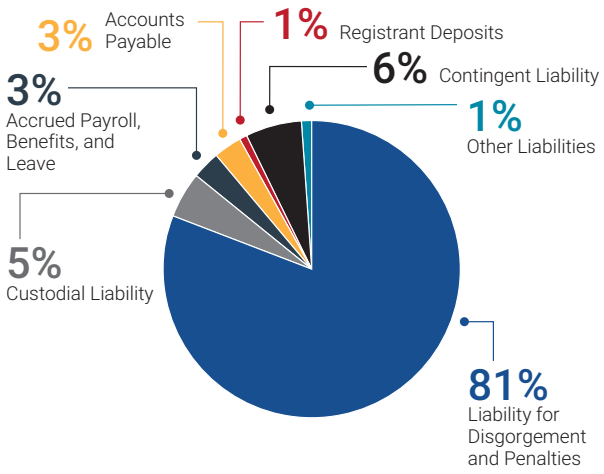


Table 1.3 | Liabilities as of September 30, 2017 and 2016

(DOLLARS IN MILLIONS)	2017	2016
Liability for Disgorgement and Penalties	$ 2,800	$ 3,090
Custodial Liability	174	666
Accrued Payroll, Benefits, and Leave	118	115
Accounts Payable	84	81
Registrant Deposits	34	37
Contingent Liability	221	11
Other Liabilities	15	15
Total Liabilities	**$ 3,446**	**$ 4,015**

Results of Operations

Earned Revenues. Total earned revenues for the year ended September 30, 2017 increased by $164 million, or eight percent above FY 2016.

An increase of $109 million in Section 31 fee revenue is the result of the increase in the Section 31 fee rate of $21.80 per million dollars transacted in effect through June 2017. Beginning in July 2017, the Section 31 fee rate was increased to $23.10 per million dollars transacted.

For the comparable time period, the fee rate in effect was $18.40 per million dollars transacted for the majority of the first half of FY 2016, until it was raised to $21.80 per million dollars transacted in February 2016.

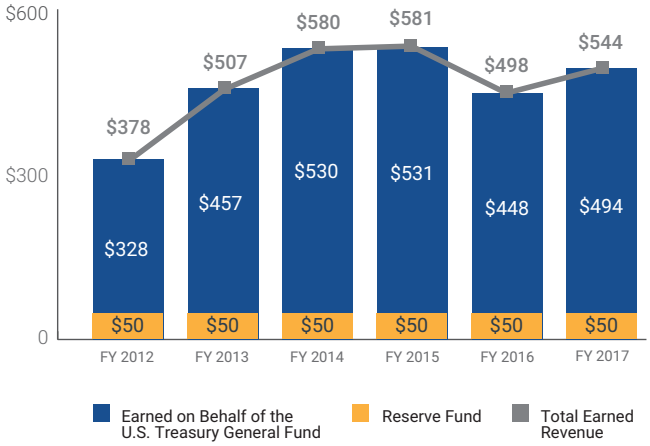
Reserve Fund. Section 991(e) of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank Act) authorized the creation of the SEC's Reserve Fund. Funded from filing fee collections, the SEC can deposit up to $50 million per fiscal year, and the fund cannot hold more than $100 million in total. Excess filing fees are deposited to the U.S. Treasury General Fund.

For the year ended September 30, 2017, filing fee revenues totaled $544 million. Fifty million dollars was deposited into the Reserve Fund, of which $5 million was sequestered. The excess of $494 million was earned on behalf of the U.S. Treasury General Fund.

Table 1.4 | Earned Revenues
For the years ended September 30, 2017 and 2016

(DOLLARS IN MILLIONS)	2017	2016
Section 31 Securities Transaction Fees	$ 1,595	$ 1,486
Securities Registration, Tender Offer, and Merger Fees (Filing Fees)	543	489
Other	1	—
Total Earned Revenues	**$ 2,139**	**$ 1,975**

Chart 1.5 | Reserve Fund Earned Revenue
(DOLLARS IN MILLIONS)



Filing fees deposited to the Reserve Fund can be used to fund the SEC's operations, create budgetary authority, and are reported as a component of Appropriations (Discretionary and Mandatory) on the SEC's Statement of Budgetary Resources. Filing fees deposited to the U.S. Treasury General Fund cannot be used to fund the SEC's operations. These amounts do not create budgetary authority, and are reported as a component of Other Financing Sources: Other on the SEC's Statement of Changes in Net Position.

Reserve Fund resources totaling $52 million were obligated, for the year ended September 30, 2017, for both capitalized and non-capitalized IT related hardware, software, and contracting, leaving a remaining amount of $1 million of available resources.

Program Costs. Total Program Costs were $2.0 billion for the year ended September 30, 2017, an increase of $267 million, or 15 percent, compared to FY 2016. Salary and Benefit Expenses increased more than $42 million, as the result of merit pay compensation and increased benefits including the supplemental retirement program. Other Expenses increased more than $225 million, which includes $202 million in accrued expenses for whistleblower payments from the SEC's Investor Protection Fund, and $23 million in additional expenses for contractual services.

The SEC had increased expenses in the areas of information technology service contracts and licensing; capitalized and non-capitalized information systems software and hardware; and whistleblower award payments.

Chart 1.6 | FY 2017 Filing Fee Revenue

(DOLLARS IN MILLIONS)

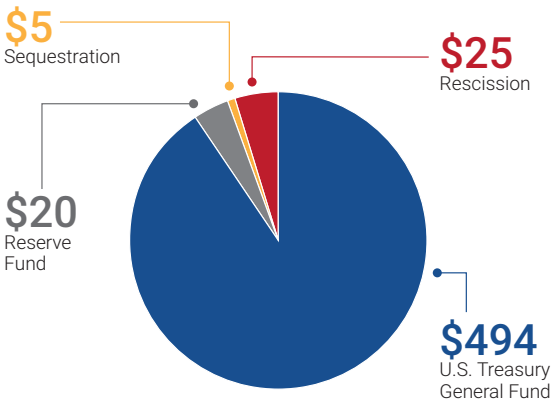
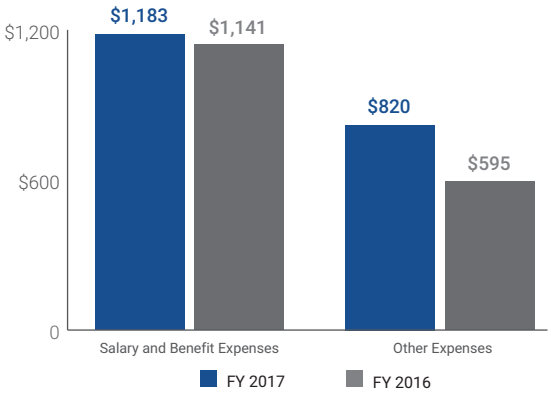


Chart 1.7 | Program Costs

(DOLLARS IN MILLIONS)



Budgetary Resources

In FY 2017, the SEC's total budgetary resources equaled $1.9 billion, a one percent decrease from FY 2016. Significant components of the SEC's Total Budgetary Resources are described below.

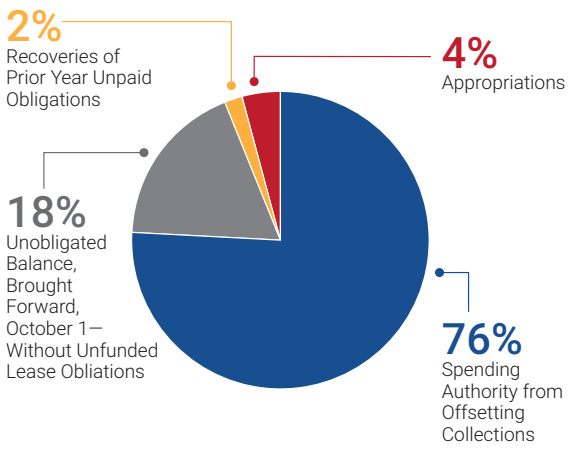
Unobligated Balance Brought Forward—Unfunded Lease Obligations. Unfunded lease obligations totaled $213 million at the beginning of FY 2017. The balance through the year ended September 30, 2017 is $139 million.

Recoveries of Prior Year Obligations. Between September 30, 2017 and 2016, Recoveries of Prior Year Obligations decreased $18 million. The variance is due to a larger volume of recoveries from obligations over $1 million in the previous year.

In FY 2017, the SEC recovered $8 million from four contracts over $1 million in value, compared to recovering $19 million from six contracts over $1 million in FY 2016.

For obligations ranging between $100 thousand and $1 million in value, the SEC recorded deobligations of $23 million in FY 2017, compared to $27 million in FY 2016.

Chart 1.8 | FY 2017 Sources of Funds



Percentages do not include the Unobligated Balance Brought Forward, October 1—Interpretation for Lease Obligations

Table 1.5 | Total Budgetary Resources
For the years ended September 30, 2017 and 2016

(DOLLARS IN MILLIONS)	2017	2016
Unobligated Balance, Brought Forward, October 1:		
Salaries and Expenses Fund—Without Unfunded Lease Obligations	$ 25	$ 51
Salaries and Expenses Fund—Effect of Change in Legal Interpretation for Lease Obligations	(213)	(286)
Investor Protection Fund	340	398
Total Unobligated Balance, Brought Forward, October 1	154	163
Recoveries of Prior Year Unpaid Obligations	39	57
Other Changes in Unobligated Balance (+ or -)	1	2
Appropriations (Discretionary and Mandatory)		
Salaries and Expenses Fund	20	129
Reserve Fund	50	50
Investor Protection Fund	4	1
Spending Authority from Offsetting Collections	1,587	1,477
Total Budgetary Resources	**$ 1,855**	**$ 1,879**

Spending Authority from Offsetting Collections and Appropriations

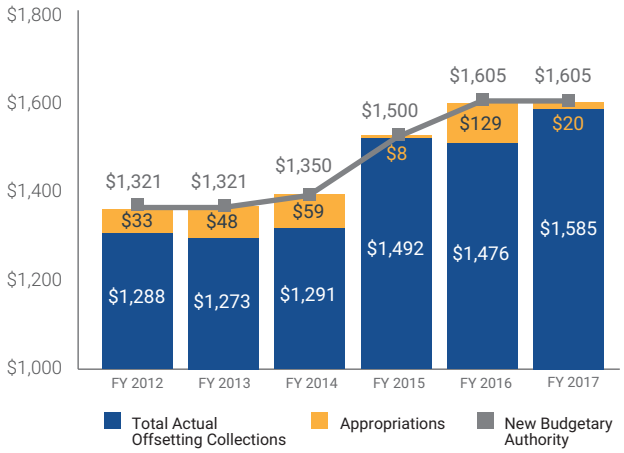
During the fiscal year, the SEC receives an appropriation to fund its operations. This appropriation establishes the SEC's new budget authority in its Salaries and Expenses Fund for the fiscal year. The SEC's new budget authority of $1,605 million was for FY 2017.

The SEC's Section 31 fee collections are used to offset the appropriation, and as the collections come in, the appropriated authority is returned to the U.S. Treasury General Fund.

For the year ended September 30, 2017, appropriations was $20 million, the difference between appropriations legislated and offsetting collections.

In FY 2016, the SEC In FY 2016, the SEC received a $1,605 million appropriation, offset by collections of $1,476 million. In FY 2017, the SEC's appropriation was $1,605 million, which was offset by $1,585 million in collections.

Chart 1.9 | Offsetting Collections vs. New Budgetary Authority
Section 31 Exchange and Filing Fees
(DOLLARS IN MILLIONS)



Investor Protection Fund

The SEC prepares stand alone financial statements for the Investor Protection Fund as required by the Dodd-Frank Act. The Fund was established in FY 2010 to provide funding for a whistleblower award program and to finance the operations of the SEC OIG's Employee Suggestion Program.

For FY 2017, the balance of the Investor Protection Fund decreased by $46 million between October 1, 2016 and September 30, 2017.

The Fund recognized non-exchange revenues totaling $3 million, from interest earned on investments in U.S. Treasury Securities. In addition, the Investor Protection Fund disbursed payments of $49 million for whistleblower awards and employee related expenses.

Limitations of the Financial Statements

The principal financial statements are prepared to report the financial position and results of operations of the reporting entity, pursuant to the requirements of 31 U.S.C. § 3515(b).The statements are prepared from the books and records of the entity in accordance with federal GAAP and the formats prescribed by OMB. Reports used to monitor and control budgetary resources are prepared from the same books and records. The financial statements should be read with the realization that they are for a component of the U.S. Government.

Table 1.6 | Investor Protection Fund Activity
For the years ended September 30, 2017 and 2016

(DOLLARS IN MILLIONS)	2017	2016
Balance of Fund at beginning of fiscal year, October 1	$ 368	$ 401
Amount of earnings on investments during the fiscal year	3	2
Amount paid from the Fund during the fiscal year to whistleblowers	(49)	(35)
Balance of the Fund at the end of the reporting period	**$ 322**	**$ 368**

PERFORMANCE HIGHLIGHTS

The SEC's performance data provides a foundation for both programmatic and organizational decision-making and is critical for gauging the agency's success in meeting its objectives. The SEC is committed to using performance management best practices to promote greater accountability. This section provides information on its key performance measures for FY 2017. It outlines the SEC's strategic and performance planning framework, provides information on the costs incurred by the agency's four strategic goals and 10 national programs, and highlights the agency's progress toward reaching key performance targets.

The SEC's FY 2017 Annual Performance Report (APR) will be issued with the agency's FY 2019 Congressional Budget Justification, and will provide a complete discussion of all of the agency's strategic goals, including a description of performance goals and objectives, data sources, performance results and trends, and information about internal reviews and evaluations. The summary presented below of the SEC's verification and validation of all performance data also will be included in the APR. The SEC's APR is expected to be available in 2018 at www.sec.gov/about/secreports.shtml.

Verification and Validation of Performance Data

The SEC's programs require accurate data to properly assess program performance and make sound management decisions. To ensure data is correct, a system of data verification and validation is used. Data verification is a systematic process for evaluating a set of data against a set of standards to ascertain its completeness, correctness, and consistency using the methods and criteria defined in the project documentation. Data validation follows the data verification process in an effort to ensure that performance data are free of systematic error or bias, and that what is intended to be measured is actually measured. Together, these processes are used to evaluate whether the information has been generated according to specifications, satisfies acceptance criteria, and is appropriate and consistent with its intended use.

Below is a list of steps taken to ensure the performance data presented in this report is complete, reliable, and accurate.

1. The agency develops performance goals through its strategic planning process.
2. The SEC's divisions and offices provide:
   - The procedures used to obtain assurance as to the accuracy and reliability of the data;
   - The data definitions for reference;
   - Documentation and explanation of the performance goal calculations; and
   - The sources of the underlying data elements.
3. The divisions and offices calculate and report the performance goals to the Office of Financial Management, and the performance goals are approved by the division directors and office heads. This process ensures that the data used in the calculation of performance goals is accurate and reliable, and that internal control is maintained throughout the approval process.

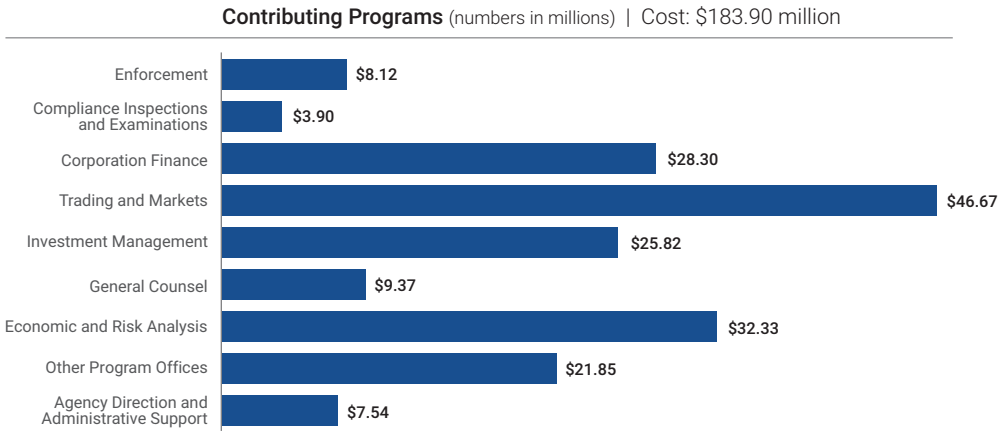
Strategic and Performance Planning Framework

The SEC's FY 2017 strategic and performance planning framework is based on the FY 2014–FY 2018 Strategic Plan, available at www.sec.gov/about/sec-strategic-plan-2014-2018.pdf. The Strategic Plan outlines the agency's mission, vision, values, strategic goals, and strategic objectives. The SEC's work is structured around four strategic goals, as well as 12 strategic objectives the agency plans to achieve in support of those four goals. The SEC's goals and priorities in the Strategic Plan are influenced by several external environmental factors, including global, complex, and constantly evolving securities markets.

Chart 1.10 displays the agency's FY 2017 costs for its four strategic goals and how these costs are divided among the SEC's programs, as previously described in Table 1.1.

Chart 1.10 | FY 2017 Strategic Goals with Contributing Program Costs ($ in millions)

STRATEGIC GOAL 1: Establish and maintain an effective regulatory environment



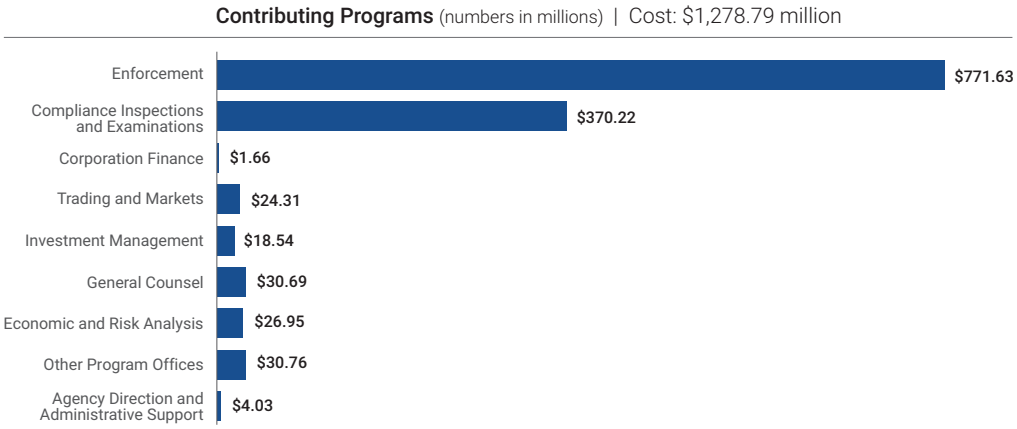
Strategic Objective 1.1: The SEC establishes and maintains a regulatory environment that promotes high-quality disclosure, financial reporting, and governance, and that prevents abusive practices by registrants, financial intermediaries, and other market participants.

Strategic Objective 1.2: The SEC promotes capital markets that operate in a fair, efficient, transparent, and competitive manner, fostering capital formation and useful innovation.

Strategic Objective 1.3: The SEC adopts and administers regulations and rules that are informed by robust economic analysis and public comment and that enable market participants to understand clearly their obligations under the securities laws.

Strategic Objective 1.4: The SEC engages with a multitude of stakeholders to inform and enhance regulatory activities domestically and internationally.

STRATEGIC GOAL 2: Foster and enforce compliance with the federal securities laws



Strategic Objective 2.1: The SEC fosters compliance with the federal securities laws.

Strategic Objective 2.2: The SEC promptly detects and deters violations of the federal securities laws.

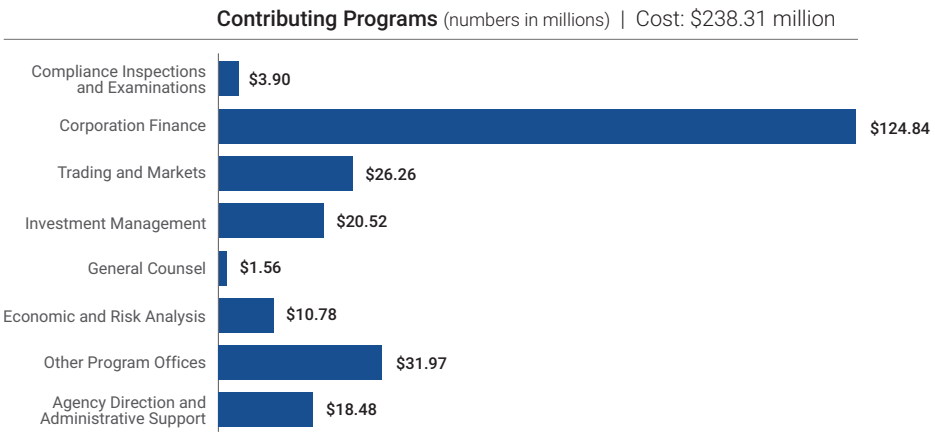
Strategic Objective 2.3: The SEC prosecutes violations of federal securities laws and holds violators accountable through appropriate sanctions and remedies.

Chart 1.10 | *Continued from previous page*

STRATEGIC GOAL 3: Facilitate access to the information investors need to make informed investment decisions

Strategic Objective 3.1: The SEC works to ensure that investors have access to high-quality disclosure materials that facilitate informed investment decision-making.

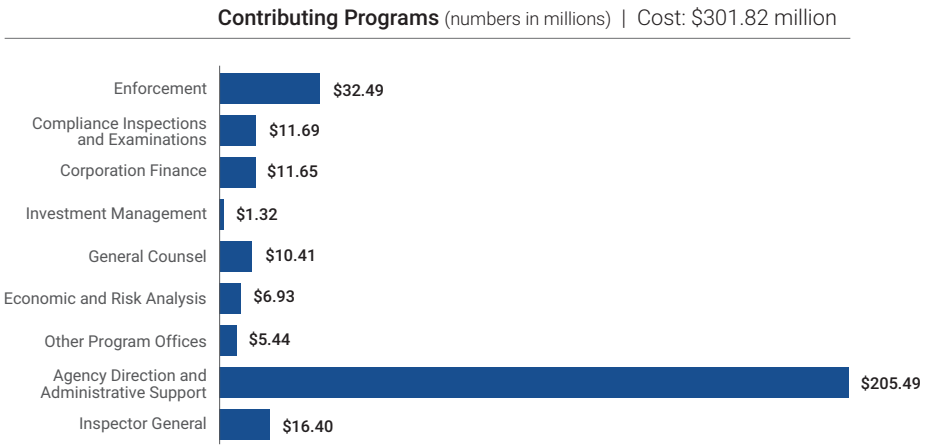
Strategic Objective 3.2: The SEC works to understand investor needs and educate investors so they are better prepared to make informed investment decisions.



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

Strategic Objective 4.1: The SEC promotes a results-oriented work environment that attracts, engages, and retains a technically proficient and diverse workforce, including leaders who provide motivation and strategic direction.

Strategic Objective 4.2: The SEC encourages a collaborative environment across divisions and offices and leverages technology and data to fulfill its mission more effectively and efficiently.



Strategic Objective 4.3: The SEC maximizes the use of agency resources by continually improving agency operations and bolstering internal controls.

The SEC expended about $2.0 billion in FY 2017 to achieve its four strategic goals and 12 strategic objectives. The agency's APR will provide a complete explanation of how many planned performance goal targets were exceeded, met, and not met. Where the agency met or exceeded its planned performance targets, the report will provide a discussion of the increased efficiencies and improved processes employed by the agency. When a planned performance target was not met, the report will provide a description of actions that will be taken to achieve the target in the future.

Performance Achievements

Strengthening and continuing focused examination coverage of the industry helps the Commission promptly detect violations of federal securities laws and promote compliance with such laws (Strategic Objective 2.2). During FY 2017, the examination program met or exceeded its coverage targets. The program concentrated particular efforts in the investment adviser space and was able to improve coverage beyond targeted levels. The SEC continued to exert considerable time and attention during the year on enhancing its risk assessment efforts to ensure that the program is spending its limited time and resources on those activities and firms presenting the highest risk.

Table 1.7

PERFORMANCE GOAL 2.2.1
Percentage of investment advisers, investment companies, and broker-dealers examined during the year

Description: This metric indicates the number of registrants examined by the SEC or an SRO as a percentage of the total number of registrants. This metric includes all types of examinations: risk priority examinations, cause inspections to follow up on tips and complaints, limited-scope special inspections to probe emerging risk areas, and oversight examinations of broker-dealers to test compliance and the quality of examinations by FINRA.

Fiscal Year	FY 2012	FY 2013	FY 2014	FY 2015	FY 2016	FY 2017 Plan	FY 2017 Actual	FY 2017 Results
Investment advisers	8%	9%	10%	10%	11%	13%	15%	Exceeded
Investment companies	12%	11%	10%	15%	17%	10%	11%	Exceeded
Broker-dealers (exams by SEC and SROs)	49%	46%	49%	51%	50%	48%	48%	Met

Responsible Division/Office: Office of Compliance Inspections and Examinations

Data Source: Tracking and Reporting Exam National Documentation System (TRENDS) (investment adviser [IA], investment company [IC], and broker-dealer [BD] SEC data) and SRO Databases (BD self-regulatory organization [SRO] Data)

Enforcement's litigation efforts help the SEC obtain appropriate settlements in other cases by demonstrating that it will pursue litigation and trial, if necessary, to obtain appropriate relief (Strategic Objective 2.3). The SEC endeavors to resolve actions quickly and on a favorable basis where practicable, while at the same time filing contested matters where favorable settlements are unavailable before filing. The agency seeks to direct its limited resources toward cases that are likely to have the greatest impact in furthering the SEC's mission.

Table 1.8

PERFORMANCE GOAL 2.3.1
Percentage of enforcement actions in which the Commission obtained relief on one or more claims

Description: This metric identifies, as to all parties to enforcement actions that were resolved in the fiscal year, the percentage against whom the Commission obtained a judgment or order entered on consent, a default judgment, a judgment of liability on one or more charges, and/or the imposition of monetary or other relief.

Fiscal Year	FY 2012	FY 2013	FY 2014	FY 2015	FY 2016	FY 2017 Plan	FY 2017 Actual	FY 2017 Results
Percentage	89%	93%	94%	95%	97%	92%	94%	Exceeded

Responsible Division/Office: Division of Enforcement

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

The federal securities laws place great emphasis on ensuring that corporations, investment companies, and other entities provide investors with timely, clear, complete, and accurate financial and non-financial information, allowing investors to make wise investment decisions (Strategic Objective 3.1). The SEC understands the purpose of company disclosure is to provide investors the information they need to make informed investment and voting decisions. Consistent with Section 408 of the Sarbanes-Oxley Act of 2002, the SEC completed its review of disclosures made by certain public issuers, including issuers' financial statements, no less frequently than once every three years (Performance Goal 3.1.1).

Table 1.9

PERFORMANCE GOAL 3.1.1
Percentage of public companies and investment companies with disclosures reviewed each year

Description: The Sarbanes-Oxley Act requires that the SEC review, at least once every three years, the disclosures of all companies and investment company portfolios reporting under the Exchange Act. These reviews help improve the information available to investors and may identify possible violations of the federal securities laws. This metric gauges the number of public companies and investment companies reviewed each year.

Fiscal Year	FY 2012	FY 2013	FY 2014	FY 2015	FY 2016	FY 2017 Plan	FY 2017 Actual	FY 2017 Results
Division of Investment Management								
Investment company portfolios	36%	34%	35%	35%	36%	33%	35%	Exceeded
Responsible Division/Office: Division of Investment Management								
Data Source: Microsoft Office Suite Tools								
Division of Corporation Finance								
Corporations	48%	52%	52%	51%	56%	33%	56%	Exceeded
Responsible Division/Office: Division of Corporation Finance								
Data Source: Electronic Data Gathering, Analysis, and Retrieval (EDGAR)/Filing Activity Tracking System (FACTS)								

The SEC continued to address investor needs and educate investors to prepare investors to make informed investment decisions (Strategic Objective 3.2). Specifically, the Office of Investor Education and Advocacy (OIEA) implemented technical changes in FY 2016 to help users navigate SEC online investor education content more efficiently, resulting in fewer site page views. As a result, the target for FY 2017 was changed from 37.5 million to eight million page views. In FY 2017, a record 2.2 million new users visiting Investor.gov helped the SEC exceed its goal of page views of online investor education content. OIEA exceeded its target for in-person events by identifying dozens of new outreach opportunities, many of which focused on military personnel and their families as part of its Military Financial Literacy Campaign.

Table 1.10

PERFORMANCE GOAL 3.2.1
Number of page views of online investor education content and number of in-person events, including those with specifically-targeted communities and organizations

Description: The Office of Investor Education and Advocacy (OIEA) initiates investor education campaigns on key strategies for making informed investment decisions, including publicizing online resources for researching investment professionals and investments, understanding fees, and identifying fraud. OIEA staff also participates in in-person events for investors, both general and those targeted toward specific investors such as seniors, service members, and other affinity groups. This metric tracks page views of SEC online investor education materials and the number of investor events in which OIEA staff participated.

Fiscal Year	FY 2012	FY 2013	FY 2014	FY 2015	FY 2016	FY 2017 Plan	FY 2017 Actual	FY 2017 Results
Number of page views (in millions)	Prior-year data not available	12.1	22.2	23.6	23.7	8	9.1	Exceeded
Number of in-person events	Prior-year data not available	52	51	71	112	80	146	Exceeded

Responsible Division/Office: Office of Investor Education and Advocacy

Data Source: Google Analytics, Microsoft Office Suite Tools

The SEC employees are the most important asset of the agency. In FY 2017, the SEC continued to foster a work environment that attracts, engages, and retains a technically proficient and diverse workforce (Strategic Objective 4.1). Specifically, the Federal Employee Viewpoint Survey (FEVS) results demonstrate continued improvement in some of the most important drivers of employee engagement and organizational health. The SEC ranked among the top four highest scores in each of the indices among all medium-sized agencies in the federal government. In the Employee Engagement Index, the SEC was the third highest and tied for the largest increase from 2016 among all medium-sized federal agencies. In the Global Satisfaction Index, the SEC positive score was the highest score among all medium-sized agencies. Based on the 2017 FEVS results for the Global Satisfaction Index, the agency expects to improve on the 6th place ranking from 2016. The *Best Places to Work* rankings will be announced in December of 2017.

Table 1.11

PERFORMANCE GOAL 4.1.4
Survey rankings

Description: Annual and other rankings, together with other metrics and indicators of federal government agencies, is one type of metric that will be used to determine the SEC's overall success in improving employee morale and employee engagement.

Fiscal Year	FY 2012	FY 2013	FY 2014	FY 2015	FY 2016	FY 2017 Plan	FY 2017 Actual	FY 2017 Results
Best Places to Work ranking	Ranked # 19	Ranked # 15	Ranked # 14	Ranked # 10	Ranked # 6	Ranked # 5	Will be released in Dec 2017	N/A
Average of Employee Engagement and Global Satisfaction Index	Prior-year data not available	61%	66%	68%	75%	75%	79%	Exceeded

Responsible Division/Office: Office of Human Resources

Data Source: Annual Partnership for Public Service calculated ranking based on Annual Employee Viewpoint Survey (EVS) administered by OPM and Average of Employee Engagement and Global Satisfaction Index from OPM EVS

MANAGEMENT ASSURANCES AND COMPLIANCE WITH LAWS

In FY 2017, the SEC demonstrated its continued commitment to maintaining strong internal controls. Internal control is an integral component of effective agency management, providing reasonable assurance that the following objectives are being achieved: effectiveness and efficiency of operations, reliability of reporting, and compliance with laws and regulations. The Federal Managers' Financial Integrity Act of 1982 (FMFIA) establishes management's responsibility to assess and report on internal accounting and administrative controls. Such controls include program, operational, and administrative areas, as well as accounting and financial management. The FMFIA requires federal agencies to establish controls that reasonably ensure obligations and costs are in compliance with applicable laws; funds, property, and other assets are safeguarded against waste, loss, unauthorized use, or misappropriation; and revenues and expenditures are properly recorded and accounted for to maintain accountability over the assets. The FMFIA also requires agencies to annually assess whether financial management systems conform to related requirements (FMFIA § 4). Guidance for implementing the FMFIA is provided through Office of Management and Budget (OMB) Circular A-123, *Management's Responsibility for Enterprise Risk Management and Internal Control*.

Section 963 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank Act) describes the responsibility of SEC management to establish and maintain adequate internal controls and procedures for financial reporting. This section requires an annual financial controls audit, a Government Accountability Office (GAO) audit of the SEC's assessment of the effectiveness of internal control, and attestation by the Chairman and the chief financial officer (CFO). Section 922 of the Dodd-Frank Act requires the SEC to submit audited financial statements of the Investor Protection Fund to the Senate Committee on Banking, Housing, and Urban Affairs, and the House of Representative Committee on Financial Services. The following Assurance Statement is issued in accordance with the FMFIA, OMB Circular A-123, and Sections 963 and 922 of the Dodd-Frank Act.

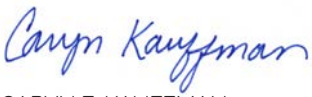
Annual Assurance Statement

Assurance Statement on Internal Control Over Operations: The SEC management is responsible for establishing and maintaining effective internal control that meets the objectives of the Federal Managers' Financial Integrity Act of 1982 (FMFIA). In accordance with OMB Circular A-123, *Management's Responsibility for Enterprise Risk Management and Internal Control*, the SEC conducted its annual assessment of the effectiveness of internal controls. Based on the results of this evaluation, internal controls over financial reporting were found to be effective as of September 30, 2017. One material weakness related to cybersecurity risks was identified in internal control over the effectiveness and efficiency of operations as of September 30, 2017. Other than the one material weakness described within this section, the internal controls were operating effectively.

Assurance Statement on Internal Control Over Financial Reporting (ICFR): In accordance with OMB Circular A-123 Appendix A, *Internal Control Over Reporting*, the SEC conducted its assessment of the effectiveness of internal control over financial reporting, which includes safeguarding of assets and compliance with applicable laws and regulations. Based on the results of the assessment, the SEC is able to provide reasonable assurance that the internal controls over financial reporting, both for the agency as a whole and for the Investor Protection Fund, met the objectives of FMFIA and were operating effectively as of September 30, 2017. No material weaknesses were found in the design or operation of controls.

SEC also conducted reviews of its financial management systems in accordance with OMB Circular A-123 Appendix D, *Compliance with the Federal Financial Management Improvement Act*. Based on the results of these reviews, SEC can provide reasonable assurance that its financial management systems substantially comply with the requirements of the FFMIA as of September 30, 2017.

JAY CLAYTON
Chairman
November 9, 2017



CARYN E. KAUFFMAN
Acting Chief Financial Officer
November 9, 2017

Management's Assessment of Internal Control

The assurance statements are based on reports from each division director and office head on the effectiveness of their controls. These statements were based on self-assessments and internal reviews supported by control testing, as well as recommendations for improvement from audits, investigations, and reviews conducted internally by the SEC Office of Inspector General (OIG) and GAO.

The FY 2017 Chairman and Acting CFO's annual assurance statements for FMFIA and internal controls over reporting provided reasonable assurance that the necessary objectives (effective and efficient operations, compliance with applicable laws and regulations, and reliability of reporting) are achieved.

The results of these statements were considered with other sources of information that included, but were not limited to, the following:

- An entity-level control assessment;
- A fraud risk assessment;
- Internal management reviews, self-assessments, and tests of internal controls;
- Management's personal knowledge gained from daily operations;
- Reports from GAO and the OIG;
- Reviews of financial management systems under OMB Circular A-123 Appendix D, *Compliance with the Federal Financial Management Improvement Act of 1996*;
- Reports pursuant to the Federal Information Security Management Act (FISMA) and OMB Circular A-130, *Management of Federal Information Resources*;
- Reviews on improper payments;
- Reports and other information from Congress or agencies such as OMB, the Office of Personnel Management, and/or the General Services Administration reflecting the adequacy of internal controls; and
- Additional reviews relating to a division or office's operations.

With respect to internal controls over financial reporting, the SEC performed a comprehensive risk assessment. The agency documented its key controls to address risks, and then assessed the design and operating effectiveness of these controls through detailed test procedures. The agency also tested the operating effectiveness of control activities that were found to be deficient in prior years. SEC management analyzed the magnitude of internal control deficiencies, both individually and in the aggregate, to determine if a material weakness existed in the financial reporting processes.

Taking into account the assurance statements from directors and office heads, the supplemental sources of information as described above, and the results of the assessment of internal controls over financial reporting, the agency established the Financial Management Oversight Committee. This committee advises the Chairman as to whether the SEC had any deficiencies in internal control or financial system design significant enough to be reported as a material weakness or unmodified, modified, or no assurance.

Material Weakness Related to Cybersecurity Risks

The management assessment of the EDGAR cyber intrusion disclosed in Chairman Clayton's September 2017 press release and public statement highlighted a deficiency in particular controls within the SEC's

information technology entity level controls. The reviews of the EDGAR intrusion by SEC management and the SEC's Office of Inspector General are ongoing and will take substantial time to complete. The cyber intrusion reflected a deficiency in the SEC's ability to detect and mitigate vulnerabilities in the EDGAR application in a timely manner. Specifically, the incident revealed that EDGAR system security reviews and monitoring for potential security anomalies were not consistently implemented. The intrusion also highlighted that formalized protocols were not effective in communicating information for use by management to address cybersecurity risks. Responsibilities for communications did not adequately prescribe the conditions and structure for internal reporting and escalation. Additional formalized procedures are needed to appropriately and quickly inform management, and allow cyber risks to be promptly identified and addressed. Taken together, these two deficiencies represent a material weakness in the agency's internal control system over operations.

As noted above, reviews of the EDGAR intrusion are still ongoing. While these reviews are underway, the agency is proactively working to address and mitigate these deficiencies in FY 2018, which includes taking steps to improve communication and escalation protocols and enhance the information security of the EDGAR system.

This report provides a Summary of Financial Statement Audits and Management Assurances under the section entitled Other Information, as required by OMB Circular A-136, *Financial Reporting Requirements*.

Other Reviews

Fraud Reduction Report

The Fraud Reduction and Data Analytics Act of 2015 (Pub. L. 114-186, 31 U.S.C. 3321 note) requires agencies to implement the GAO's *A Framework to Managing Fraud Risks in Federal Programs*. The GAO framework identifies four steps that agencies should follow: 1) commit to creating an organization that is conductive to manage fraud risk; 2) assess the fraud risks within the organization; 3) design and implement controls that reduce risk of fraud; and 4) evaluate and adapt assessment outcomes. The SEC's approach to managing fraud risk starts with a strong tone at the top. This includes messaging from senior officials regarding the importance of a culture committed to a high level of integrity and resources dedicated to ensuring that ethics training is provided annually to all employees. The SEC leverages its Risk Management Oversight Committee, which consists of senior executives from divisions/offices throughout the SEC who oversee the Commission's efforts to assess, address, and report on identified fraud risks.

The SEC has established a system of internal controls to support effective and efficient operations that also helps to mitigate the risk of fraud. Such controls, which overlay formal policies and procedures, typically deal with factors such as approval and authorization processes, access restrictions and transaction controls, account reconciliations, and physical security. These procedures often include the division of responsibilities and checks and balances to reduce risk. To the extent that these controls affect financial reporting, they are reviewed and tested by management on an annual basis. Controls that do not impact financial reporting are reviewed annually and tested on a rotational basis based upon risk as part of the Commission's management assurance attestation. While strong internal controls help to mitigate the risk of fraud, employees are strongly encouraged to speak with management or the OIG should they suspect instances of fraud.

Analysis of results from testing performed and the overall business environment can lead to additional training opportunities for which there is a heightened risk of fraud. For example, over the past year, SEC

management developed and provided training to contracting officers and contracting officer representatives around the potential for fraud in the area of procurement. The OIG provided a block of instruction during training. Management recognizes that the assessment of fraud is an ongoing process and that mitigation strategies need to change as business processes and the overall environment evolve.

Improper Payments Information Act

The Improper Payments Information Act of 2002, as amended by the Improper Payments Elimination and Recovery Act of 2010, the Improper Payments Elimination and Recovery Improvement Act of 2012, and the Federal Improper Payments Coordination Act of 2015, requires agencies to review all programs and activities they administer and identify those which may be susceptible to significant erroneous payments. For all programs and activities in which the risk of erroneous payments is significant, agencies are to estimate the annual amount of erroneous payments made in those programs. The SEC's risk assessments have consistently indicated that none of the SEC's programs are susceptible to significant improper payments. Therefore, per OMB guidelines, SEC does not need to conduct another risk assessment until FY 2019. The SEC will be required to perform another risk assessment sooner, if a program has a significant change in legislation and/or a significant increase in its funding.

Financial Management System Conformance

The FFMIA requires that each agency implement and maintain financial management systems that comply substantially with federal financial management systems requirements, applicable federal accounting standards, and the U.S. Standard General Ledger at the transaction level. The purpose of the FFMIA is to advance federal financial management by verifying that financial management systems provide accurate, reliable, and timely financial management information in order to manage daily operations, produce reliable financial statements, maintain effective internal control, and comply with legal and regulatory requirements. Although the SEC is exempt from the requirement to determine substantial compliance with the FFMIA, the agency assesses its financial management systems annually for conformance with the requirements of OMB Circular A-123, Appendix D, and other federal financial system requirements.

Summary of Current Financial System and Future Strategies

The FY 2017 assessment demonstrated that a low risk rating would be appropriate, and that the agency substantially complied with the requirements of Section 803(a) of the FFMIA. The SEC's financial system, Delphi, is supported by an approved Federal Shared Service Provider (FSSP) and meets all of the requirements of the FFMIA.

In FY 2017, the SEC continued to work with its FSSP, the Department of Transportation's Enterprise Services Center, to enhance its existing systems and implement additional financial and mixed systems. For example, the SEC made significant progress by implementing two new applications in FY 2017, the EDGAR Filing System Modernization tool and the Financial Data Allocation Platform. SEC is continuing to improve efficiencies with the project to create a new Disgorgements and Penalties System. This project is on-track and scheduled for implementation in FY 2019. The SEC believes that continuing to invest in technology-based solutions will help to put its controls on a more sustainable path.

Federal Information Security Modernization Act (FISMA)

FISMA requires federal agencies to "develop, document, and implement an agency-wide information security program to provide information security for the information and information systems that support

the operations and assets of the agency, including those provided or managed by another agency, contractor, or other source." In addition, FISMA requires federal agencies to conduct annual assessments of their information security and privacy programs, to develop and implement remediation efforts for identified weaknesses and vulnerabilities, and to report compliance to OMB. The SEC's OIG, chief information security officer, and senior agency official for privacy perform a joint review of the Commission's compliance with FISMA requirements each year. The Commission submitted its FY 2017 report to OMB on October 31, 2017.

Oversight and Compliance

The SEC's Office of Information Technology (OIT), in partnership with business owners, completed assessment and authorization activities for 29 FISMA reportable systems. OIT completed an annual enterprise disaster recovery exercise and two additional recovery exercises for major information systems. OIT also conducted two incident response exercises. OIT facilitated the remediation of over 201 self-identified deficiencies that consist of Plans of Action and Milestones (POA&Ms) associated with the SEC's assessments of its network infrastructure and major applications, as well as recommendations issued by the OIG and the GAO that were open at the beginning of FY 2017. At the beginning of FY 2017, OIT had successfully closed all open prior-year OIG recommendations and was actively managing 11 prior-year recommendations from GAO. As of September 30, 2017, OIT had submitted corrective actions for 39 of 43 new recommendations issued in FY 2017.

OIT conducted 301 privacy reviews for information collections in accordance with the Paperwork Reduction Act, new and updated information technology systems, and SharePoint collaboration sites. Because of the privacy reviews, OIT conducted and published four Privacy Impact Assessments.

Training and Communications

OIT developed and delivered Privacy and Information Security Awareness training for all SEC employees and contractors, and achieved 99 percent compliance. Network restrictions were placed on personnel who failed to complete training. In August 2016, OIT launched a privacy awareness campaign focused on safeguarding personally identifiable information (PII). The "PII Tips" were displayed via the agency's digital display monitors during the first two weeks of each month and offered practical methods for protecting PII at home and in the office. In addition, OIT provided in-person privacy training during Telework Week aimed toward the safe handling of PII when teleworking. In the month of July, OIT organized and hosted a Privacy Incident Response Team tabletop exercise to improve the efficiency and effectiveness of the SEC's capabilities to respond to a high-impact breach.

Governance and Technology

On September 20, 2017, the Chairman released a cybersecurity statement that, among other things, disclosed a previously-identified security incident was recently determined to have resulted in access to nonpublic information. As a result, OIT is supporting the Chairman's efforts to improve interagency collaboration around cybersecurity risk, increase awareness on the types and nature of all data the agency maintains within its information systems, and implement business process enhancements to external-facing systems, including EDGAR.

OIT updated the agency's Privacy and Security Policy for its external website, www.sec.gov, to ensure that the policy provided notice rights under the Privacy Act for covered persons pursuant to Judicial Redress Act of 2015. Also, OIT completed the bi-annual review of its privacy-related policies, which resulted in the approval and publishing of the agency's new, Breach Response Plan policy in accordance with OMB Memorandum,

M-17-12, *Preparing for and Responding to a Breach of Personally Identifiable Information*, and the reissuance of three additional privacy-related policies. In addition, OIT implemented a privacy continuous monitoring strategy and developed a comprehensive privacy program plan pursuant to new OMB privacy policy requirements.

OIT continues updating governance documentation to be consistent with OMB policy and NIST guidance. OIT continues to enhance its operational security capabilities though the continued development of an Information Security Continuous Monitoring Program and the continued investment and implementation of proactive security capabilities and detection mechanisms as well as numerous application and database security and vulnerability assessment tools. In support of the Continuous Monitoring (CM) Program, OIT deployed an integrated information security compliance management capability using a tool recommended by the Department of Homeland Security (DHS), RSA Archer, to serve as a centralized repository for the management of the Commission's FISMA compliance obligations, information system POA&Ms, and incident tracking and response efforts. The SEC is well positioned to continue the transition to CM and is an active participant in interagency cybersecurity initiatives, many of which are led by DHS. The SEC continues to safely explore cloud computing technologies and solutions based on federal information protection requirements. The SEC leveraged six cloud service providers that have been through the Federal Risk and Authorization Management Program and is exploring opportunities to leverage additional cloud service providers in accordance with emerging agency objectives.

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Treasurer of the United States.
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FINANCIAL SECTION

This section contains the SEC's financial statements and additional information for FYs 2017 and 2016. Information presented here satisfies the financial reporting requirements of the Accountability of Tax Dollars Act of 2002 and Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank Act). The SEC prepares these statements and accompanying notes in compliance with U.S. generally accepted accounting principles for the federal government and OMB Circular A-136, *Financial Reporting Requirements*.

SEC Financial Statements

Balance Sheets

Presents, as of a specific time, the amount of resources that embody economic benefits or services owned or managed by the SEC (assets); amounts owed by the SEC (liabilities); and amounts that comprise the difference (net position).

Statements of Net Cost

Presents the gross cost incurred by the SEC, less exchange revenue earned from its activities. The SEC presents cost of operations by program to provide cost information at the program level, and recognizes collections as exchange revenue on the Statement of Net Cost, even when the collections are transferred to other entities.

Statements of Changes in Net Position

Reports the change in net position during the reporting period, including changes to Cumulative Results of Operations and Unexpended Appropriations.

Statements of Budgetary Resources[1]

Provides information about how budgetary resources were made available, and reports their status at year-end.

Statements of Custodial Activity

Reports the collection of revenue for the Treasury General Fund. The SEC accounts for sources and disposition of the collections as custodial activities on this statement. Custodial collections of non-exchange revenue, such as amounts collected from violators of securities laws as a result of enforcement proceedings, are reported only on the Statement of Custodial Activity.

Accompanying Notes to the Financial Statements

Provides a description of significant accounting policies and detailed information on select statement line items.

Required Supplementary Information (Unaudited)[2]

Reports the Combining Statements of Budgetary Resources by fund account.

Investor Protection Fund Financial Statements

Investor Protection Fund Financial Statements

Provides stand-alone, comparative financial statements (Balance Sheets, Statements of Net Cost, Statements of Changes in Net Position, and Statements of Budgetary Resources), as required by the Dodd-Frank Act.

Accompanying Notes to the Investor Protection Fund Financial Statements

Provides a description of significant accounting policies and detailed information on select statement line items, as required by the Dodd-Frank Act.

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[1] Budgetary information aggregated for purposes of the Statement of Budgetary Resources is disaggregated for each of the SEC's major budget accounts and is presented as Required Supplementary Information.

[2] The SEC does not have stewardship over resources or responsibilities for which supplementary stewardship reporting would be required.

MESSAGE FROM THE ACTING CHIEF FINANCIAL OFFICER

I am pleased to join Chairman Clayton in presenting the SEC's Agency Financial Report (AFR) for FY 2017. The AFR provides program, performance, and financial information that demonstrates our approach to sound management.

Our independent auditor, the U.S. Government Accountability Office (GAO), released an unmodified opinion of our financial statements and internal controls over financial reporting in which no significant issues were identified. This sustained achievement underscores our commitment to sound financial management and our high standards of accountability, transparency, and ethics. Given the SEC's role of protecting investors and maintaining efficient and transparent markets, we understand the need for accountability, the obligation to operate effective and efficient programs, and that sound financial management is a cornerstone of program performance.

We continually strive for strong internal controls to improve data quality and reporting, and recognize they are critical to effective execution. In FY 2017, the SEC continued to strengthen its efficiency in operations and improve its operational performance. There are many positive achievements to highlight from the past year, some of which are listed below.

- Implementing the EDGAR Fee System Modernization, which replaced the legacy system that previously supported the SEC's management of registration fees.
- Implementing the Budget Formulation and Execution Manager, a shared-service offering of the Bureau of the Fiscal Service, to replace the SEC's legacy system for budget formulation and add capabilities for tracking the agency's strategic performance metrics.
- Implementing the Digital Accountability and Transparency Act of 2014.
- Initiating the build of a disgorgement and penalties system to improve both financial and programmatic reporting of enforcement actions.
- Building upon an Enterprise Risk Management function.

This section provides citizens with detailed information about the SEC's finances and its internal controls over financial reporting. It contains the results of the FY 2017 audit conducted by GAO and the agency's response. This section also includes the SEC's financial statements and notes, both for the entity as a whole and for the Investor Protection Fund, as required under Section 922 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010.

I want to extend special thanks to the staff of the Office of Financial Management as well as other divisions and offices throughout the SEC who remain committed to ensuring sound financial management that delivers relevant and reliable information to stakeholders. The excellent results in financial stewardship could not have been achieved without their efforts.

Sincerely,

Caryn Kauffman

CARYN E. KAUFFMAN
Acting Chief Financial Officer
November 13, 2017

REPORT OF INDEPENDENT AUDITORS

U.S. GOVERNMENT ACCOUNTABILITY OFFICE

441 G St. N.W.
Washington, DC 20548

Independent Auditor's Report

To the Chairman of the United States Securities and Exchange Commission

In our audits of the fiscal years 2017 and 2016 financial statements of the United States Securities and Exchange Commission (SEC)[1] and the Investor Protection Fund (IPF),[2] we found

- the SEC and IPF financial statements as of and for the fiscal years ended September 30, 2017, and 2016, are presented fairly, in all material respects, in accordance with U.S. generally accepted accounting principles;
- SEC maintained, in all material respects, effective internal control over financial reporting for SEC and for IPF as of September 30, 2017; and
- no reportable noncompliance for 2017 with provisions of applicable laws, regulations, contracts, and grant agreements we tested.

The following sections discuss in more detail (1) our report on SEC's and IPF's financial statements and on internal control over financial reporting, which includes required supplementary information (RSI)[3] and other information included with the financial statements;[4] (2) our report on compliance with laws, regulations, contracts, and grant agreements; and (3) agency comments.

Report on the Financial Statements and on Internal Control over Financial Reporting

The Accountability of Tax Dollars Act of 2002 requires that SEC annually prepare and submit audited financial statements to Congress and the Office of Management and

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[1]Section 963 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act), requires that (1) SEC annually submit a report to Congress describing management's responsibility for internal control over financial reporting and assessing the effectiveness of such internal control during the fiscal year; (2) the SEC Chairman and Chief Financial Officer attest to SEC's report; and (3) GAO assess the effectiveness of SEC's internal control over financial reporting and assess, attest to, and report on SEC's assessment. Pub. L. No. 111-203, § 963 (a), (b), 124 Stat. 1376, 1910 (July 21, 2010), *classified at* 15 U.S.C. § 78d-8(a), (b). SEC evaluated its internal control over financial reporting in accordance with the Office of Management and Budget's Circular A-123, *Management's Responsibility for Enterprise Risk Management and Internal Control*, based on criteria established under 31 U.S.C. § 3512(c), (d), commonly known as the Federal Managers' Financial Integrity Act.

[2]IPF, which was established by section 922 of the Dodd-Frank Act, funds the activities of SEC's whistleblower award program and the SEC Office of Inspector General Employee Suggestion Program established under section 966 of the Dodd-Frank Act. IPF is a separate SEC fund, and its financial statements present SEC's financial activity associated with these programs. Accordingly, IPF's financial transactions are also included in SEC's overall financial statements. Pub. L. No. 111-203, § 922(a), 124 Stat. 1376, 1844 (July 21, 2010), *classified at* 15 U.S.C. § 78u-6(g).

[3]The RSI consists of the Management's Discussion and Analysis and the Combined Statement of Budgetary Resources, by Fund, which are included with the financial statements.

[4]Other information consists of information included with the financial statements, other than the RSI and the auditor's report.

Budget.[5] The Securities Exchange Act of 1934, as amended in 2010 by section 922 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act), requires SEC to annually submit a complete set of audited financial statements for IPF to Congress.[6] IPF's financial transactions are also included in SEC's overall financial statements. In accordance with the authority conferred by the Chief Financial Officers Act of 1990, as amended by the Government Management Reform Act of 1994,[7] we have audited the SEC and IPF financial statements. Further, in accordance with the Dodd-Frank Act, we have assessed the effectiveness of SEC's internal control over financial reporting, evaluated SEC's assessment of such effectiveness, and are attesting to and reporting on SEC's assessment of its internal control over financial reporting. SEC's financial statements comprise the balance sheets as of September 30, 2017, and 2016; the related statements of net cost of operations, changes in net position, budgetary resources, and custodial activity for the fiscal years then ended; and the related notes to the financial statements. IPF's financial statements comprise the balance sheets as of September 30, 2017, and 2016; the related statements of net cost of operations, changes in net position, and budgetary resources for the fiscal years then ended; and the related notes to the financial statements. We also have audited SEC's internal control over financial reporting as of September 30, 2017, based on criteria established under 31 U.S.C. § 3512(c), (d), commonly known as the Federal Managers' Financial Integrity Act (FMFIA).

We conducted our audits in accordance with U.S. generally accepted government auditing standards. We believe that the audit evidence we obtained is sufficient and appropriate to provide a basis for our audit opinions.

Management's Responsibility

SEC management is responsible for (1) the preparation and fair presentation of SEC's financial statements and those of IPF in accordance with U.S. generally accepted accounting principles; (2) preparing, measuring, and presenting the RSI in accordance with U.S. generally accepted accounting principles; (3) preparing and presenting other information included in documents containing the audited financial statements and auditor's report, and ensuring the consistency of that information with the audited financial statements and the RSI; (4) maintaining effective internal control over financial reporting, including the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; (5) evaluating the effectiveness of internal control over financial reporting based on the criteria established under FMFIA; and (6) its assessment about the effectiveness of internal control over financial reporting as of September 30, 2017, included in the Management Assurance section of the agency financial report.

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[5] Pub. L. No. 107-289, § 2, 116 Stat. 2049-50 (Nov. 7, 2002), *amending* 31 U.S.C. § 3515.

[6] Dodd-Frank Act, § 922(a), 124 Stat. 1844 (July 21, 2010), *adding* § 21F(g)(5) of the Securities Exchange Act of 1934, *classified at* 15 U.S.C. § 78u-6(g)(5).

[7] See the Chief Financial Officers Act of 1990, Pub. L. No. 101-576, 104 Stat. 2838 (Nov. 15, 1990), *codified, in relevant part, as amended, at* 31 U.S.C. § 3521(g); see also the Government Management Reform Act of 1994, Pub. L. No. 103-356, 108 Stat. 3410 (Oct. 13, 1994), *codified, in relevant part, as amended, at* 31 U.S.C. § 3515(c).

Auditor's Responsibility

Our responsibility is to express opinions on SEC's and IPF's financial statements and opinions on internal control over financial reporting for SEC and for IPF, based on our audits. U.S. generally accepted government auditing standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free from material misstatement, and whether effective internal control over financial reporting was maintained in all material respects. We are also responsible for applying certain limited procedures to other information included with the financial statements.

An audit of financial statements involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the auditor's assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances. An audit of financial statements also involves evaluating the appropriateness of the accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

An audit of internal control over financial reporting involves performing procedures to obtain evidence about whether a material weakness exists.[8] The procedures selected depend on the auditor's judgment, including the assessment of the risk that a material weakness exists. An audit of internal control over financial reporting also includes obtaining an understanding of internal control over financial reporting, and evaluating and testing the design and operating effectiveness of internal control over financial reporting based on the assessed risk. Our audit of internal control also considered SEC's process for evaluating and reporting on internal control over financial reporting based on criteria established under FMFIA. Our audits also included performing such other procedures as we considered necessary in the circumstances.

We did not evaluate all internal controls relevant to operating objectives as broadly established under FMFIA, such as those controls relevant to preparing performance information and ensuring efficient operations. We limited our internal control testing to testing controls over financial reporting. Our internal control testing was for the purpose of expressing an opinion on whether effective internal control over financial reporting was maintained, in all material respects. Consequently, our audit may not identify all deficiencies in internal control over financial reporting that are less severe than a material weakness.

Definition and Inherent Limitations of Internal Control over Financial Reporting

An entity's internal control over financial reporting is a process effected by those charged with governance, management, and other personnel, the objectives of which are to provide reasonable assurance that (1) transactions are properly recorded, processed, and summarized to permit the preparation of financial statements in accordance with U.S. generally accepted accounting principles, and assets are safeguarded against loss from unauthorized acquisition, use, or disposition, and (2) transactions are executed in accordance with provisions of

[8]A material weakness is a deficiency, or combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis. A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis.

applicable laws, regulations, contracts, and grant agreements, noncompliance with which could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent, or detect and correct, misstatements due to fraud or error. We also caution that projecting any evaluation of effectiveness to future periods is subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Opinions on SEC's Financial Statements

In our opinion, SEC's financial statements present fairly, in all material respects, SEC's financial position as of September 30, 2017, and 2016, and its net cost of operations, changes in net position, budgetary resources, and custodial activity for the fiscal years then ended in accordance with U.S. generally accepted accounting principles.

Opinion on IPF's Financial Statements

In our opinion, IPF's financial statements present fairly, in all material respects, IPF's financial position as of September 30, 2017, and 2016, and its net cost of operations, changes in net position, and budgetary resources for the fiscal years then ended in accordance with U.S. generally accepted accounting principles.

Opinion on Internal Control over Financial Reporting

In our opinion, SEC maintained, in all material respects, effective internal control over financial reporting as of September 30, 2017, for SEC and for IPF, based on criteria established under FMFIA. Our opinions on SEC's internal control are consistent with SEC's assessment that its internal control over financial reporting, both for the agency as a whole and for IPF, was operating effectively as of September 30, 2017, and that no material weaknesses were found in the design or operation of the controls.

During our 2017 audit, we identified deficiencies in SEC's internal control over financial reporting that we do not consider to be material weaknesses or significant deficiencies.[9] Nonetheless, these deficiencies warrant SEC management's attention. We have communicated these matters to SEC management and, where appropriate, will report on them separately.

Other Matters

Required Supplementary Information

U.S. generally accepted accounting principles issued by the Federal Accounting Standards Advisory Board (FASAB) require that the RSI be presented to supplement the financial statements. Although the RSI is not a part of the financial statements, FASAB considers this information to be an essential part of financial reporting for placing the financial statements in appropriate operational, economic, or historical context. We have applied certain limited procedures to the RSI in accordance with U.S. generally accepted government auditing standards, which consisted of inquiries of management about the methods of preparing the RSI

[9]A significant deficiency is a deficiency, or a combination of deficiencies, in internal control over financial reporting that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

and comparing the information for consistency with management's responses to the auditor's inquiries, the financial statements, and other knowledge we obtained during the audit of the financial statements, in order to report omissions or material departures from FASAB guidelines, if any, identified by these limited procedures. We did not audit and we do not express an opinion or provide any assurance on the RSI because the limited procedures we applied do not provide sufficient evidence to express an opinion or provide any assurance.

Other Information

SEC's other information contains a wide range of information, some of which is not directly related to the financial statements. This information is presented for purposes of additional analysis and is not a required part of the financial statements or the RSI. We read the other information included with the financial statements in order to identify material inconsistencies, if any, with the audited financial statements. Our audit was conducted for the purpose of forming an opinion on SEC's and IPF's financial statements. We did not audit and do not express an opinion or provide any assurance on the other information.

Report on Compliance with Laws, Regulations, Contracts, and Grant Agreements

In connection with our audits of SEC's and IPF's financial statements, we tested compliance with selected provisions of applicable laws, regulations, contracts, and grant agreements consistent with our auditor's responsibility discussed below. We caution that noncompliance may occur and not be detected by these tests. We performed our tests of compliance in accordance with U.S. generally accepted government auditing standards.

Management's Responsibility

SEC management is responsible for complying with applicable laws, regulations, contracts, and grant agreements applicable to SEC and IPF.

Auditor's Responsibility

Our responsibility is to test compliance with selected provisions of laws, regulations, contracts, and grant agreements applicable to SEC and IPF that have a direct effect on the determination of material amounts and disclosures in the SEC and IPF financial statements, and to perform certain other limited procedures. Accordingly, we did not test compliance with all laws, regulations, contracts, and grant agreements applicable to SEC and IPF.

Results of Our Tests for Compliance with Laws, Regulations, Contracts, and Grant Agreements

Our tests for compliance with selected provisions of applicable laws, regulations, contracts, and grant agreements disclosed no instances of noncompliance for fiscal year 2017 that would be reportable under U.S. generally accepted government auditing standards. However, the objective of our tests was not to provide an opinion on compliance with laws, regulations, contracts, and grant agreements applicable to SEC and IPF. Accordingly, we do not express such an opinion.

Intended Purpose of Report on Compliance with Laws, Regulations, Contracts, and Grant Agreements

The purpose of this report is solely to describe the scope of our testing of compliance with selected provisions of applicable laws, regulations, contracts, and grant agreements, and the

results of that testing, and not to provide an opinion on compliance. This report is an integral part of an audit performed in accordance with U.S. generally accepted government auditing standards in considering compliance. Accordingly, this report on compliance with laws, regulations, contracts, and grant agreements is not suitable for any other purpose.

Agency Comments

In commenting on a draft of this report, SEC expressed pleasure that GAO found that SEC's financial statements and notes were presented fairly, in all material respects, and in accordance with U.S. generally accepted accounting principles. SEC stated that it will continue to build upon this positive result in financial reporting by continuing to improve its internal control environment. SEC stated that it plans to take actions to help strengthen the agency's enterprise risk management program, modernize the tracking of disgorgement and penalties resulting from enforcement actions, and to enhance the processing of registration fees.

SEC also stated that it is already taking a number of proactive steps to enhance the agency's information security, related to deficiencies in its controls over operations that were identified as a result of the 2016 cyber intrusion involving the Electronic Data Gathering, Analysis, and Retrieval system (EDGAR). GAO plans to monitor SEC's actions in response to the intrusion as a separate matter. The complete text of SEC's response is reprinted in enclosure I.

James R. Dalkin
Director
Financial Management and Assurance

November 13, 2017

ENCLOSURE I: MANAGEMENT'S RESPONSE TO AUDIT OPINION

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

OFFICE OF
THE CHAIRMAN

November 9, 2017

Mr. James R. Dalkin
Director
Financial Management and Assurance
United States Government Accountability Office
441 G Street, N.W.
Washington, DC 20548

Dear Mr. Dalkin:

Thank you for the opportunity to review and comment on the audit report of the Government Accountability Office (GAO). I am pleased that the GAO's FY 2017 audit found that the SEC's financial statements and notes were presented fairly, in all material respects, and in conformity with U.S. generally accepted accounting principles.

The SEC intends to build upon this positive result in financial reporting by continuing to improve our internal control environment. I recently announced my intent to establish and fill a new Chief Risk Officer role to strengthen the agency's enterprise risk management program. The SEC also plans to take further action in FY 2018 to modernize the tracking of disgorgement and penalties resulting from enforcement actions and to enhance the newly implemented capabilities in EDGAR that manage the processing of registration fees.

As you know, the SEC also self-identified a material weakness in internal controls over operations related to deficiencies identified as a result of the EDGAR intrusion I disclosed in September 2017. The investigations into this incident are ongoing. However, as described more fully elsewhere in this Annual Financial Report, we are already taking a number of proactive steps to enhance the agency's information security, including uplift of the security over EDGAR and enhanced protocols for communication and escalation around cyber incidents.

I very much appreciate the professional manner in which you and your team conducted the audit for FY 2017. I look forward to continuing our productive dialogue in the coming months on the SEC's efforts to address the areas noted in your report. If you have any questions, please feel free to contact me.

Sincerely,

Jay Clayton
Chairman

SEC FINANCIAL STATEMENTS

U.S. SECURITIES AND EXCHANGE COMMISSION

Balance Sheets

As of September 30, 2017 and 2016

(DOLLARS IN THOUSANDS)	2017	2016
ASSETS (NOTE 2):		
Intragovernmental:		
Fund Balance with Treasury (Note 3)	$ 7,504,874	$ 7,629,504
Investments, Net (Note 5)	2,763,528	2,856,588
Accounts Receivable (Note 6)	—	25
Advances and Prepayments	10,579	11,991
Total Intragovernmental	10,278,981	10,498,108
Cash and Other Monetary Assets (Note 4)	8	27
Accounts Receivable, Net (Note 6)	365,265	1,027,779
Property and Equipment, Net (Note 7)	131,075	125,908
Advances and Prepayments	2	3
Total Assets	$ 10,775,331	$ 11,651,825
LIABILITIES (NOTE 8):		
Intragovernmental:		
Accounts Payable	$ 2,460	$ 5,381
Employee Benefits	7,279	6,991
Unfunded FECA and Unemployment Liability	896	949
Custodial Liability	173,896	665,507
Liability for Non-Entity Assets	580	2,225
Total Intragovernmental	185,111	681,053
Accounts Payable	81,581	76,200
Actuarial FECA Liability	4,779	5,558
Accrued Payroll and Benefits	35,369	35,387
Accrued Leave	75,752	72,836
Registrant Deposits	34,284	36,652
Liability for Disgorgement and Penalties (Note 16)	2,799,436	3,089,688
Contingent Liabilities (Note 10)	221,044	10,800
Other Accrued Liabilities (Note 8)	9,071	6,409
Total Liabilities	3,446,427	4,014,583
Commitments and Contingencies (Note 10)		
NET POSITION:		
Cumulative Results of Operations – Funds from Dedicated Collections (Note 11)	7,328,904	7,637,242
Total Net Position	$ 7,328,904	$ 7,637,242
Total Liabilities and Net Position	$ 10,775,331	$ 11,651,825

The accompanying notes are an integral part of these financial statements.

Statements of Net Cost

For the years ended September 30, 2017 and 2016

(DOLLARS IN THOUSANDS)	2017	2016
PROGRAM COSTS (NOTE 12):		
Enforcement	$ 812,238	$ 602,923
Compliance Inspections and Examinations	389,707	375,888
Corporation Finance	166,451	163,607
Trading and Markets	97,241	92,689
Investment Management	66,199	65,788
Economic and Risk Analysis	76,994	66,669
General Counsel	52,029	51,389
Other Program Offices	90,024	83,316
Agency Direction and Administrative Support	235,533	218,724
Inspector General	16,402	14,928
Total Program Costs	2,002,818	1,735,921
Less: Earned Revenue Not Attributed to Programs (Note 12)	2,138,149	1,974,920
Net (Income) Cost from Operations (Note 15)	$ (135,331)	$ (238,999)

The accompanying notes are an integral part of these financial statements.

Statements of Changes in Net Position

For the years ended September 30, 2017 and 2016

(DOLLARS IN THOUSANDS)	2017		
	Funds from Dedicated Collections	All Other Funds	Consolidated Total
CUMULATIVE RESULTS OF OPERATIONS:			
Beginning Balances	$ 7,637,242	$ —	$ 7,637,242
Budgetary Financing Sources:			
Appropriations Used	19,731	—	19,731
Non-Exchange Revenue	2,734	—	2,734
Other Financing Sources:			
Imputed Financing	27,671	—	27,671
Other (Note 17)	—	(493,805)	(493,805)
Total Financing Sources	50,136	(493,805)	(443,669)
Net Income (Cost) from Operations	(358,474)	493,805	135,331
Net Change	(308,338)	—	(308,338)
Cumulative Results of Operations (Note 11)	7,328,904	—	7,328,904
UNEXPENDED APPROPRIATIONS:			
Budgetary Financing Sources:			
Appropriations Received	19,731	—	19,731
Appropriations Used	(19,731)	—	(19,731)
Total Budgetary Financing Sources	—	—	—
Total Unexpended Appropriations	—	—	—
Net Position, End of Period	$ 7,328,904	$ —	$ 7,328,904

Statements of Changes in Net Position *(continued)*

For the years ended September 30, 2017 and 2016

(DOLLARS IN THOUSANDS)	2016		
	Funds from Dedicated Collections	All Other Funds	Consolidated Total
CUMULATIVE RESULTS OF OPERATIONS:			
Beginning Balances	$ 7,683,210	$ —	$ 7,683,210
Budgetary Financing Sources:			
Appropriations Used	128,529	—	128,529
Non-Exchange Revenue	2,413	—	2,413
Other Financing Sources:			
Imputed Financing	34,360	—	34,360
Other (Note 17)	—	(450,269)	(450,269)
Total Financing Sources	165,302	(450,269)	(284,967)
Net Income (Cost) from Operations	(211,270)	450,269	238,999
Net Change	(45,968)	—	(45,968)
Cumulative Results of Operations (Note 11)	7,637,242	—	7,637,242
UNEXPENDED APPROPRIATIONS:			
Budgetary Financing Sources:			
Appropriations Received	128,529	—	128,529
Appropriations Used	(128,529)	—	(128,529)
Total Budgetary Financing Sources	—	—	—
Total Unexpended Appropriations	—	—	—
Net Position, End of Period	$ 7,637,242	$ —	$ 7,637,242

The accompanying notes are an integral part of these financial statements.

Statements of Budgetary Resources

For the years ended September 30, 2017 and 2016

(DOLLARS IN THOUSANDS)	2017	2016
BUDGETARY RESOURCES:		
Unobligated Balance, Brought Forward, October 1	$ 154,015	$ 162,555
Recoveries of Prior Year Unpaid Obligations	39,554	56,948
Other Changes in Unobligated Balance	599	2,233
Unobligated Balance from Prior Year Budget Authority, Net	194,168	221,736
Appropriations (Discretionary and Mandatory)	73,874	179,605
Spending Authority from Offsetting Collections (Discretionary and Mandatory)	1,586,559	1,476,708
Total Budgetary Resources	$ 1,854,601	$ 1,878,049
STATUS OF BUDGETARY RESOURCES:		
New Obligations and Upward Adjustments (Total) (Note 14)	$ 1,679,431	$ 1,724,034
Unobligated Balance, End of Year:		
Apportioned, Unexpired Accounts	310,180	358,864
Exempt from Apportionment, Unexpired Accounts	1,212	1,848
Unapportioned, Unexpired Accounts	(136,222)	(206,697)
Unobligated Balance, End of Year (Total)	175,170	154,015
Total Budgetary Resources	$ 1,854,601	$ 1,878,049
CHANGE IN OBLIGATED BALANCE:		
Unpaid Obligations:		
Unpaid Obligations, Brought Forward, October 1 (Gross)	$ 852,446	$ 905,843
New Obligations and Upward Adjustments	1,679,431	1,724,034
Outlays (Gross)	(1,761,853)	(1,720,483)
Recoveries of Prior Year Unpaid Obligations	(39,554)	(56,948)
Unpaid Obligations, End of Year	730,470	852,446
Uncollected Payments:		
Uncollected Payments, Federal Sources, Brought Forward, October 1	(25)	(26)
Change in Uncollected Payments, Federal Sources	(675)	1
Uncollected Payments, Federal Sources, End of Year	(700)	(25)
Obligated Balance, End of Year	729,770	852,421
Memorandum (non-add) entries:		
Obligated Balance, Start of Year	$ 852,421	$ 905,817
Obligated Balance, End of Year	$ 729,770	$ 852,421
BUDGET AUTHORITY AND OUTLAYS, NET:		
Budget Authority, Gross (Discretionary and Mandatory)	$ 1,660,433	$ 1,656,313
Actual Offsetting Collections (Discretionary and Mandatory)	(1,585,738)	(1,469,825)
Change in Uncollected Customer Payments from Federal Sources (Discretionary and Mandatory)	(675)	1
Recoveries of Prior Year Paid Obligations (Discretionary and Mandatory)	599	2,233
Budget Authority, Net (Discretionary and Mandatory)	$ 74,619	$ 188,722
Outlays, Gross (Discretionary and Mandatory)	$ 1,761,853	$ 1,720,483
Actual Offsetting Collections (Discretionary and Mandatory)	(1,585,738)	(1,469,825)
Outlays, Net (Discretionary and Mandatory)	176,115	250,658
Distributed Offsetting Receipts	(5,048)	(1,588)
Agency Outlays, Net (Discretionary and Mandatory)	$ 171,067	$ 249,070

The accompanying notes are an integral part of these financial statements.

Statements of Custodial Activity

For the years ended September 30, 2017 and 2016

(DOLLARS IN THOUSANDS)	2017	2016
REVENUE ACTIVITY:		
Sources of Cash Collections:		
Disgorgement and Penalties	$ 1,962,021	$ 1,611,289
Other	1,354	1,543
Total Cash Collections	1,963,375	1,612,832
Accrual Adjustments (Note 13)	(491,612)	165,270
Total Custodial Revenue	1,471,763	1,778,102
DISPOSITION OF COLLECTIONS:		
Amounts Transferred to:		
Department of the Treasury	1,963,375	1,612,832
Amounts Yet to be Transferred	(491,612)	165,270
Total Disposition of Collections	1,471,763	1,778,102
NET CUSTODIAL ACTIVITY	$ —	$ —

The accompanying notes are an integral part of these financial statements.

NOTES TO THE FINANCIAL STATEMENTS

As of September 30, 2017 and 2016

NOTE 1. SIGNIFICANT ACCOUNTING POLICIES

A. Reporting Entity

The U.S. Securities and Exchange Commission (SEC) is an independent agency of the U.S. Government established pursuant to the Securities Exchange Act of 1934 (Exchange Act), charged with regulating this country's capital markets. The SEC's mission is to protect investors; maintain fair, orderly, and efficient markets; and facilitate capital formation. The SEC works with Congress, other executive branch agencies, self-regulatory organizations (SROs) (e.g., stock exchanges and the Financial Industry Regulatory Authority), accounting and auditing standards setters, state securities regulators, law enforcement officials, and many other organizations in support of the agency's mission.

The SEC consists of five presidentially-appointed Commissioners, with staggered five-year terms. The SEC is organized into five divisions and multiple offices. The five divisions are the Division of Enforcement, the Division of Corporation Finance, the Division of Trading and Markets, the Division of Investment Management, and the Division of Economic and Risk Analysis. The offices include the Office of Compliance Inspections and Examinations, the Office of General Counsel, the Office of Investor Education and Advocacy, the Office of the Chief Accountant, the Office of International Affairs, the Office of Administrative Law Judges, the Office of Credit Ratings, the Office of the Investor Advocate, the Office of Municipal Securities, the Office of Inspector General, 11 regional offices, and various supporting services.

The SEC reporting entity includes the Investor Protection Fund. In addition to being included in the SEC's financial statements, the Investor Protection Fund's financial activities and balances are also presented separately as stand-alone financial statements, as required by Exchange Act Section 21F(g)5.

As discussed in *Note 10.A, Commitments: Securities Investor Protection Act*, the SEC reporting entity does not include the Securities Investor Protection Corporation (SIPC).

As discussed in *Note 1.R, Disgorgement and Penalties*, disgorgement funds collected and held by the SEC on behalf of harmed investors are part of the SEC reporting entity. However, disgorgement funds held by the U.S. Courts and by non-federal receivers on behalf of harmed investors are not part of the SEC reporting entity.

B. Basis of Presentation and Accounting

The accompanying financial statements present the financial position, net cost of operations, changes in net position, budgetary resources, and custodial activities of the SEC as required by the Accountability of Tax Dollars Act of 2002. The statements may differ from other financial reports submitted pursuant to Office of Management and Budget (OMB) directives for the purpose of monitoring and controlling the use of the SEC's budgetary resources, due to differences in accounting and reporting principles discussed in the following paragraphs. The SEC's books and records serve as the source of the information presented in the accompanying financial statements.

The agency classifies assets, liabilities, revenues, and costs in these financial statements according to the type of entity associated with the transactions. Intragovernmental assets and liabilities are those due from or to other federal entities. Intragovernmental revenues are

earned from other federal entities. Intragovernmental costs are payments or accruals due to other federal entities.

The SEC's financial statements are prepared in conformity with generally accepted accounting principles (GAAP) for federal reporting entities and presented in conformity with OMB Circular A-136, *Financial Reporting Requirements*. The Balance Sheet, Statement of Net Cost, and Statement of Changes in Net Position are prepared using the accrual basis of accounting. Accordingly, revenues are recognized when earned and expenses are recognized when incurred without regard to the receipt or payment of cash. These principles differ from budgetary accounting and reporting principles on which the Statement of Budgetary Resources is prepared. The differences relate primarily to the capitalization and depreciation of property and equipment, as well as the recognition of other assets and liabilities. The Statement of Custodial Activity is presented on the modified cash basis of accounting. See *Note 13, Custodial Revenues*.

The SEC presents cost of operations by program. OMB Circular A-136 defines the term "major program" as describing an agency's mission, strategic goals, functions, activities, services, projects, processes, or any other meaningful grouping. The presentation by program is consistent with the presentation used by the agency in submitting its budget requests.

C. Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities. These estimates and assumptions include, but are not limited to, the allowance for uncollectible accounts and the allocation of costs to the SEC programs presented in the Statement of Net Cost. Estimates also include (a) the disclosure of any contingent liabilities and the disclosure of other potential future payments as of the date of the financial statements, and (b) the reported amounts of revenue and expenses during the reporting period. Actual results may differ from these estimates.

D. Intra- and Inter-Agency Relationships

The SEC is a single federal agency composed of various Treasury Appropriation Fund Symbols (Funds), and it has only limited intra-entity transactions. The Investor Protection Fund finances the operations of the SEC Office of Inspector General's Employee Suggestion Program on a reimbursable basis. This has given rise to a small amount of intra-entity eliminations of the related revenue and expense transactions between the Investor Protection Fund and the SEC's general Salaries and Expenses Fund. See *Note 1.E, Fund Accounting Structure*, for more information about the SEC's Treasury Appropriation Symbols.

E. Fund Accounting Structure

The SEC, in common with other federal agencies, utilizes various Funds, to recognize and track appropriation authority provided by Congress, collections from the public, and other financial activity. These funds are described below.

1. Funds from Dedicated Collections: Statement of Federal Financial Accounting Standards 27, *Identifying and Reporting Funds from Dedicated Collections*, as amended, states that, "funds from dedicated collections are financed by specifically identified revenues, provided to the government by non-federal sources, often supplemented by other financing sources, which remain available over time. These specifically identified revenues and other financing sources are required by statute to be used for designated activities, benefits, or purposes, and must be accounted for separately from the government's general revenues. The SEC's funds from dedicated collections are deposited into Fund X0100, *Salaries and Expenses*; Fund X5567, *Investor Protection Fund*; and Fund X5566, *Reserve Fund*.

   - Salaries and Expenses: Earned revenues from securities transaction fees from SROs are depos-

ited into Fund X0100, *Salaries and Expenses, Securities and Exchange Commission*. These collections are dedicated to carrying out the SEC's mission, functions, and day to day operations and may be used in accordance with spending limits established by Congress. Collections in excess of Congressional spending limits are unavailable by law and reported as Non-Budgetary Fund Balance with Treasury. See *Note 3, Fund Balance with Treasury*.

- Investor Protection Fund: The Investor Protection Fund provides funding for the payment of whistleblower awards as required by the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank Act). The Investor Protection Fund is financed by a portion of monetary sanctions collected by the SEC in judicial or administrative actions brought by the SEC. Persons may receive award payments from the Investor Protection Fund if they voluntarily provide original information to the SEC that results in a successful enforcement action and other conditions are met. In addition, the Investor Protection Fund is used to finance the operations of the SEC's Office of Inspector General's Employee Suggestion Program for the receipt of suggestions for improvements in work efficiency and effectiveness, and allegations of misconduct or mismanagement within the SEC. This activity is recognized in Fund X5567, *Monetary Sanctions and Interest, Investor Protection Fund, Securities and Exchange Commission (Investor Protection Fund)*.

- Reserve Fund: A portion of SEC registration fee collections up to $50 million in any one fiscal year may be deposited in the Reserve Fund, the balance of which cannot exceed $100 million. The Reserve Fund may be used by the SEC to obligate up to $100 million in one fiscal year as the SEC determines necessary to carry out its functions. Although amounts deposited in the Reserve Fund are not subject to apportionment, the SEC must notify Congress when funds are obligated. Resources available in the Reserve Fund may be rescinded or sequestered through Congressional action. This activity is recognized in Fund X5566, *Securities and Exchange Commission Reserve Fund*.

2. Miscellaneous Receipt Accounts: Miscellaneous Receipt Accounts hold non-entity receipts and accounts receivable from custodial activities that the SEC cannot deposit into funds under its control. These accounts include registration fee collections in excess of amounts deposited into the Reserve Fund, receipts pursuant to certain SEC enforcement actions and other small collections that will be sent to the U.S. Treasury General Fund upon collection. These activities are recognized in Fund 0850.150, *Registration, Filing, and Transaction Fees, Securities and Exchange Commission*; Fund 1060, *Forfeitures of Unclaimed Money and Property;* Fund 1099, *Fines, Penalties, and Forfeitures, Not Otherwise Classified*; Fund 1435, *General Fund Proprietary Interest, Not Otherwise Classified;* and Fund 3220, *General Fund Proprietary Receipts, Not Otherwise Classified*. Miscellaneous Receipt Accounts are reported as "All Other Funds" on the Statement of Changes in Net Position. The SEC has custodial responsibilities, as disclosed in *Note 1.L, Liabilities*.

3. Deposit Funds: Deposit Funds hold disgorgement, penalties, and interest collected and held on behalf of harmed investors, registrant monies held temporarily until earned by the SEC, and collections awaiting disposition or reclassification. These activities are recognized in Fund X6561, *Unearned Fees, Securities and Exchange Commission* and Fund X6563, *Disgorgement and Penalty Amounts Held for Investors, Securities and Exchange Commission*. Deposit Funds do not impact the SEC's Net Position and are not reported on the Statement of Changes in Net Position.

F. Entity and Non-Entity Assets

Entity assets are assets that the SEC may use in its operations.

Non-entity assets are assets that the SEC holds on behalf of another federal agency or a third party and are not available for the SEC to use in its operations. See *Note 2, Entity and Non-Entity Assets*.

G. Fund Balance with Treasury

Fund Balance with Treasury (FBWT) reflects amounts the SEC holds in the U.S. Treasury that have not been invested in federal securities. Additional information regarding the SEC's FBWT is provided in *Note 3, Fund Balance with Treasury*.

The SEC conducts all of its banking activity in accordance with directives issued by the U.S. Department of the Treasury's Bureau of the Fiscal Service.

H. Investments

The SEC has the authority to invest disgorgement funds in Treasury securities, including civil penalties collected under the "Fair Fund" provision of the Sarbanes-Oxley Act of 2002. As the funds are collected, the SEC holds them in a deposit fund account and may invest them in overnight and short-term market-based Treasury securities through the U.S. Department of the Treasury's Bureau of the Fiscal Service.

The SEC also has authority to invest amounts in the Investor Protection Fund in overnight and short-term market-based Treasury securities through the Bureau of the Fiscal Service. The interest earned on the investments is a component of the balance of the Fund and available to be used for expenses of the Investor Protection Fund.

Additional information regarding the SEC's investments is provided in *Note 5, Investments*.

I. Accounts Receivable and Allowance for Uncollectible Accounts

The SEC's entity and non-entity accounts receivable consist primarily of amounts due from the public. Entity accounts receivable are amounts that the SEC may retain upon collection. Non-entity accounts receivable are amounts that the SEC will forward to another federal agency or to the public after the funds are collected.

Entity Accounts Receivable

The bulk of the SEC's entity accounts receivable arise from securities transaction fees. Securities transaction fees are payable to the SEC twice a year: in March for the period September through December, and in September for the period January through August. Accordingly, the year-end accounts receivable accrual generally represents fees payable to the SEC for one month of securities transaction fee activity (September). In addition, the SEC has small amounts of activity arising from the sale of services provided by the SEC to other federal agencies and employee-related debt.

Non-Entity Accounts Receivable

Non-entity accounts receivable arise mainly from amounts assessed against violators of securities laws, including disgorgement of illegal gains, civil penalties, and related assessed interest. The SEC is responsible for collection, and recognizes a receivable, when an order of the Commission or a federal court directs payment to the SEC or the U.S. Treasury.

Interest recognized by the SEC on non-entity accounts receivable includes prejudgment interest specified by the court or administrative order as well as post-judgment interest on collectible accounts. The SEC does not recognize interest revenue on accounts considered to be uncollectible.

The SEC's enforcement investigation and litigation activities often result in court orders directing violators of federal securities laws to pay amounts assessed to

a federal court or to a non-federal receiver acting on behalf of harmed investors. These orders are not recognized as accounts receivable by the SEC because the debts are payable to, and collected by, another party.

Securities registration, tender offer, merger, and other fees from registrants (filing fee) collections in excess of those deposited into the SEC's Reserve Fund are not available for the SEC's operations and are transferred to the U.S. Treasury General Fund. Accounts receivable amounts arising from filing fees in excess of those deposited into the Reserve Fund are non-entity and are held on behalf of the U.S. Treasury.

Allowance for Uncollectible Accounts

The SEC uses a three-tiered methodology for calculating the allowance for loss on its disgorgement and penalties accounts receivable. The first tier involves making an individual collection assessment of cases that represent at least 65 percent of the portfolio. The second and third tiers are composed of the remaining cases that are equal to or less than 30 days old and over 30 days old, respectively. For the second and third tiers, the SEC applies an allowance rate based on historical collection data analysis.

The SEC calculates the allowance for uncollectible accounts and the related provision for estimated losses for filing fees and other accounts receivable using an analysis of historical collection data. No allowance for uncollectible accounts or related provision for estimated losses has been established for securities transaction fees payable by SROs, as these amounts are fully collectible based on historical experience.

The SEC writes off receivables that are delinquent for two or more years by removing the debt amounts from the gross accounts receivable and any related allowance for uncollectible accounts.

Additional information about the SEC's accounts receivable and allowance for doubtful accounts is provided in *Note 6, Accounts Receivable, Net*.

J. Other Assets

Payments made in advance of the receipt of goods and services are recorded as advances or prepayments and recognized as expenses when the related goods and services are received.

K. Property and Equipment, Net

The SEC's property and equipment consists of software, general-purpose equipment used by the agency, capital improvements made to buildings leased by the SEC for office space, and, when applicable, internal-use software development costs for projects in development. The SEC reports property and equipment purchases and additions at historical cost. The agency expenses property and equipment acquisitions that do not meet the capitalization criteria as well as normal repairs and maintenance.

The SEC depreciates property and equipment over the estimated useful lives using the straight-line method of depreciation. The agency removes property and equipment from its asset accounts in the period of disposal, retirement, or removal from service. The SEC recognizes the difference between the book value and any proceeds as a gain or loss in the period that the asset is removed.

L. Liabilities

The SEC recognizes liabilities for probable future outflows or other sacrifices of resources as a result of events that have occurred as of the Balance Sheet date. The SEC's liabilities consist of routine operating accounts payable, accrued payroll and benefits, legal liabilities, liabilities to offset non-entity assets such as registrant monies held temporarily until earned by the SEC, disgorgement and penalties collected and receivable, and amounts collected or receivable on behalf of the U.S. Treasury. See *Note 1.F, Entity and Non-Entity Assets*, for additional information.

Enforcement Related Liabilities

A liability for disgorgement and penalties arises when an order is issued for the SEC to collect disgorgement, penalties, and interest from securities law violators.

When the Commission or court issues such an order, the SEC establishes an accounts receivable due to the SEC offset by a liability. The presentation of this liability on the Balance Sheet is dependent upon several factors. If the court or Commission order indicates that collections are to be retained by the federal government by transfer to the U.S. Treasury General Fund, the liabilities are classified as custodial (that is, collected on behalf of the government) and intragovernmental. If the order indicates that the funds are eligible for distribution to harmed investors, the SEC will recognize a governmental liability (that is, a liability of the government to make a payment to the public). This liability is not presented as a custodial liability. The SEC does not record liabilities on its financial statements for disgorgement and penalty amounts that another government entity such as a court, or a non-governmental entity, such as a receiver, has collected or will collect.

In accordance with the provisions of the Dodd-Frank Act, collections not distributed to harmed investors may be transferred to either the Investor Protection Fund or the U.S. Treasury General Fund. Collections not distributed to harmed investors are transferred to the Investor Protection Fund if the Fund's balance does not exceed $300 million at the time of collection. See *Note 16, Disgorgement and Penalties,* for additional information.

Liability Classification

The SEC recognizes liabilities that are covered by budgetary resources, liabilities that are not covered by budgetary resources, and liabilities that do not require the use of budgetary resources. See *Note 8, Liabilities Covered and Not Covered by Budgetary Resources*, for more information.

M. Employee Retirement Systems and Benefits

The SEC's employees may participate in either the Civil Service Retirement System (CSRS) or the Federal Employees Retirement System (FERS), depending on when they started working for the federal government. FERS and Social Security automatically cover most employees hired after December 31, 1983. Employees who are rehired after a break in service of more than one year and who had five years of federal civilian service prior to 1987 are eligible to participate in the CSRS offset retirement system or may elect to join FERS.

All employees are eligible to contribute to a Thrift Savings Plan (TSP). For those employees participating in FERS, the TSP is automatically established, and the SEC makes a mandatory 1 percent contribution to this plan. In addition, the SEC matches contributions ranging from 1 to 4 percent for FERS-eligible employees who contribute to their TSP. Employees participating in CSRS do not receive matching contributions to their TSP. The SEC also provides a supplemental retirement contribution program that matches an employee's TSP contribution up to an additional 3 percent of their salary.

Employees participating in FERS are subject to Social Security payroll taxes and are eligible for Social Security benefits based upon their federal employment. The SEC contributes the employer's matching amount for Social Security to the Social Security Administration under the Federal Insurance Contributions Act, which fully covers FERS participating employees.

The SEC does not report CSRS, FERS, Federal Employees Health Benefits Program, Federal Employees Group Life Insurance Program assets, or accumulated plan benefits; the U.S. Office of Personnel Management (OPM) reports this information. In accordance with federal accounting standards, the SEC recognizes costs incurred by the SEC but financed by OPM on behalf of the SEC as an expense. The funding for this expense is reflected as imputed financing on the Statement of Changes in Net Position.

N. Injury and Post-employment Compensation

The Federal Employees' Compensation Act (FECA), administered by the U.S. Department of Labor, provides income and medical cost protection to covered federal civilian employees harmed on the job or who have contracted an occupational disease, and dependents of employees whose death is attributable to a job-related injury or occupational disease. See *Note 8, Liabilities Covered and Not Covered by Budgetary Resources*.

O. Annual, Sick, and Other Leave

The SEC accrues annual leave and compensatory time as earned and reduces the accrual when leave is taken. The balances in the accrued leave accounts reflect current leave balances and pay rates. See *Note 8, Liabilities Covered and Not Covered by Budgetary Resources*. The SEC expenses sick leave and other types of non-vested leave as used.

P. Revenue and Other Financing Sources

The SEC's revenue and financing sources include exchange revenues, which are generated from transactions in which both parties give and receive value, and non-exchange revenues, which arise from the federal government's ability to demand payment.

Exchange Revenue

The SEC's exchange revenue consists primarily of collections of securities transaction fees from SROs and of securities registration, tender offer, merger, and other fees from registrants (filing fees). The fee rates are calculated by the SEC's Division of Economic and Risk Analysis and established by the SEC in accordance with federal law and are applied to volumes of activity reported by SROs or to filings submitted by registrants. Fees are recognized as exchange revenue on the effective date of transaction or filing. These fee collections are the primary source of the SEC's funding and may be used up to limits established by Congress. See *Note 1.E, Fund Accounting Structure*.

The SEC recognizes amounts remitted by registrants in advance of the transaction or filing date as a liability until earned by the SEC or returned to the registrant. Federal regulation requires the return of registrant advance deposits when an account is dormant for three years, except in certain cases where refunds are not permitted. The Securities Act of 1933 and the Exchange Act do not permit refunds to registrants for securities that remain unsold after the completion, termination, or withdrawal of an offering. However, Code of Federal Regulations (CFR) Title 17 Chapter II, Part 230, Section 457(p) permits filers to offset a fee paid (filing fee offset) for a subsequent registration statement (offering) filed within five years of the initial filing date of the earlier registration statement. The total aggregate dollar amount of the filing fee associated with the unsold securities may be offset against the total filing fee due on the subsequent offering. Unused filing fee offsets are not an accounts payable to the SEC because registrants cannot obtain refunds of fees or additional services in relation to securities that remain unsold. See *Note 12, Costs and Exchange Revenue*.

Non-Exchange Revenue

The SEC's non-exchange revenue mainly consists of amounts collected from violators of securities laws as a result of enforcement proceedings. These amounts may take the form of disgorgement of illegal gains, civil penalties, and related interest. Amounts collected may be paid to injured investors, transferred to the Investor Protection Fund, or transferred to the U.S. Treasury General Fund, based on established policy and regulation.

All non-exchange revenue expected to be forwarded to the U.S. Treasury General Fund is recognized on the Statement of Custodial Activity. The result is that, in accordance with federal accounting standards, the entire amount of custodial activity is presented on the Statement of Custodial Activity to document the movement of funds, and the portion retained by the SEC is recognized as SEC activity.

The SEC does not recognize amounts collected and held by another government entity, such as a court registry, or a non-government entity, such as a receiver.

Q. Budgets and Budgetary Accounting

Salaries and Expenses

The SEC deposits securities transaction fee revenue in the SEC's Salaries and Expenses account. However, the SEC may use funds from this account only as authorized by Congress and made available by OMB apportionment, upon issuance of a Treasury warrant. Revenue collected in excess of appropriated amounts is restricted from use by the SEC. Collections in excess of Congressional spending limits are unavailable by law and reported as Non-Budgetary Fund Balance with Treasury (See *Note 3, Fund Balance with Treasury*). Each fiscal year, OMB provides the SEC's Salaries and Expenses account with Category A apportionments, which are quarterly distributions of budgetary resources for the fiscal year. These apportionments include both new budget authority appropriated by Congress and unused no-year funds (unobligated balances) from prior years. The Salaries and Expenses account also receives a small amount of Category B funds related to reimbursable activity, which are exempt from quarterly apportionment. See *Note 1.E, Fund Accounting Structure*.

Investor Protection Fund

The Dodd-Frank Act provides that the Investor Protection Fund has a permanent indefinite appropriation that is available without further appropriation or fiscal year limitation for the purpose of funding awards to whistleblowers and for the operations of the Office of Inspector General's Employee Suggestion Program. However, the SEC is required to request and obtain an annual apportionment from OMB to use these funds. All of the funds are Category B, exempt from quarterly apportionment. The Investor Protection Fund is financed by transferring a portion of monetary sanctions collected by the SEC under Section 308 of the Sarbanes-Oxley Act of 2002 (15 U.S.C. 7246). Sanctions collected by the Commission payable either to the SEC or the U.S. Treasury General Fund will be transferred to the Investor Protection Fund if the balance in that fund is less than $300 million on the day of collection. See *Note 1.E, Fund Accounting Structure*.

Reserve Fund

The Reserve Fund is a special fund that has the authority to retain certain revenues not used in the current period for future use. The Dodd-Frank Act provides that the Fund is available to the SEC without further appropriation or fiscal year limitation "to carry out the functions of the Commission." Amounts in the Reserve Fund are exempt from apportionment. Collections arising from securities registration, tender offer, and merger fees from registrants, other than those that are deposited in the Reserve Fund, are not available to be used in the operations of the SEC. See *Note 1.E, Fund Accounting Structure*.

Borrowing Authority

The SEC's borrowing authority is limited to authority to borrow funds from the U.S. Treasury in order to loan funds to the Securities Investor Protection Corporation, as discussed in *Note 10.A, Commitments: Securities Investor Protection Act*.

R. Disgorgement and Penalties

The SEC maintains non-entity assets related to disgorgement and penalties ordered pursuant to civil injunctive and administrative proceedings. The SEC also recognizes an equal and offsetting liability for these assets, as discussed in *Note 1.I, Accounts Receivable and Allowance for Uncollectible Accounts*, and *Note 1.L, Liabilities*. Additional details regarding disgorgement and penalties are presented in *Note 11, Funds from Dedicated Collections,* and *Note 16, Disgorgement and Penalties*.

NOTE 2. ENTITY AND NON-ENTITY ASSETS

Entity assets are assets that the SEC may use in its operations.

Non-entity assets are assets that the SEC holds on behalf of another federal agency or a third party and are not available for the SEC's use. The SEC's non-entity assets include the following: (a) disgorgement, penalties, and interest collected and held or invested by the SEC; (b) disgorgement, penalties, and interest receivable that will be collected by the SEC; (c) securities registration, tender offer, merger, and other fees collected and receivable from registrants, in excess of amounts deposited in the SEC's Reserve Fund; and (d) other miscellaneous receivables and collections such as registrant monies held temporarily until earned by the SEC. Additional details are provided in *Note 16, Disgorgement and Penalties*.

At September 30, 2017, SEC entity and non-entity assets consisted of the following:

(DOLLARS IN THOUSANDS)	Entity	Non-Entity	Total
INTRAGOVERNMENTAL:			
Fund Balance with Treasury:			
SEC Funds	$ 7,195,397	$ —	$ 7,195,397
Registrant Deposits	—	34,284	34,284
Disgorgement and Penalties (Note 16)	—	275,167	275,167
Custodial and Other Non-Entity Assets	—	26	26
Investments, Net:			
Disgorgement and Penalties (Note 16)	—	2,471,245	2,471,245
Investor Protection Fund	292,283	—	292,283
Accounts Receivable	—	—	—
Advances and Prepayments	10,579	—	10,579
Total Intragovernmental Assets	7,498,259	2,780,722	10,278,981
Cash and Other Monetary Assets:			
Disgorgement and Penalties (Note 16)	—	8	8
Accounts Receivable, Net:			
SEC Funds	137,765	—	137,765
Disgorgement and Penalties (Note 16)	—	226,524	226,524
Custodial and Other Non-Entity Assets	—	976	976
Property and Equipment, Net (Note 7)	131,075	—	131,075
Advances and Prepayments	2	—	2
Total Assets	$ 7,767,101	$ 3,008,230	$ 10,775,331

At September 30, 2016, SEC entity and non-entity assets consisted of the following:

(DOLLARS IN THOUSANDS)	Entity	Non-Entity	Total
INTRAGOVERNMENTAL:			
Fund Balance with Treasury:			
SEC Funds	$ 7,241,081	$ —	$ 7,241,081
Registrant Deposits	—	36,652	36,652
Disgorgement and Penalties (Note 16)	—	351,735	351,735
Custodial and Other Non-Entity Assets	—	36	36
Investments, Net:			
Disgorgement and Penalties (Note 16)	—	2,506,317	2,506,317
Investor Protection Fund	350,271	—	350,271
Accounts Receivable	25	—	25
Advances and Prepayments	11,991	—	11,991
Total Intragovernmental Assets	7,603,368	2,894,740	10,498,108
Cash and Other Monetary Assets:			
Disgorgement and Penalties (Note 16)	—	27	27
Accounts Receivable, Net:			
SEC Funds	128,419	—	128,419
Disgorgement and Penalties (Note 16)	—	896,328	896,328
Custodial and Other Non-Entity Assets	—	3,032	3,032
Property and Equipment, Net (Note 7)	125,908	—	125,908
Advances and Prepayments	3	—	3
Total Assets	$ 7,857,698	$ 3,794,127	$ 11,651,825

NOTE 3. FUND BALANCE WITH TREASURY

The Fund Balance with Treasury by type of fund and Status of Fund Balance with Treasury as of September 30, 2017 and 2016 consists of the following:

(DOLLARS IN THOUSANDS)	2017	2016
FUND BALANCES:		
General Funds	$ 7,080,452	$ 7,139,871
Special Funds	114,921	101,163
Other Funds	309,501	388,470
Total Fund Balance with Treasury	$ 7,504,874	$ 7,629,504
STATUS OF FUND BALANCE WITH TREASURY:		
Unobligated Balance:		
Available	21,553	15,303
Unavailable	96,664	100,175
Obligated Balance not Yet Disbursed	591,739	639,394
Non-Budgetary Fund Balance with Treasury	6,794,918	6,874,632
Total Status of Fund Balance with Treasury	$ 7,504,874	$ 7,629,504

Special Funds consist of the Investor Protection Fund and the Reserve Fund. Refer to *Note 1.E, Fund Accounting Structure*, for additional information.

Other Funds consist of Fund Balance with Treasury held in deposit funds.

Obligated and unobligated balances reported for the status of Fund Balance with Treasury differ from the amounts reported in the Statement of Budgetary Resources due to the fact that budgetary balances are supported by amounts other than Fund Balance with Treasury. These amounts include Investor Protection Fund investments, uncollected payments from federal sources, and the impact of the change in legal interpretation for leases. See *Note 14.C, Other Budgetary Disclosures, Change in Legal Interpretation for Lease Obligations*.

Non-Budgetary Fund Balance with Treasury consists of amounts in deposit funds and offsetting collections temporarily precluded from obligation in the SEC's general Salaries and Expenses Fund (X0100). Amounts temporarily precluded from obligation represent offsetting collections in excess of appropriated amounts related to securities transactions fees, as well as securities registration, tender offer, merger, and other fees from registrants (filing fees) collected in fiscal years 2011 and prior.

There were no significant differences between the Fund Balance with Treasury reflected in the SEC's financial statements and the corresponding balance in the U.S. Treasury Department accounts.

NOTE 4. CASH AND OTHER MONETARY ASSETS

The SEC had a cash balance of $8 thousand as of September 30, 2017. The SEC receives collections throughout the year. Any collections received after the U.S. Treasury Department cut-off for deposit of checks are treated as deposits in transit and recognized as Cash on the Balance Sheet. The SEC had a cash balance of $27 thousand as of September 30, 2016.

NOTE 5. INVESTMENTS

The SEC invests funds in overnight and short-term non-marketable market-based Treasury securities. The SEC records the value of its investments in Treasury securities at cost and amortizes any premium or discount on a straight-line basis (S/L) through the maturity date of these securities. Non-marketable market-based Treasury securities are issued by the U.S. Treasury Department's Bureau of the Fiscal Service to federal agencies. They are not traded on any securities exchange but mirror the prices of similar Treasury securities trading in the government securities market. The market value of Treasury securities is a composite market bid price, using market data provided by the Federal Reserve Bank of New York, that reflects the average price that brokers were offering to pay on the reporting date.

At September 30, 2017, investments consisted of the following:

(DOLLARS IN THOUSANDS)	Cost	Amortization Method	Amortized (Premium) Discount	Interest Receivable	Investment, Net	Market Value Disclosure
Non-Marketable Market-Based Securities						
Disgorgement and Penalties	$ 2,467,217	S/L	$ 4,009	$ 19	$ 2,471,245	$ 2,162,154
Investor Protection Fund – Entity	294,098	S/L	(3,680)	1,865	292,283	290,274
Total	$ 2,761,315		$ 329	$ 1,884	$ 2,763,528	$ 2,452,428

At September 30, 2016, investments consisted of the following:

(DOLLARS IN THOUSANDS)	Cost	Amortization Method	Amortized (Premium) Discount	Interest Receivable	Investment, Net	Market Value Disclosure
Non-Marketable Market-Based Securities						
Disgorgement and Penalties	$ 2,504,983	S/L	$ (1,673)	$ 3,007	$ 2,506,317	$ 2,487,799
Investor Protection Fund – Entity	353,742	S/L	(6,277)	2,806	350,271	347,759
Total	$ 2,858,725		$ (7,950)	$ 5,813	$ 2,856,588	$ 2,835,558

Intragovernmental Investments in Treasury Securities

The federal government does not set aside assets to pay future benefits or other expenditures associated with the investment by federal agencies in non-marketable federal securities. The balances underlying these investments are deposited in the U.S. Treasury, which uses the cash for general government purposes. Treasury securities are issued to the SEC as evidence of these balances. Treasury securities are an asset of the SEC and a liability of the U.S. Treasury. Because the SEC and the U.S. Treasury are both components of the government, these assets and liabilities offset each other from the standpoint of the government as a whole. For this reason, the investments presented by the SEC do not represent an asset or a liability in the U.S. Government-wide financial statements.

Treasury securities provide the SEC with authority to draw upon the U.S. Treasury to make future payments from these accounts. When the SEC requires redemption of these securities to make expenditures, the government finances those expenditures out of accumulated cash balances, by raising taxes or other receipts, by borrowing from the public or repaying less debt, or by curtailing other expenditures. This is the same manner in which the government finances all expenditures.

NOTE 6. ACCOUNTS RECEIVABLE, NET

At September 30, 2017, accounts receivable consisted of the following:

(DOLLARS IN THOUSANDS)	Gross Receivables	Allowance	Net Receivables
Intragovernmental Entity Accounts Receivable:			
Reimbursable Activity	$ —	$ —	$ —
Entity Accounts Receivable:			
Securities Transaction Fees	$ 137,217	$ —	$ 137,217
Other	548	—	548
Non-Entity Accounts Receivable:			
Disgorgement and Penalties[1]	1,938,273	1,711,749	226,524
Filing Fees	620	40	580
Other	7,009	6,613	396
Subtotal Non-Intragovernmental Accounts Receivable	2,083,667	1,718,402	365,265
Total Accounts Receivable	$ 2,083,667	$ 1,718,402	$ 365,265

1

Disgorgement and Penalties Accounts Receivable by Tiers (Note 1.I)			
(DOLLARS IN THOUSANDS)	Gross Receivable	Allowance	Net Receivable
Tier 1	1,196,433	1,074,179	122,254
Tier 2	37,145	24,494	12,651
Tier 3	704,695	613,076	91,619
Total Non-Entity Accounts Receivable: Disgorgement and Penalties	1,938,273	1,711,749	226,524

At September 30, 2016, accounts receivable consisted of the following:

(DOLLARS IN THOUSANDS)	Gross Receivables	Allowance	Net Receivables
Intragovernmental Entity Accounts Receivable:			
Reimbursable Activity	$ 25	$ —	$ 25
Entity Accounts Receivable:			
Securities Transaction Fees	$ 127,874	$ —	$ 127,874
Other	545	—	545
Non-Entity Accounts Receivable:			
Disgorgement and Penalties[2]	3,075,435	2,179,107	896,328
Filing Fees	2,249	24	2,225
Other	6,203	5,396	807
Subtotal Non-Intragovernmental Accounts Receivable	3,212,306	2,184,527	1,027,779
Total Accounts Receivable	$ 3,212,331	$ 2,184,527	$ 1,027,804

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Disgorgement and Penalties Accounts Receivable by Tiers (Note 1.I)			
(DOLLARS IN THOUSANDS)	Gross Receivable	Allowance	Net Receivable
Tier 1	2,084,204	1,360,545	723,659
Tier 2	115,992	57,360	58,632
Tier 3	875,239	761,202	114,037
Total Non-Entity Accounts Receivable: Disgorgement and Penalties	3,075,435	2,179,107	896,328

Refer to Note 1.I, Accounts Receivable and Allowance for Uncollectible Accounts for methods used to estimate allowances. The SEC does not recognize interest revenue on accounts considered to be uncollectible. The SEC estimates that accumulated interest on accounts receivable considered to be uncollectible is $6.6 million and $5.4 million, respectively, as of September 30, 2017 and 2016. This estimate does not include interest accumulated on debts written off or officially waived.

As of September 30, 2017 and 2016, the balances include disgorgement and penalty accounts receivable, net of allowance, of $173.5 million and $664.7 million, respectively, designated as payable to the U.S. Treasury General Fund per court order. As discussed in *Note 1.L, Liabilities*, these receivables, their offsetting liabilities, and the associated revenues, are classified as custodial.

As discussed in Note *1.I, Accounts Receivable and Allowance for Uncollectible Accounts*, pursuant to Section 991(e) of the Dodd-Frank Act, accounts receivable for securities registration, tender offer, merger, and other fees from registrants in excess of the amounts deposited into the Reserve Fund are held on behalf of the U.S. Treasury and are transferred to the U.S. Treasury General Fund upon collection.

NOTE 7. PROPERTY AND EQUIPMENT, NET

At September 30, 2017, property and equipment consisted of the following:

Class of Property *(DOLLARS IN THOUSANDS)*	Depreciation/ Amortization Method	Capitalization Threshold for Individual Purchases	Capitalization Threshold for Bulk Purchases	Service Life (Years)	Acquisition Cost	Accumulated Depreciation/ Amortization	Net Book Value
Furniture and Equipment	S/L	50	300	3–5	$ 135,766	$ 112,967	$ 22,799
Software	S/L	300	300	3–5	282,138	192,265	89,873
Leasehold Improvements	S/L	300	N/A	10	111,324	92,921	18,403
Total					$ 529,228	$ 398,153	$ 131,075

At September 30, 2016, property and equipment consisted of the following:

Class of Property *(DOLLARS IN THOUSANDS)*	Depreciation/ Amortization Method	Capitalization Threshold for Individual Purchases	Capitalization Threshold for Bulk Purchases	Service Life (Years)	Acquisition Cost	Accumulated Depreciation/ Amortization	Net Book Value
Furniture and Equipment	S/L	50	300	3–5	$ 126,467	$ 107,649	$ 18,818
Software	S/L	300	300	3–5	245,231	158,891	86,340
Leasehold Improvements	S/L	300	N/A	10	108,476	87,726	20,750
Total					$ 480,174	$ 354,266	$ 125,908

Bulk purchases are acquisitions of a quantity of similar items that individually cost less than the threshold for individual purchases but collectively exceed the designated bulk purchase threshold of $300,000.

NOTE 8. LIABILITIES COVERED AND NOT COVERED BY BUDGETARY RESOURCES

The SEC recognizes liabilities that are covered by budgetary resources, liabilities that are not covered by budgetary resources, and liabilities that do not require the use of budgetary resources.

Liabilities that are covered by budgetary resources are liabilities incurred for which budgetary resources are available to the SEC during the reporting period without further Congressional action.

The SEC also recognizes liabilities not covered by budgetary resources. Budgetary and financial statement reporting requirements sometimes differ on the timing for the required recognition of an expense. For example, in the financial statements, annual leave expense must be accrued in the reporting period when the annual leave is earned. However, in the budget, annual leave is required to be recognized and funded in the fiscal year when the annual leave is either used or paid out to a separating employee, not when it is earned. As a result of this timing difference, accrued annual leave liability is classified as a liability "not covered by budgetary resources" as of the financial statement date.

Liabilities that do not require the use of budgetary resources are covered by assets that do not represent budgetary resources to the SEC. Liabilities that do not require the use of budgetary resources include registrant monies held temporarily until earned by the SEC and offsetting liabilities that correspond to non-entity assets that the SEC holds, such as collections and receivables from disgorgement and penalties, as discussed in *Note 1.L, Liabilities*.

At September 30, 2017, liabilities consisted of the following:

(DOLLARS IN THOUSANDS)	Liabilities Covered by Budgetary Resources	Liabilities Not Covered by Budgetary Resources	Liabilities Not Requiring Budgetary Resources	Total
Intragovernmental:				
Accounts Payable	$ 2,460	$ —	$ —	$ 2,460
Other Intragovernmental Liabilities				
Accrued Employee Benefits	7,279	—	—	7,279
Unfunded FECA and Unemployment Liability	—	896	—	896
Custodial Liability	—	—	173,896	173,896
Liability for Non-Entity Assets	—	—	580	580
Subtotal – Other Intragovernmental Liabilities	7,279	896	174,476	182,651
Total Intragovernmental	9,739	896	174,476	185,111
Accounts Payable	81,581	—	—	81,581
Actuarial FECA Liability	—	4,779	—	4,779
Other Liabilities				
Accrued Payroll and Benefits	35,369	—	—	35,369
Accrued Leave	—	75,752	—	75,752
Registrant Deposits	—	—	34,284	34,284
Liability for Disgorgement and Penalties (Note 16)	—	—	2,799,436	2,799,436
Contingent Liabilities (Note 10)	—	221,044	—	221,044
Other Accrued Liabilities				
Recognition of Lease Liability (Note 9)	—	9,013	—	9,013
Other	—	—	58	58
Subtotal – Other Liabilities	35,369	305,809	2,833,778	3,174,956
Total Liabilities	$ 126,689	$ 311,484	$ 3,008,254	$ 3,446,427

Other Liabilities (intragovernmental and governmental) totaled $3.4 billion as of September 30, 2017, of which all but $306 million is current. The non-current portion of Other Liabilities includes the appropriate portions of Accrued Employee Benefits, Unfunded FECA and Unemployment Liability, Accrued Leave, Contingent Liabilities, and Lease Liability. Current liabilities not covered by budgetary resources totaled $404 thousand as of September 30, 2017.

At September 30, 2016, liabilities consisted of the following:

(DOLLARS IN THOUSANDS)	Liabilities Covered by Budgetary Resources	Liabilities Not Covered by Budgetary Resources	Liabilities Not Requiring Budgetary Resources	Total
Intragovernmental:				
Accounts Payable	$ 5,381	$ —	$ —	$ 5,381
Other Intragovernmental Liabilities				
Accrued Employee Benefits	6,991	—	—	6,991
Unfunded FECA and Unemployment Liability	—	949	—	949
Custodial Liability	—	—	665,507	665,507
Liability for Non-Entity Assets	—	—	2,225	2,225
Subtotal – Other Intragovernmental Liabilities	6,991	949	667,732	675,672
Total Intragovernmental	12,372	949	667,732	681,053
Accounts Payable	76,200	—	—	76,200
Actuarial FECA Liability	—	5,558	—	5,558
Other Liabilities				
Accrued Payroll and Benefits	35,387	—	—	35,387
Accrued Leave	—	72,836	—	72,836
Registrant Deposits	—	—	36,652	36,652
Liability for Disgorgement and Penalties (Note 16)	—	—	3,089,688	3,089,688
Contingent Liabilities (Note 10)	—	10,800	—	10,800
Other Accrued Liabilities				
Recognition of Lease Liability (Note 9)	—	6,307	—	6,307
Other	—	—	102	102
Subtotal – Other Liabilities	35,387	89,943	3,126,442	3,251,772
Total Liabilities	$ 123,959	$ 96,450	$ 3,794,174	$ 4,014,583

Other Liabilities (intragovernmental and governmental) totaled $3.9 billion as of September 30, 2016, of which all but $90 million was current. The non-current portion of Other Liabilities includes the appropriate portions of the Unfunded FECA and Unemployment Liability, Accrued Leave, and Lease Liability. Current liabilities not covered by budgetary resources totaled $424 thousand as of September 30, 2016.

NOTE 9. LEASES

Operating Leases

At September 30, 2017, the SEC leased office space at 15 locations under operating lease agreements that expire between FY 2018 and FY 2029. The SEC paid $97 million for rent for the years ended September 30, 2017 and 2016, respectively.

The following table details expected future lease payments for (a) the full term of all non-cancelable leases with terms of more than one year and (b) the non-cancelable portion of all cancelable leases with terms of more than one year. "Non-cancelable" leases are leases for which the lease agreements do not provide an option for the lessee to cancel the lease prior to the end of the lease term. The total expected future lease payments reflect an estimate of base rent and contractually required costs.

Under existing commitments, expected future lease payments through FY 2022 and thereafter are as follows:

FISCAL YEAR *(DOLLARS IN THOUSANDS)*	Non-Cancelable Expected Future Lease Payments
2018	$ 85,072
2019	71,088
2020	39,752
2021	20,631
2022	4,235
2023 and thereafter	22,487
Total	$ 243,265

As discussed in *Note 14.C, Other Budgetary Disclosures*, $139 million of the above $243.3 million are unfunded obligations.

Expense Recognition of "Rent Holiday"

In the execution of lease agreements, many times lessors offer incentives for the occupation of office space. These include months of free rent at the occupied space or a temporary space while the new office is being prepared for occupancy. When a rent holiday occurs at the beginning of the lease term or at the beginning of occupancy of the temporary space, a rent expense is accrued, even though no payment is due. This accrued expense is recognized as an unfunded liability because funding will not be provided until the future period in which payment is due. The accrual and amortization of rent holiday discounts allow the rent expense to be allocated equally to each period of the lease term. The accrued lease liability for rent holidays was $9 million and $6.3 million as of September 30, 2017 and 2016, respectively.

NOTE 10. COMMITMENTS AND CONTINGENCIES

A. Commitments: Securities Investor Protection Act

The Securities Investor Protection Act of 1970 (SIPA), as amended, created the Securities Investor Protection Corporation (SIPC) to restore funds and securities to investors and to protect the securities markets from disruption following the failure of broker-dealers. Generally, if a brokerage firm is not able to meet its obligations to customers, then customers' cash and securities held by the brokerage firm are returned to customers on a pro rata basis. If sufficient funds are not available at the firm to satisfy customer claims, the reserve funds of SIPC are used to supplement the distribution, up to a ceiling of $500,000 per customer, including a maximum of $250,000 for cash claims.

SIPA authorizes SIPC to create a fund to maintain all monies received and disbursed by SIPC. SIPA gives SIPC the authority to borrow up to $2.5 billion from the SEC in the event that the SIPC Fund is or may appear insufficient for purposes of SIPA. To borrow the funds, SIPC must file with the SEC a statement of the uses of such a loan and a repayment plan, and then the SEC must certify to the Secretary of the Treasury that the loan is necessary to protect broker-dealer customers and maintain confidence in the securities markets and that the repayment plan provides as reasonable assurance of prompt repayment as may be feasible under the circumstances. The U.S. Treasury would make these funds available to the SEC through the purchase of notes or other obligating instruments issued by the SEC. Such notes or other obligating instruments would bear interest at a rate determined by the Secretary of the Treasury. As of September 30, 2017, the SEC had not loaned any funds to the SIPC, and there are no outstanding notes or other obligating instruments issued by the SEC.

Based on the estimated costs to complete ongoing customer protection proceedings, the current size of the SIPC Fund supplemented by SIPC's ongoing assessments on brokers is expected to provide sufficient funds to cover acknowledged customer claims. There are several broker-dealers that are being liquidated under SIPA or that have been referred to SIPC for liquidation that may result in additional customer claims. In the event that the SIPC Fund is or may reasonably appear to be insufficient for the purposes of SIPA, SIPC may seek a loan from the SEC.

B. Commitments and Contingencies: Investor Protection Fund

As discussed in *Note 1.E, Fund Accounting Structure*, the Investor Protection Fund is used to pay awards to whistleblowers if they voluntarily provide original information to the SEC and meet other conditions. Approved awards are between 10 and 30 percent of the monetary sanctions collected in the covered action or in a related action, with the actual percentage being determined at the discretion of the SEC, using criteria provided in the legislation and the related rules to implement the legislation adopted by the SEC.

A Preliminary Determination is an assessment, made by the Claims Review Staff appointed by the Director of the Division of Enforcement, as to whether the claim should be allowed or denied and, if allowed, what the proposed award percentage amount should be. A contingent liability is recognized when (a) a positive Preliminary Determination has been made by the Claims Review Staff, (b) collection has been made, and (c) the percentage to be paid can be reasonably estimated. A potential liability is disclosed but not recognized when a positive Preliminary Determination is expected and a collection has been received. A liability is recognized when a Final Determination has been

approved by the Commission and collection has been received. In all cases, the whistleblower award is not paid until amounts have been collected, a final order is issued by the Commission, and the appeal rights of all claimants on the matter have been exhausted.

The SEC recognized a contingent liability for potential future whistleblower awards for the period ended September 30, 2017 of $221.0 million. The SEC recognized a contingent liability for potential future whistleblower awards for the period ended September 30, 2016 of $10.8 million.

As of September 30, 2017, potential whistleblower payments for cases where positive Preliminary Determinations have not been made, but are reasonably possible, are estimated to range from $7.5 million to $22.6 million given the amount of current collections on those cases. Such claims do not meet the criteria for recognition as contingent liabilities in FY 2017. In the event that whistleblower award payments reduce the Investor Protection Fund total asset balance below $300 million, the Investor Protection Fund will be replenished, as described in *Note 1.Q, Budgets and Budgetary Accounting, Investor Protection Fund*.

As of September 30, 2016, potential whistleblower payments that were reasonably possible, but did not meet the criteria for recognition as contingent liabilities, were estimated to range from $303.9 million to $911.7 million.

C. Other Commitments

In addition to future lease commitments discussed in *Note 9, Leases*, the SEC is obligated for the purchase of goods and services that have been ordered, but not received. As of September 30, 2017, net obligations for all of the SEC's activities were $729.8 million, of which $126.7 million was delivered and unpaid. As of September 30, 2016, net obligations for all of SEC's activities were $852.4 million, of which $124.0 million was delivered and unpaid.

NOTE 11. FUNDS FROM DEDICATED COLLECTIONS

The SEC's funds from dedicated collections consist of transactions and balances recorded in its Salaries and Expenses Fund, Investor Protection Fund, and Reserve Fund. See *Note 1.E.1, Funds from Dedicated Collections*, and *Note 5, Investments*, for additional information about intragovernmental investments in Treasury securities.

For FY 2017, the assets, liabilities, net position, and net income from operations relating to funds from dedicated collections consisted of the following:

(DOLLARS IN THOUSANDS)	Salaries & Expenses	Investor Protection Fund	Reserve Fund	Eliminations	Total Funds From Dedicated Collections
Balance Sheet as of September 30, 2017					
ASSETS					
Fund Balance with Treasury	$ 7,080,452	$ 29,397	$ 85,524	$ —	$ 7,195,373
Investments, Net	—	292,283	—	—	292,283
Accounts Receivable, Net	137,765	—	—	—	137,765
Property and Equipment, Net	66,716	—	64,359	—	131,075
Advances and Prepayments	10,581	—	—	—	10,581
Total Assets	$ 7,295,514	$ 321,680	$ 149,883	$ —	$ 7,767,077
LIABILITIES					
Accounts Payable	$ 58,065	$ 20,838	$ 5,138	$ —	$ 84,041
FECA and Unemployment Liability	5,675	—	—	—	5,675
Accrued Payroll and Benefits	42,648	—	—	—	42,648
Accrued Leave	75,752	—	—	—	75,752
Contingent Liabilities	—	221,044	—	—	221,044
Other Accrued Liabilities	9,013	—	—	—	9,013
Total Liabilities	191,153	241,882	5,138	—	438,173
NET POSITION					
Cumulative Results of Operations	7,104,361	79,798	144,745	—	7,328,904
Total Net Position	7,104,361	79,798	144,745	—	7,328,904
Total Liabilities and Net Position	$ 7,295,514	$ 321,680	$ 149,883	$ —	$ 7,767,077
Statement of Net Cost for the year ended September 30, 2017					
Gross Program Costs	$ 1,702,587	$ 257,294	$ 43,051	$ (129)	$ 2,002,803
Less Earned Revenues Not Attributable to Program Costs	1,594,458	—	50,000	(129)	1,644,329
Net (Income) Cost from Operations	$ 108,129	$ 257,294	$ (6,949)	$ —	$ 358,474

(continued on next page)

(DOLLARS IN THOUSANDS)	Salaries & Expenses	Investor Protection Fund	Reserve Fund	Eliminations	Total Funds From Dedicated Collections
Statement of Changes in Net Position for the year ended September 30, 2017					
Cumulative Results of Operations:					
Net Position, Beginning of Period	$ 7,165,088	$ 334,358	$ 137,796	$ —	$ 7,637,242
Budgetary Financing Sources:					
Appropriations Used	19,731	—	—	—	19,731
Non-Exchange Revenue	—	2,734	—	—	2,734
Other Financing Sources:					
Imputed Financing	27,671	—	—	—	27,671
Net Income (Cost) from Operations	(108,129)	(257,294)	6,949	—	(358,474)
Net Change	(60,727)	(254,560)	6,949	—	(308,338)
Cumulative Results of Operations	7,104,361	79,798	144,745	—	7,328,904
Unexpended Appropriations:					
Budgetary Financing Sources:					
Appropriations Received	19,731	—	—	—	19,731
Appropriations Used	(19,731)	—	—	—	(19,731)
Total Unexpended Appropriations	—	—	—	—	—
Net Position, End of Period	$ 7,104,361	$ 79,798	$ 144,745	$ —	$ 7,328,904

NOTE 11. FUNDS FROM DEDICATED COLLECTIONS *(CONTINUED)*

For FY 2016, the assets, liabilities, net position, and net income from operations relating to funds from dedicated collections consisted of the following:

(DOLLARS IN THOUSANDS)	Salaries & Expenses	Investor Protection Fund	Reserve Fund	Eliminations	Total Funds From Dedicated Collections
Balance Sheet as of September 30, 2016					
ASSETS					
Fund Balance with Treasury	$ 7,139,871	$ 17,845	$ 83,318	$ —	$ 7,241,034
Investments, Net	—	350,271	—	—	350,271
Accounts Receivable, Net	128,444	—	—	—	128,444
Property and Equipment, Net	66,999	—	58,909	—	125,908
Advances and Prepayments	11,994	—	—	—	11,994
Total Assets	$ 7,347,308	$ 368,116	$ 142,227	$ —	$ 7,857,651
LIABILITIES					
Accounts Payable	$ 54,192	$ 22,958	$ 4,431	$ —	$ 81,581
FECA and Unemployment Liability	6,507	—	—	—	6,507
Accrued Payroll and Benefits	42,378	—	—	—	42,378
Accrued Leave	72,836	—	—	—	72,836
Contingent Liabilities	—	10,800	—	—	10,800
Other Accrued Liabilities	6,307	—	—	—	6,307
Total Liabilities	182,220	33,758	4,431	—	220,409
NET POSITION				—	
Cumulative Results of Operations	7,165,088	334,358	137,796	—	7,637,242
Total Net Position	7,165,088	334,358	137,796	—	7,637,242
Total Liabilities and Net Position	$ 7,347,308	$ 368,116	$ 142,227	$ —	$ 7,857,651
Statement of Net Cost for the year ended September 30, 2016					
Gross Program Costs	$ 1,648,723	$ 55,166	$ 34,330	$ (44)	$ 1,738,175
Less Earned Revenues Not Attributable to Program Costs	1,476,949	—	50,000	(44)	1,526,905
Net (Income) Cost from Operations	$ 171,774	$ 55,166	$ (15,670)	$ —	$ 211,270

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(DOLLARS IN THOUSANDS)	Salaries & Expenses	Investor Protection Fund	Reserve Fund	Eliminations	Total Funds From Dedicated Collections
Statement of Changes in Net Position for the year ended September 30, 2016					
Cumulative Results of Operations:					
Net Position, Beginning of Period	$ 7,173,973	$ 387,111	$ 122,126	$ —	$ 7,683,210
Budgetary Financing Sources:					
Appropriations Used	128,529	—	—	—	128,529
Non-Exchange Revenue	—	2,413	—	—	2,413
Other Financing Sources:					
Imputed Financing	34,360	—	—	—	34,360
Net Income (Cost) from Operations	(171,774)	(55,166)	15,670	—	(211,270)
Net Change	(8,885)	(52,753)	15,670	—	(45,968)
Cumulative Results of Operations	7,165,088	334,358	137,796	—	7,637,242
Unexpended Appropriations:					
Budgetary Financing Sources:					
Appropriations Received	128,529	—	—	—	128,529
Appropriations Used	(128,529)	—	—	—	(128,529)
Total Unexpended Appropriations	—	—	—	—	—
Net Position, End of Period	$ 7,165,088	$ 334,358	$ 137,796	$ —	$ 7,637,242

NOTE 12. COSTS AND EXCHANGE REVENUE

The Statement of Net Cost presents the SEC's results of operations for its major programs. The SEC assigns all costs incurred to 10 programs, consistent with its budget submissions. The full cost of the SEC's programs is the sum of (1) the costs of resources directly or indirectly consumed by those programs, and (2) the costs of identifiable supporting services provided by other responsibility segments within the agency. Typical examples of indirect costs include costs of general administrative services, technical support, security, rent, and operating and maintenance costs for buildings, equipment, and utilities. The SEC allocates support costs to its programs using activity-based cost accounting.

Intragovernmental costs arise from purchases of goods and services from other components of the federal government. In contrast, public costs arise from the purchase of goods and services from non-federal entities.

These exchange revenues are a means to recover all or most of the total cost of all SEC programs and to deposit excess collections from registrants to the U.S. Treasury General Fund. As a result, they offset the total costs of the organization in the Statement of Net Cost, rather than individual SEC programs. This presentation is consistent with the financial accounting concepts described in Statement of Federal Financial Accounting Concepts 2, *Entity and Display*.

The Statements of Net Cost, for the years ended September 30, 2017 and 2016, with a breakout of intragovernmental and public costs is presented below.

(DOLLARS IN THOUSANDS)	2017		
	Intragovernmental Gross Cost	Gross Cost with the Public	Total
SEC Programs:			
Enforcement	$ 87,841	$ 724,397	$ 812,238
Compliance Inspections and Examinations	66,008	323,699	389,707
Corporation Finance	28,027	138,424	166,451
Trading and Markets	15,734	81,507	97,241
Investment Management	11,094	55,105	66,199
Economic and Risk Analysis	8,981	68,013	76,994
General Counsel	8,900	43,129	52,029
Other Program Offices	13,631	76,393	90,024
Agency Direction and Administrative Support	37,878	197,655	235,533
Inspector General	3,270	13,132	16,402
Total Program Costs	$ 281,364	$ 1,721,454	$ 2,002,818
Less: Exchange Revenues			
Securities Transaction Fees			1,594,613
Securities Registration, Tender Offer, and Merger Fees			543,032
Other			504
Total Exchange Revenues			2,138,149
Net (Income) Cost from Operations			$ (135,331)

(DOLLARS IN THOUSANDS)	2016		
	Intragovernmental Gross Cost	Gross Cost with the Public	Total
SEC Programs:			
Enforcement	$ 87,838	$ 515,085	$ 602,923
Compliance Inspections and Examinations	64,220	311,668	375,888
Corporation Finance	29,233	134,374	163,607
Trading and Markets	15,970	76,719	92,689
Investment Management	11,504	54,284	65,788
Economic and Risk Analysis	8,701	57,968	66,669
General Counsel	9,054	42,335	51,389
Other Program Offices	13,810	69,506	83,316
Agency Direction and Administrative Support	38,231	180,493	218,724
Inspector General	3,072	11,856	14,928
Total Program Costs	$ 281,633	$ 1,454,288	$ 1,735,921
Less: Exchange Revenues			
Securities Transaction Fees			1,485,828
Securities Registration, Tender Offer, and Merger Fees			488,844
Other			248
Total Exchange Revenues			1,974,920
Net (Income) Cost from Operations			$ (238,999)

Intragovernmental exchange revenue was $460 thousand for the year ended September 30, 2017.

Intragovernmental exchange revenue was $193 thousand for the year ended September 30, 2016.

NOTE 13. CUSTODIAL REVENUES

The Statement of Custodial Activity reports custodial collections and accounts receivable on a modified cash basis of accounting. Cash collections and amounts transferred to U.S. Treasury General Fund are reported on a cash basis. The change in receivables and related payables are reported on an accrual basis. The SEC's Miscellaneous Receipt Accounts are used to account for custodial receipts pursuant to SEC enforcement actions and other small collections that will be sent to the U.S. Treasury. For more information about the SEC's Miscellaneous Receipt Accounts, see *Note 1.E, Fund Accounting Structure*. For information about the estimated collectability of accounts receivable, see *Note 1.I, Accounts Receivable and Allowance for Uncollectible Accounts*.

NOTE 14. STATUS OF BUDGETARY RESOURCES

A. Apportionment Categories of Obligations Incurred

Category A funds are those amounts that are subject to quarterly apportionment by OMB, meaning that a portion of the annual appropriation is not available to the agency until apportioned each quarter. Category B funds represent budgetary resources distributed by a specified time period, activity, project, object, or a combination of these categories. The SEC's Category B funds represent amounts apportioned at the beginning of the fiscal year for the SEC's reimbursable and Investor Protection Fund activities. The SEC's Reserve Fund is exempt from apportionment. For additional information, see *Note 1.E, Fund Accounting Structure*, and *Note 1.Q, Budgets and Budgetary Accounting*. For the years ended September 30, 2017 and 2016, the SEC incurred obligations against Category A, Category B, and Exempt funds as follows:

New Obligations and Upward Adjustments *(DOLLARS IN THOUSANDS)*	2017	2016
Direct Obligations		
Category A	$ 1,579,913	$ 1,612,813
Category B — Investor Protection Fund	47,050	57,932
Exempt From Apportionment — Reserve Fund	51,879	53,050
Total Direct Obligations	1,678,842	1,723,795
Reimbursable Obligations		
Category B	589	239
Total New Obligations and Upward Adjustments	$ 1,679,431	$ 1,724,034

Undelivered Orders at the End of the Period

Undelivered orders consist of orders of goods and services that the SEC has not received. The SEC's total undelivered orders are $614.4 million and $740.5 million for the years ended September 30, 2017 and 2016, respectively. The total undelivered orders contain unpaid and paid undelivered orders, with unpaid orders making up the majority of the total. The SEC's total unpaid undelivered orders are $603.8 and $728.5 for the years ended September 30, 2017 and 2016, respectively.

B. Explanation of Differences between the Statement of Budgetary Resources (SBR) and the Budget of the U.S. Government

A comparison between the FY 2017 SBR and the actual FY 2017 data in the President's budget cannot be presented, as the FY 2019 President's budget which will contain FY 2017 actual data is not yet available. The comparison will be presented in next year's financial statements. The comparison as of September 30, 2016 is presented below:

(DOLLARS IN MILLIONS)	Budgetary Resources	New Obligations and Upward Adjustments	Distributed Offsetting Receipts	Outlays, Net
Combined Statement of Budgetary Resources	$ 1,878	$ 1,724	$ 2	$ 251
FY 2016 Ending Balance: Comptroller General Decision B 322160, *Recording of Obligation for Multiple Year Contract*	213	—	—	—
Backdated Adjustment to Offsetting Collections for Filing Fee Registrants	—	—	—	(9)
Rounding	—	—	—	1
Budget of the U.S. Government	$ 2,091	$ 1,724	$ 2	$ 243

The differences between the FY 2016 SBR and the prior year column in the FY 2018 Budget of the U.S. Government exist because certain data elements are reported on the SBR differently than those same data elements are reported in the Budget.

The data elements reported differently are those used to report the SEC's recording of obligations in FY 2011 to reflect the impact of Comptroller General Decision B 322160, Securities and Exchange Commission—Recording of Obligation for Multiple-Year Contract and the subsequent adjustment and liquidation of those obligations. In consultation with OMB, in FY 2011 the SEC recognized obligations for leases entered into in FY 2010 and prior. The recognition of these lease obligations resulted in an unfunded obligation (deficiency) of $778 million.

In the Budget, the unfunded obligation is not included in the beginning of the year unobligated balance brought forward, but instead is reported in a separate schedule of the SEC's Budget titled "Unfunded Deficiencies."

Based on an agreement with OMB, the SEC funds the deficiency over time as budgetary resources become available for current year lease operations and as the prior year unfunded lease obligation amounts are recovered. At the end of FY 2016, the SEC's SBR included $213 million in remaining unfunded obligations after the SEC funded $73 million for current year lease operations. The SEC SBR for FY 2017 presents this balance as part of the beginning of the year unobligated balance brought forward.

The differences in Outlays, Net is the result of an FY 2016 adjustment of $9.1 million to the Fund Balance with Treasury account for the Salaries and Expenses Fund, and a rounding variance of -$1million.

C. Other Budgetary Disclosures

General Provisions of Appropriation

The SEC's annual Appropriations Act contains general provisions that limit the amount that can be obligated for international conferences, International Organization of Securities Commission (IOSCO) dues, and representation expenses. The Act also requires the SEC to fund its Office of Inspector General with a minimum of $14,700,000 and the Division of Economic and Risk Analysis with a minimum of $72,049,000 in new budget authority.

Change in Legal Interpretation for Lease Obligations

The SEC was granted independent leasing authority in 1990. Based on a legal review of its statutory authority at the time, the SEC adopted a policy of obligating only the annual portion of lease payments due each year. On October 3, 2011, the Government Accountability Office (GAO) issued a decision that this longstanding practice of recording lease obligations only on an annual basis violated the recording statute, 31 U.S.C. sect. 1501(a)(1). Specifically, the GAO's decision was that the SEC lacks statutory authority to obligate an amount less than the government's total obligation. If the SEC lacks sufficient budget authority to cover this obligation, the SEC should report a violation of the Antideficiency Act.

The SEC recorded obligations in the same manner for all its leasing actions between the time the agency was granted independent leasing authority in 1990 and 2010. Further, the agency did not have sufficient remaining unobligated funds in the years in which the various leases were entered to cover the full obligations associated with those leases. As a result, the agency recorded unfunded obligations totaling $778 million for leases executed between 1990 and

2010 in FY 2011. The SEC appropriately obligated the government's total financial responsibility for lease actions that were executed in FY 2011 and thereafter.

Unfunded lease obligations totaled $139 million and $213 million as of September 30, 2017 and 2016, respectively. Accrual accounting requires expenses to be recognized in the period in which the expenses are incurred. Because future lease expenses are not an expense of the current fiscal year, they are not reported as expenses or liabilities in the current fiscal year. See *Note 9, Leases*, for additional information.

Borrowing Authority

See *Note 10.A, Commitments: Securities Investor Protection Act*, for information on the SEC's borrowing authority.

NOTE 15. RECONCILIATION OF NET COST OF OPERATIONS TO BUDGET

For the years ended September 30, 2017 and 2016:

(DOLLARS IN THOUSANDS)	2017	2016
RESOURCES USED TO FINANCE ACTIVITIES:		
Budgetary Resources Obligated:		
New Obligations and Upward Adjustments (Note 14)	$ 1,679,431	$ 1,724,034
Less: Spending Authority from Offsetting Collections, Recoveries, and Downward Adjustments of Prior Year Unfunded Lease Obligations	(1,625,967)	(1,526,772)
Less: Reserve Fund Appropriations	(50,000)	(50,000)
Net Obligations	3,464	147,262
Other Resources:		
Imputed Financing from Cost Absorbed by Others	27,671	34,360
Total Resources Used to Finance Activities	31,135	181,622
RESOURCES USED TO FINANCE ITEMS NOT PART OF THE NET COST OF OPERATIONS:		
Change in Budgetary Resources Obligated for Goods, Services, and Benefits Ordered But Not Yet Provided	126,817	60,942
Resources that Finance the Acquisition of Assets Capitalized on the Balance Sheet	(58,226)	(69,066)
Total Resources Used to Finance Items Not Part of the Net Cost of Operations	68,591	(8,124)
Total Resources Used to Finance the Net Cost of Operations	99,726	173,498
COMPONENTS OF NET COST OF OPERATIONS THAT WILL NOT REQUIRE OR GENERATE RESOURCES IN THE CURRENT PERIOD:		
Components Requiring or Generating Resources in Future Periods:		
Change in Accrued Leave Liability	2,916	5,201
Change in Revenue Receivables Not Generating Resources Until Collected	(9,346)	(9,572)
Change in Lease Liability	2,706	(133)
Change in Unfunded Liability	209,412	(4,484)
Total Components of Net Cost of Operations that will Require or Generate Resources in Future Periods	205,688	(8,988)
Components not Requiring or Generating Resources:		
Depreciation and Amortization	52,716	46,743
Revaluation of Assets or Liabilities	344	17
Non-Entity Filing Fee Revenue, Net	(493,761)	(450,214)
Other Costs that will not Require or Generate Resources	(44)	(55)
Total Components of Net Cost of Operations that will not Require or Generate Resources in the Future Period	(440,745)	(403,509)
Total Components of Net Cost of Operations that will not Require or Generate Resources in the Current Period	(235,057)	(412,497)
Net (Income) Cost from Operations	$ (135,331)	$ (238,999)

Components of net cost of operations that will not require or generate budgetary resources represent required timing differences in the Statement of Net Cost and the Statement of Budgetary Resources.

For example, as noted in *Note 1.L, Liabilities*, annual leave that is earned but not either taken or paid out to separating employees by the end of the fiscal year is required to be reported as an expense in the financial

statements in the year when it is earned, but it is required to be funded by budgetary resources in the future fiscal year when it is either used or paid out to separating employees. In the reconciliation above, it is reported as a component of net cost that will not require resources in the current period.

Another example is depreciation expense. In budgetary reporting, the entire cost of a depreciable asset is recognized in the period when the asset is purchased. However, in financial statement reporting, accrual accounting requires the cost of such assets to be allocated among the reporting periods that represent the estimated useful life of the asset. In the reconciliation above, depreciation is recognized as a "component not requiring or generating resources."

An example of a revenue that does not generate budgetary resources is Non-Entity Filing Fee Revenue, Net. "Non-entity" filing fee revenue is not available to the SEC for use in its operations; accordingly, this revenue does not generate budgetary resources for the SEC.

NOTE 16. DISGORGEMENT AND PENALTIES

The SEC's non-entity assets include disgorgement, penalties, and interest assessed against securities law violators by the Commission or a federal court. The SEC also recognizes an equal and offsetting liability for these non-entity assets, as discussed in *Note 1.L, Liabilities*.

When the Commission or court issues an order for the SEC to collect disgorgement, penalties, and interest from securities law violators, the SEC establishes an account receivable due to the SEC. Upon collection, the SEC may (a) hold receipts in the Disgorgement and Penalty Deposit Fund as FBWT or Treasury investments pending distribution to harmed investors, (b) deposit receipts in the U.S. Treasury General Fund or, (c) transfer amounts to the Investor Protection Fund. The situations where funds would not be held for distribution to harmed investors arise when the SEC either determines it is not practical to return funds to investors or when court orders expressly state that funds are to be remitted to the U.S. Treasury. The determination as to whether funds not held for distribution to harmed investors will be deposited in the U.S. Treasury or transferred to the Investor Protection Fund is made in accordance with the provisions of the Dodd-Frank Act, and is dependent on the balance in the Investor Protection Fund on the day the amounts are collected.

Disbursements related to disgorgement and penalties include distributions to harmed investors, payments to tax authorities, and fees paid to plan administrators and the Bureau of the Fiscal Service. The SEC does not record accounts receivable on its financial statements for any amounts ordered to another government entity such as a court, or a non-governmental entity such as a receiver. See *Note 1.R, Disgorgement and Penalties*, and *Note 2, Entity and Non-Entity Assets*.

In FY 2017, total Disgorgement and Penalties assets of $3.0 billion include $2.8 billion held for distribution to harmed investors and $174 million to be transferred to the U.S. Treasury General Fund. In FY 2016, total Disgorgement and Penalties assets of $3.8 billion included $3.1 billion held for distribution to harmed investors and $665 million to be transferred to the U.S. Treasury General Fund.

At September 30, the net inflows and outflows for FBWT, Investments, and Accounts Receivable related to disgorgement and penalties consisted of the following:

(DOLLARS IN THOUSANDS)	2017	2016
Fund Balance with Treasury:		
Beginning Balance	$ 351,735	$ 321,000
Collections	2,078,713	1,710,192
Purchases and Redemptions of Treasury Securities	52,532	(30,204)
Disbursements	(245,792)	(37,964)
Transfers and Deposits to the U.S. Treasury General Fund	(1,962,021)	(1,611,289)
Total Fund Balance with Treasury (Note 2)	275,167	351,735
Cash and Other Monetary Assets:		
Beginning Balance	27	13
Net Activity	(19)	14
Total Cash and Other Monetary Assets (Notes 2 and 4)	8	27
Investments, Net:		
Beginning Balance	2,506,317	2,468,813
Net Activity	(35,072)	37,504
Total Investments, Net (Notes 2 and 5)	2,471,245	2,506,317
Accounts Receivable, Net:		
Beginning Balance	896,328	738,705
Net Activity	(669,804)	157,623
Total Accounts Receivable, Net (Notes 2 and 6)	226,524	896,328
Total Disgorgement and Penalties	$ 2,972,944	$ 3,754,407

NOTE 17. STATEMENT OF CHANGES IN NET POSITION

In FY 2017, the negative $493,805 thousand in "Other" Financing Sources reported in the Statement of Changes in Net Position consists of $493,761 thousand in securities registration, tender offer, merger, and other fees from registrants ("filing fees") and $44 thousand in Freedom of Information Act (FOIA) fee collected, or to be collected, for deposit into the U.S. Treasury General Fund.

In FY 2016, the negative $450,269 thousand consists $450,214 thousand in filing fees and $55 thousand in FOIA revenues collected, or to be collected, for deposit into the U.S. Treasury General Fund.

REQUIRED SUPPLEMENTARY INFORMATION (UNAUDITED)

This section provides the Required Supplementary Information as prescribed by OMB Circular A-136, *Financial Reporting Requirements*.

U.S. SECURITIES AND EXCHANGE COMMISSION

Combining Statements of Budgetary Resources by Fund

For the year ended September 30, 2017

(DOLLARS IN THOUSANDS)	Salaries and Expenses and Other Funds	Investor Protection Fund	Reserve Fund	Total
	X0100, 1435, 3220, 3875	5567	5566	
BUDGETARY RESOURCES:				
Unobligated Balance, Brought Forward, October 1	$ (188,052)	$ 340,219	$ 1,848	$ 154,015
Recoveries of Prior Year Unpaid Obligations	38,236	—	1,318	39,554
Other Changes in Unobligated Balance	599	—	—	599
Unobligated Balance from Prior Year Budget Authority, Net	(149,217)	340,219	3,166	194,168
Appropriations (Discretionary and Mandatory)	19,731	4,218	49,925	73,874
Spending Authority from Offsetting Collections (Discretionary and Mandatory)	1,586,559	—	—	1,586,559
Total Budgetary Resources	$ 1,457,073	$ 344,437	$ 53,091	$ 1,854,601
STATUS OF BUDGETARY RESOURCES:				
New Obligations and Upward Adjustments (Total) (Note 14)	$ 1,580,502	$ 47,050	$ 51,879	$ 1,679,431
Unobligated Balance, End of Year:				
Apportioned, Unexpired Accounts	12,793	297,387	—	310,180
Exempt from Apportionment, Unexpired Accounts	—	—	1,212	1,212
Unapportioned, Unexpired Accounts	(136,222)	—	—	(136,222)
Unobligated Balance, End of Year (Total)	(123,429)	297,387	1,212	175,170
Total Budgetary Resources	$ 1,457,073	$ 344,437	$ 53,091	$ 1,854,601
CHANGE IN OBLIGATED BALANCE:				
Unpaid Obligations:				
Unpaid Obligations, Brought Forward, October 1 (Gross)	$ 778,117	$ 22,958	$ 51,371	$ 852,446
New Obligations and Upward Adjustments	1,580,502	47,050	51,879	1,679,431
Outlays (Gross)	(1,664,889)	(49,170)	(47,794)	(1,761,853)
Recoveries of Prior Year Unpaid Obligations	(38,236)	—	(1,318)	(39,554)
Unpaid Obligations, End of Year	655,494	20,838	54,138	730,470
Uncollected Payments:				
Uncollected Payments, Federal Sources, Brought Forward, October 1	(25)	—	—	(25)
Change in Uncollected Payments, Federal Sources	(675)	—	—	(675)
Uncollected Payments, Federal Sources, End of Year	(700)	—	—	(700)
Obligated Balance, End of Year	654,794	20,838	54,138	729,770
Memorandum (non-add) entries:				
Obligated Balance, Start of Year	$ 778,092	$ 22,958	$ 51,371	$ 852,421
Obligated Balance, End of Year	$ 654,794	$ 20,838	$ 54,138	$ 729,770
BUDGET AUTHORITY AND OUTLAYS, NET:				
Budget Authority, Gross (Discretionary and Mandatory)	$ 1,606,290	$ 4,218	$ 49,925	$ 1,660,433
Actual Offsetting Collections (Discretionary and Mandatory)	(1,585,738)	—	—	(1,585,738)
Change in Uncollected Customer Payments from Federal Sources (Discretionary and Mandatory)	(675)	—	—	(675)
Recoveries of Prior Year Paid Obligations (Discretionary and Mandatory)	599	—	—	599
Budget Authority, Net (Discretionary and Mandatory)	$ 20,476	$ 4,218	$ 49,925	$ 74,619
Outlays, Gross (Discretionary and Mandatory)	$ 1,664,889	$ 49,170	$ 47,794	$ 1,761,853
Actual Offsetting Collections (Discretionary and Mandatory)	(1,585,738)	—	—	(1,585,738)
Outlays, Net (Discretionary and Mandatory)	79,151	49,170	47,794	176,115
Distributed Offsetting Receipts	(570)	(4,478)	—	(5,048)
Agency Outlays, Net (Discretionary and Mandatory)	$ 78,581	$ 44,692	$ 47,794	$ 171,067

The accompanying notes are an integral part of these financial statements.

Combining Statements of Budgetary Resources by Fund

For the year ended September 30, 2016

(DOLLARS IN THOUSANDS)	Salaries and Expenses and Other Funds	Investor Protection Fund	Reserve Fund	Total
	X0100, 1435, 3220, 3875	5567	5566	
BUDGETARY RESOURCES:				
Unobligated Balance, Brought Forward, October 1	$ (235,222)	$ 397,449	$ 328	$ 162,555
Recoveries of Prior Year Unpaid Obligations	52,753	–	4,195	56,948
Other Changes in Unobligated Balance	2,233	–	–	2,233
Unobligated Balance from Prior Year Budget Authority, Net	(180,236)	397,449	4,523	221,736
Appropriations (Discretionary and Mandatory)	128,528	701	50,376	179,605
Spending Authority from Offsetting Collections (Discretionary and Mandatory)	1,476,708	–	–	1,476,708
Total Budgetary Resources	$ 1,425,000	$ 398,150	$ 54,899	$ 1,878,049
STATUS OF BUDGETARY RESOURCES:				
New Obligations and Upward Adjustments (Total) (Note 14)	$ 1,613,052	$ 57,931	$ 53,051	$ 1,724,034
Unobligated Balance, End of Year:				
Apportioned, Unexpired Accounts	18,645	340,219	–	358,864
Exempt from Apportionment, Unexpired Accounts	–	–	1,848	1,848
Unapportioned, Unexpired Accounts	(206,697)	–	–	(206,697)
Unobligated Balance, End of Year (Total)	(188,052)	340,219	1,848	154,015
Total Budgetary Resources	$ 1,425,000	$ 398,150	$ 54,899	$ 1,878,049
CHANGE IN OBLIGATED BALANCE:				
Unpaid Obligations:				
Unpaid Obligations, Brought Forward, October 1 (Gross)	$ 851,013	$ 17	$ 54,813	$ 905,843
New Obligations and Upward Adjustments	1,613,052	57,931	53,051	1,724,034
Outlays (Gross)	(1,633,195)	(34,990)	(52,298)	(1,720,483)
Recoveries of Prior Year Unpaid Obligations	(52,753)	–	(4,195)	(56,948)
Unpaid Obligations, End of Year	778,117	22,958	51,371	852,446
Uncollected Payments:				
Uncollected Payments, Federal Sources, Brought Forward, October 1	(26)	–	–	(26)
Change in Uncollected Payments, Federal Sources	1	–	–	1
Uncollected Payments, Federal Sources, End of Year	(25)	–	–	(25)
Obligated Balance, End of Year	778,092	22,958	51,371	852,421
Memorandum (non-add) entries:				
Obligated Balance, Start of Year	$ 850,987	$ 17	$ 54,813	$ 905,817
Obligated Balance, End of Year	$ 778,092	$ 22,958	$ 51,371	$ 852,421
BUDGET AUTHORITY AND OUTLAYS, NET:				
Budget Authority, Gross (Discretionary and Mandatory)	$ 1,605,236	$ 701	$ 50,376	$ 1,656,313
Actual Offsetting Collections (Discretionary and Mandatory)	(1,469,825)	–	–	(1,469,825)
Change in Uncollected Customer Payments from Federal Sources (Discretionary and Mandatory)	1	–	–	1
Recoveries of Prior Year Paid Obligations (Discretionary and Mandatory)	2,233	–	–	2,233
Budget Authority, Net (Discretionary and Mandatory)	$ 137,645	$ 701	$ 50,376	$188,722
Outlays, Gross (Discretionary and Mandatory)	$ 1,633,195	$ 34,990	$ 52,298	$ 1,720,483
Actual Offsetting Collections (Discretionary and Mandatory)	(1,469,825)	–	–	(1,469,825)
Outlays, Net (Discretionary and Mandatory)	163,370	34,990	52,298	250,658
Distributed Offsetting Receipts	(836)	(752)	–	(1,588)
Agency Outlays, Net (Discretionary and Mandatory)	$ 162,534	$ 34,238	$ 52,298	$ 249,070

The accompanying notes are an integral part of these financial statements.

INVESTOR PROTECTION FUND FINANCIAL STATEMENTS

U.S. SECURITIES AND EXCHANGE COMMISSION
INVESTOR PROTECTION FUND

Balance Sheets

As of September 30, 2017 and 2016

(DOLLARS IN THOUSANDS)	2017	2016
ASSETS:		
Intragovernmental:		
Fund Balance with Treasury (Note 2)	$ 29,397	$ 17,845
Investments, Net (Note 3)	292,283	350,271
Total Assets	$ 321,680	$ 368,116
LIABILITIES (NOTE 4):		
Accounts Payable	$ —	$ —
Total Intragovernmental	—	—
Accounts Payable	20,838	22,958
Contingent Liabilities (Note 5)	221,044	10,800
Total Liabilities	241,882	33,758
Commitments and Contingencies (Note 5)		
NET POSITION:		
Cumulative Results of Operations – Funds from Dedicated Collections	79,798	334,358
Total Net Position – Funds from Dedicated Collections	79,798	334,358
Total Net Position	79,798	334,358
Total Liabilities and Net Position	$ 321,680	$ 368,116

The accompanying notes are an integral part of these financial statements.

U.S. SECURITIES AND EXCHANGE COMMISSION
INVESTOR PROTECTION FUND

Statements of Net Cost

For the years ended September 30, 2017 and 2016

(DOLLARS IN THOUSANDS)	2017	2016
PROGRAM COSTS (NOTE 6):		
Awards to Whistleblowers	$ 257,165	$ 55,122
Employee Suggestion Program	129	44
Total Program Costs	257,294	55,166
Net (Income) Cost from Operations	$ 257,294	$ 55,166

The accompanying notes are an integral part of these financial statements.

U.S. SECURITIES AND EXCHANGE COMMISSION
INVESTOR PROTECTION FUND

Statements of Changes in Net Position

For the years ended September 30, 2017 and 2016

(DOLLARS IN THOUSANDS)	2017	2016
CUMULATIVE RESULTS OF OPERATIONS— FUNDS FROM DEDICATED COLLECTIONS:		
Beginning Balances	$ 334,358	$ 387,111
Budgetary Financing Sources:		
Non-Exchange Revenue	2,734	2,413
Total Financing Sources	2,734	2,413
Net Income (Cost) from Operations	(257,294)	(55,166)
Net Change	(254,560)	(52,753)
Cumulative Results of Operations	79,798	334,358
Net Position, End of Period	$ 79,798	$ 334,358

The accompanying notes are an integral part of these financial statements.

U.S. SECURITIES AND EXCHANGE COMMISSION
INVESTOR PROTECTION FUND

Statements of Budgetary Resources

For the years ended September 30, 2017 and 2016

(DOLLARS IN THOUSANDS)	2017	2016
BUDGETARY RESOURCES:		
Unobligated Balance, Brought Forward, October 1	$ 340,219	$ 397,449
Appropriations (Discretionary and Mandatory)	4,218	701
Total Budgetary Resources	$ 344,437	$ 398,150
STATUS OF BUDGETARY RESOURCES:		
New Obligations and Upward Adjustments (Total)	$ 47,050	$ 57,931
Unobligated Balance, End of Year:		
Apportioned, Unexpired Accounts	297,387	340,219
Unobligated Balance, End of Year (Total)	297,387	340,219
Total Budgetary Resources	$ 344,437	$ 398,150
CHANGE IN OBLIGATED BALANCE:		
Unpaid Obligations:		
Unpaid Obligations, Brought Forward, October 1 (Gross)	$ 22,958	$ 17
New Obligations and Upward Adjustments	47,050	57,931
Outlays (Gross)	(49,170)	(34,990)
Unpaid Obligations, End of Year	$ 20,838	$ 22,958
BUDGET AUTHORITY AND OUTLAYS, NET:		
Budget Authority, Gross (Discretionary and Mandatory)	$ 4,218	$ 701
Budget Authority, Net (Discretionary and Mandatory)	$ 4,218	$ 701
Outlays, Gross (Discretionary and Mandatory)	$ 49,170	$ 34,990
Outlays, Net (Discretionary and Mandatory)	49,170	34,990
Distributed Offsetting Receipts	(4,478)	(752)
Agency Outlays, Net (Discretionary and Mandatory)	$ 44,692	$ 34,238

The accompanying notes are an integral part of these financial statements.

NOTES TO THE INVESTOR PROTECTION FUND FINANCIAL STATEMENTS

U.S. SECURITIES AND EXCHANGE COMMISSION

As of September 30, 2017 and 2016

NOTE 1. SIGNIFICANT ACCOUNTING POLICIES

A. Reporting Structure

The U.S. Securities and Exchange Commission (SEC) is an independent agency of the U.S. Government established pursuant to the Securities Exchange Act of 1934 (Exchange Act), charged with regulating this country's capital markets. The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank Act) established the Securities and Exchange Commission Investor Protection Fund. The Investor Protection Fund provides funding for the Dodd-Frank Whistleblower Program and finances the operations of the SEC Office of Inspector General's Employee Suggestion Program. The Investor Protection Fund is a fund within the SEC, and these financial statements present a segment of the SEC's financial activity.

B. Basis of Presentation and Accounting

The accompanying financial statements present the financial position, net cost of operations, changes in net position, and budgetary resources of the Investor Protection Fund as required by Exchange Act Section 21F(g)(5). The Act requires a complete set of financial statements that includes a balance sheet, income statement, and cash flow analysis. The legislative requirements to prepare an income statement and cash flow analysis are addressed by the Statement of Net Cost and *Note 2, Fund Balance with Treasury*, respectively.

The SEC's books and records serve as the source of the information presented in the accompanying financial statements. The SEC is a federal reporting entity, in accordance with the provisions of the Accountability of Tax Dollars Act of 2002. The SEC's financial statements are prepared in conformity with generally accepted accounting principles (GAAP) for the federal government, and are presented in conformity with the Office of Management and Budget (OMB) Circular A-136, *Financial Reporting Requirements*. As a stand-alone entity, the Investor Protection Fund does not meet the criteria provided in the CFO Act and the Accountability of Tax Dollars Act to constitute a "federal reporting entity." Audited financial statements of the Investor Protection Fund are a special-purpose report required by legislation. In addition, federal GAAP and OMB Circular A-136 do not provide for either an Income Statement or a cash flow analysis. However, the Investor Protection Fund financial statements are consistent with the SEC financial statements, except for additional elements, such as cash flow analysis, that are required by legislation.

The agency classifies assets, liabilities, revenues, and costs in these financial statements according to the type of entity associated with the transactions. Intragovernmental assets and liabilities are those due from or to other federal entities, including other funds within the SEC. Intragovernmental revenues and costs result from transactions with other federal entities, including other funds within the SEC.

The Balance Sheet, Statement of Net Cost, and Statement of Changes in Net Position are prepared using the accrual basis of accounting. Accordingly, revenues are recognized when earned and expenses are recognized when incurred without regard to the receipt or payment of cash. These principles differ from the budgetary accounting and reporting principles on which the Statement of Budgetary Resources is prepared. A reconciliation of differences, if any, between the accru-

al-based Statement of Net Cost and the budgetary-based Statement of Budgetary Resources is presented in *Note 8, Reconciliation of Net Cost of Operations to Budget*.

C. Use of Estimates

The preparation of financial statements on the accrual basis of accounting requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities. These estimates and assumptions include, but are not limited to, the disclosure of potential future whistleblower award payments as of the date of the financial statements. Actual results may differ from these estimates.

D. Intra- and Inter-Agency Relationships

Transactions with Other SEC Funds

The Investor Protection Fund is comprised of a single Treasury Appropriation Fund Symbol. The Investor Protection Fund is the recipient of non-exchange revenues collected by the SEC. Amounts transferred to the Investor Protection Fund are classified as "retained by the SEC" because the Investor Protection Fund is a fund within the SEC. These intra-agency transfers are required because the Investor Protection Fund finances the operations of the SEC Office of Inspector General's Employee Suggestion Program.

Transactions with Other Federal Agencies

Whistleblower payments may be made from the Investor Protection Fund as a result of monetary sanctions paid to other federal agencies in related actions, but only if there has been a Commission enforcement action resulting in sanctions of a million dollars or greater and the Commission has determined that the whistleblower is eligible for an award and recommended the percentage. In those instances, the SEC remains liable for paying the whistleblower. However, in instances where a whistleblower has already received an award from the Commodity Futures Trading Commission, the whistleblower is not entitled to an award from the SEC.

E. Funds from Dedicated Collections

A fund from dedicated collections is financed by specifically identified revenues, provided to the government by non-federal sources, often supplemented by other financing sources, which remain available over time. These specifically identified revenues and other financing sources are required by statute to be used for designated activities, benefits or purposes, and must be accounted for separately from the government's general revenues. Investor Protection Fund resources are funds from dedicated collections and may only be used for the purposes specified by the Dodd-Frank Act.

F. Entity Assets

Assets that an agency is authorized to use in its operations are entity assets. The SEC is authorized to use all funds in the Investor Protection Fund for the purposes specified by the Dodd-Frank Act. Accordingly, all assets are recognized as entity assets.

G. Fund Balance with Treasury

Fund Balance with Treasury reflects amounts the Investor Protection Fund holds in the U.S. Treasury that have not been invested in federal securities. The SEC conducts all of its banking activity in accordance with directives issued by the U.S. Department of the Treasury's Bureau of the Fiscal Service.

H. Investments

The SEC has authority to invest amounts in the Investor Protection Fund in overnight and short-term, market-based Treasury securities. The interest earned on the investments is a component of the Fund and is available to be used for expenses of the Investor Protection Fund. Additional details regarding Investor Protection Fund investments are provided in *Note 3, Investments*.

I. Liabilities

The SEC records liabilities for probable future outflows or other sacrifices of resources as a result of events that have occurred as of the Balance Sheet date. The Investor

Protection Fund's liabilities consist of amounts payable to whistleblowers and amounts recognized as contingent liabilities for whistleblower awards.

The SEC recognizes liabilities that are covered by budgetary resources and liabilities that are not covered by budgetary resources. Budgetary and financial statement reporting requirements sometimes differ on the timing for the required recognition of an expense. Liabilities that are covered by budgetary resources are liabilities incurred for which budgetary resources are available to the SEC without further Congressional action. Refer to *Note 4, Liabilities Covered and Not Covered by Budgetary Resources*, for detailed information regarding liabilities covered and not covered by budgetary resources.

The Dodd-Frank Act and the SEC implementing regulations establish the eligibility criteria for whistleblower awards. Refer to *Note 5, Commitments and Contingencies*, for additional information regarding the disclosure and recognition of actual and contingent liabilities for whistleblower awards.

J. Program Costs

The Investor Protection Fund reimburses the SEC's Salaries and Expenses account (X0100) for expenses incurred by the Office of Inspector General to administer the Employee Suggestion Program. The Investor Protection Fund also finances payments to whistleblowers under Section 21F of the Exchange Act.

K. Non-Exchange Revenue

Disgorgement and Penalty Transfers

Non-exchange revenue arises from the government's ability to demand payment. The Investor Protection Fund is financed through the receipt of monetary sanctions collected by the SEC in judicial or administrative actions brought by the SEC under the securities laws that are not either: (1) added to the disgorgement fund or other fund under Section 308 of the Sarbanes-Oxley Act of 2002 (15 U.S.C. 7246) or (2) otherwise distributed to victims of a violation of the securities laws. The Investor Protection Fund recognizes non-exchange revenue for disgorgement and penalty amounts transferred into the fund from the SEC's Disgorgement and Penalties Fund (X6563). No sanction collected by the SEC can be deposited into the Investor Protection Fund if the balance in the fund exceeds $300 million on the day of collection.

Interest Earnings on Investments with Treasury

Interest earned from investments in U.S. Treasury securities is classified in the same way as the predominant source of revenue to the fund. The Investor Protection Fund is financed through the receipt of non-exchange revenues and thus interest earnings are also recognized as non-exchange revenues.

L. Budgets and Budgetary Accounting

The Investor Protection Fund (X5567) is a special fund established with a permanent indefinite appropriation, with authority to retain revenues and other financing sources not used in the current period for future use. The Dodd-Frank Act provides that the Fund is available to the SEC without further appropriation or fiscal year limitation for the purpose of paying awards to whistleblowers and funding the activities of the Office of Inspector General's Employee Suggestion Program. However, the SEC is required to request and obtain an annual apportionment from OMB to use these funds.

The resources of the Investor Protection Fund are apportioned under Category B authority, which means that the funds represent budgetary resources distributed by a specified project and are not subject to quarterly apportionment. Thus, all obligations incurred as presented on the Statement of Budgetary Resources are derived from Category B funds.

NOTE 2. FUND BALANCE WITH TREASURY

The Fund Balance with Treasury by type of fund and Status of Fund Balance with Treasury as of September 30, 2017 and 2016 consisted of the following:

(DOLLARS IN THOUSANDS)	2017	2016
Fund Balances:		
Special Fund	$ 29,397	$ 17,845
Total Fund Balance with Treasury	$ 29,397	$ 17,845
Status of Fund Balance with Treasury:		
Unobligated Balance		
Available	8,249	(5,165)
Unavailable	310	52
Obligated Balance not Yet Disbursed	20,838	22,958
Total Status of Fund Balance with Treasury	$ 29,397	$ 17,845

Unobligated balances reported for the status of Fund Balance with Treasury do not agree with the amounts reported in the Statement of Budgetary Resources due to the fact that funds for unobligated balances are held in investments as well as in Fund Balance with Treasury.

There were no differences between the Fund Balance reflected in the Investor Protection Fund financial statements and the balance in the Treasury accounts.

Cash Flow

The Investor Protection Fund cash flows during FY 2017 consisted of:

- Net cash inflows from investment redemptions of $56.2 million,
- Net cash inflows for investment interest of $4.5 million (which includes $9.3 million of interest collections, less $5 million of premiums paid, and $128 thousand in discounts received), and
- Net cash outflows for payment of whistleblower awards totaling $23 million for amounts that were awarded during FY 2016 and $26.1 million for amounts that were awarded during FY 2017, and the cost of operating the Office of Inspector General's Employee Suggestion Program of $129 thousand.

Cash flows during FY 2016 consisted of:

- Net cash inflows from investment redemptions of $49.7 million,
- Net cash inflows for investment interest of $752 thousand (which includes $9.1 million of interest collections, less $8.4 million of premiums paid, and $48 thousand in discounts received), and
- Net cash outflows for payment of whistleblower awards totaling $17 thousand for amounts that were awarded during FY 2015 and $34.9 million for amounts that were awarded during FY 2016, and the cost of operating the Office of Inspector General's Employee Suggestion Program of $44 thousand.

NOTE 3. INVESTMENTS

The SEC invests funds in overnight and short-term non-marketable market-based Treasury bills. The SEC records the value of its investments in Treasury bills at cost and amortizes any premium or discount on a straight-line basis (S/L) through the maturity date of these securities. Non-marketable market-based Treasury securities are issued by the Bureau of the Fiscal Service to federal agencies. They are not traded on any securities exchange but mirror the prices of similar Treasury securities trading in the government securities market.

At September 30, 2017, investments consisted of the following:

(DOLLARS IN THOUSANDS)	Cost	Amortization Method	Amortized (Premium) Discount	Interest Receivable	Investment, Net	Market Value Disclosure
Non-Marketable Market-Based Securities						
Investor Protection Fund – Entity	$ 294,098	S/L	$ (3,680)	$ 1,865	$ 292,283	$ 290,274

At September 30, 2016, investments consisted of the following:

(DOLLARS IN THOUSANDS)	Cost	Amortization Method	Amortized (Premium) Discount	Interest Receivable	Investment, Net	Market Value Disclosure
Non-Marketable Market-Based Securities						
Investor Protection Fund – Entity	$ 353,742	S/L	$ (6,277)	$ 2,806	$ 350,271	$ 347,759

Intragovernmental Investments in Treasury Securities

Market-based Treasury securities are debt securities that the U.S. Treasury issues to federal entities without statutorily determined interest rates. Although the securities are not marketable, the terms (prices and interest rates) mirror the terms of marketable Treasury securities.

The federal government does not set aside assets to pay future benefits or other expenditures associated with the investment by federal agencies in non-marketable federal securities. The balances underlying these investments are deposited in the U.S. Treasury, which uses the cash for general government purposes. Treasury securities are issued to the SEC as evidence of these balances. Treasury securities are an asset of the SEC and a liability of the U.S. Treasury. Because the SEC and the U.S. Treasury are both components of the government, these assets and liabilities offset each other from the standpoint of the government as a whole. For this reason, the investments presented by the SEC do not represent an asset or a liability in the U.S. government-wide financial statements.

Treasury securities provide the SEC with authority to draw upon the U.S. Treasury to make future payments from these accounts. When the SEC requires redemption of these securities to make expenditures, the government finances those expenditures out of accumulated cash balances, by raising taxes or other receipts, by borrowing from the public or repaying less debt, or by curtailing other expenditures. This is the same manner in which the government finances all expenditures.

NOTE 4. LIABILITIES COVERED AND NOT COVERED BY BUDGETARY RESOURCES

The SEC recognizes liabilities that are covered by budgetary resources and liabilities that are not covered by budgetary resources. Budgetary and financial statement reporting requirements sometimes differ on the timing for the required recognition of an expense.

At September 30, 2017, liabilities consisted of the following:

(DOLLARS IN THOUSANDS)	Liabilities Covered by Budgetary Resources	Liabilities Not Covered by Budgetary Resources	Total
Accounts Payable	$ 20,838	$ —	$ 20,838
Contingent Liabilities	—	221,044	221,044
Total Liabilities	$ 20,838	$ 221,044	$ 241,882

At September 30, 2016, liabilities consisted of the following:

(DOLLARS IN THOUSANDS)	Liabilities Covered by Budgetary Resources	Liabilities Not Covered by Budgetary Resources	Total
Accounts Payable	$ 22,958	$ —	$ 22,958
Contingent Liabilities	—	10,800	10,800
Total Liabilities	$ 22,958	$ 10,800	$ 33,758

NOTE 5. COMMITMENTS AND CONTINGENCIES

Commitments: Dodd-Frank Whistleblower Program

As discussed in *Note 1.I, Liabilities*, the Investor Protection Fund is used to pay awards to whistleblowers if they voluntarily provide original information to the SEC and meet other conditions. Approved awards are between 10 and 30 percent of the monetary sanctions collected in the covered action or in a related action, with the actual percentage being determined at the discretion of the SEC using criteria provided in the legislation and the related rules to implement the legislation adopted by the SEC.

A Preliminary Determination is an assessment, made by the Claims Review Staff appointed by the Director of the Division of Enforcement, as to whether the claim should be allowed or denied, and if allowed, what the proposed award percentage amount should be. A contingent liability is recognized when (a) a positive Preliminary Determination has been made by the Claims Review Staff, (b) collection has been made, and (c) the percentage to be paid can be reasonably estimated. A potential liability is disclosed but not recognized when a positive Preliminary Determination is expected and a collection has been received. A liability is recognized when a Final Determination has been approved by the Commission and collection has been received. In all cases, the whistleblower award is not paid until amounts have been collected, a final order is issued by the Commission and the appeal rights of all claimants on the matter have been exhausted.

The SEC recognized a contingent liability for potential whistleblower awards of $221.0 million for the period ended September 30, 2017. The SEC recognized a contingent liability for potential whistleblower awards for the period ended September 30, 2016 of $10.8 million.

As of September 30, 2017, potential whistleblower payments for cases where positive Preliminary Determinations have not been made, but are reasonably possible, are estimated to range from $7.5 million to $22.6 million given the amount of current collections on those cases. Such claims do not meet the criteria for recognition as contingent liabilities in FY 2017. In the event that whistleblower award payments reduce the Investor Protection Fund total asset balance below $300 million, the Investor Protection Fund will be replenished as described in the "Disgorgement and Penalty Transfers" section of *Note 1.K, Non-Exchange Revenue*.

As of September 30, 2016, potential whistleblower payments that were reasonably possible, but did not meet the criteria for recognition as contingent liabilities, were estimated to range from $303.9 million to $911.7 million.

NOTE 6. INTRAGOVERNMENTAL COSTS

The Statement of Net Cost presents the Investor Protection Fund's results of operations for its two activities: the Employee Suggestion Program and awards to whistleblowers under the Dodd-Frank Whistleblower Program. Intragovernmental costs arise from purchases of goods and services from other components of the federal government (including other SEC funds). In contrast, public costs are those that arise from the purchase of goods and services from non-federal entities. Awards to whistleblowers are categorized as "costs with the public."

In FY 2017, the Employee Suggestion Program incurred $129 thousand of intragovernmental costs. The Dodd-Frank Whistleblower Program incurred $257.1 million of costs with the public (awards or potential awards to whistleblowers) in FY 2017.

In FY 2016, the Employee Suggestion Program incurred $44 thousand of intragovernmental costs. The Dodd-Frank Whistleblower Program incurred $55.1 million of costs with the public (awards or potential awards to whistleblowers) in FY 2016.

NOTE 7. STATUS OF BUDGETARY RESOURCES

A. Explanation of Differences between the Statement of Budgetary Resources and the Budget of the U.S. Government

A comparison between the FY 2017 Statement of Budgetary Resources and the actual FY 2017 data in the President's budget cannot be presented, as the FY 2019 President's budget which will contain FY 2017 actual data is not yet available; the comparison will be presented in next year's financial statements. There are no differences between the FY 2016 Statement of Budgetary Resources and the FY 2016 data in the President's budget.

B. Other Budgetary Disclosures

There were no budgetary resources obligated for undelivered orders as of September 30, 2017 and 2016.

There are no legal arrangements affecting the use of unobligated balances of budget authority, such as time limits, purpose, and obligation limitations.

NOTE 8. RECONCILIATION OF NET COST OF OPERATIONS TO BUDGET

For the years ended September 30, 2017 and 2016:

(DOLLARS IN THOUSANDS)	2017	2016
RESOURCES USED TO FINANCE ACTIVITIES:		
Budgetary Resources Obligated:		
New Obligations and Upward Adjustments (Total)	$ 47,050	$ 57,931
Total Resources Used to Finance the Net Cost of Operations	47,050	57,931
COMPONENTS OF NET COST OF OPERATIONS THAT WILL NOT REQUIRE OR GENERATE RESOURCES IN CURRENT PERIOD:		
Components Requiring or Generating Resources in Future Periods:		
Change in Unfunded Liability	210,244	(2,765)
Total Components of Net Cost of Operations that will not Require or Generate Resources in the Current Period	210,244	(2,765)
Net (Income) Cost from Operations	$ 257,294	$ 55,166

Components of net cost of operations that will not require or generate budgetary resources represent required timing differences in the Statement of Net Cost and the Statement of Budgetary Resources. For the year ended September 30, 2017, the SEC awarded $47 million in new whistleblower awards, of which $20.8 million was payable at September 30, 2017. The SEC also recognized $221 million in contingent liabilities for potential future whistleblower awards. Refer to *Note 4, Liabilities Covered and Not Covered by Budgetary Resources*, and *Note 5, Commitments and Contingencies*, for more information about contingent liabilities.

For the year ended September 30, 2016, the SEC awarded $57.9 million in new whistleblower awards, of which $22.9 million was payable at September 30, 2016. The SEC also recognized $10.8 million in contingent liabilities for potential future whistleblower awards.

OTHER INFORMATION

This section provides additional information related to the SEC's financial and performance management.

Inspector General's Statement on Management and Performance Challenges

Summarizes the most significant management and performance challenges facing the SEC, as identified by management and the Office of Inspector General in accordance with the Reports Consolidation Act of 2000. Also included is a response from the SEC Chairman outlining the agency's progress toward addressing these challenges.

Summary of Financial Statement Audit and Management Assurances

Reveals each material weakness and non-conformance found and/or resolved during the U.S. Government Accountability Office's audit, as well as those found by management during the evaluation of internal control and financial systems, as required by the Federal Managers' Financial Integrity Act.

Improper Payments Elimination and Recovery Act Reporting Details

Provides information about the SEC's commitment to, and progress with, reducing improper payments, and outlines the efforts taken to recapture improperly-made payments.

Civil Monetary Penalty Adjustment for Inflation

Provides inflationary adjustments to civil monetary penalties, as required by the Federal Civil Penalties Inflation Adjustment Act of 1990, as amended.

INSPECTOR GENERAL'S STATEMENT ON MANAGEMENT AND PERFORMANCE CHALLENGES

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

OFFICE OF
INSPECTOR GENERAL

MEMORANDUM

October 5, 2017

TO: Jay Clayton, Chairman

FROM: Carl W. Hoecker, Inspector General

SUBJECT: *The Inspector General's Statement on the SEC's Management and Performance Challenges, October 2017*

The Reports Consolidation Act of 2000 requires the U.S. Securities and Exchange Commission's (SEC or agency) Office of Inspector General to identify and report annually on the most serious management challenges that the SEC faces. In deciding whether to identify an issue as a challenge, we consider its significance in relation to the SEC's mission; its susceptibility to fraud, waste, and abuse; and the SEC's progress in addressing the challenge. We compiled this statement on the basis of our past and ongoing audit, evaluation, investigation, and review work; our knowledge of the SEC's programs and operations; and information from SEC management and staff, and the U.S. Government Accountability Office. We previously provided a draft of this statement to SEC officials and considered all comments received when finalizing the statement. As we begin fiscal year 2018, we have again identified the following as areas where the SEC faces management and performance challenges to varying degrees:

- Meeting Regulatory Oversight Responsibilities
- Ensuring an Effective Information Security Program
- Improving Contract Management
- Ensuring Effective Human Capital Management

The challenges and corresponding audit, evaluation, investigation, or review work are discussed in the attachment. If you have any questions, please contact Rebecca L. Sharek, Deputy Inspector General for Audits, Evaluations, and Special Projects.

Attachment

cc: Lucas Moskowitz, Chief of Staff, Office of Chairman Clayton
Sean Memon, Deputy Chief of Staff, Office of Chairman Clayton
Peter Uhlmann, Managing Executive, Office of Chairman Clayton
Michael S. Piwowar, Commissioner
Richard Grant, Counsel, Office of Commissioner Piwowar

Kara M. Stein, Commissioner
Robert Peak, Advisor to the Commissioner, Office of Commissioner Stein
Robert B. Stebbins, General Counsel
Rick A. Fleming, Investor Advocate
Bryan Wood, Director, Office of Legislative and Intergovernmental Affairs
John J. Nester, Director, Office of Public Affairs
Kenneth Johnson, Acting Chief Operating Officer
Vance Cathell, Director, Office of Acquisitions
Lacey Dingman, Chief Human Capital Officer, Office of Human Resources
Pamela C. Dyson, Director/Chief Information Officer, Office of Information Technology
Caryn Kauffman, Acting Chief Financial Officer, Office of Financial Management
Darlene L. Pryor, Management and Program Analyst, Office of the Chief Operating Officer

Attachment. THE INSPECTOR GENERAL'S STATEMENT ON THE SEC'S MANAGEMENT AND PERFORMANCE CHALLENGES, OCTOBER 2017

CHALLENGE: Meeting Regulatory Oversight Responsibilities

Overseeing Evolving Markets With Static Resources. Increases in the U.S. Securities and Exchange Commission's (SEC or agency) responsibilities in recent years continue to present challenges for the agency as it carries out its mission. For fiscal year (FY) 2018, the SEC requested about $1.6 billion, essentially the same as its FY 2017 appropriation. Despite difficult fiscal realities, as stated in the SEC's FY 2018 Congressional Budget Justification, the entities and organizations the agency is charged with overseeing continue to grow and advance:

> As markets have evolved—including as a result of innovation, technology, and globalization—the SEC's responsibilities have continued to grow and become more complex. . . . As the markets, products, and participants that the SEC oversees and regulates increase in size and complexity, the agency's mandate to protect investors, maintain fair, orderly, and efficient markets, and facilitate capital formation becomes more challenging. To maximize the use of the SEC's resources to fulfill this mission, the agency continually strives to allocate its time and funds toward the highest and best uses.[1]

The SEC is charged with overseeing over 26,000 market participants, including about 12,000 investment advisers, about 10,000 mutual funds and exchange traded funds, over 4,000 broker-dealers, over 650 mutual advisors, and 400 transfer agents. The agency also oversees 21 national securities exchanges, 10 credit rating agencies, and 7 active registered clearing agencies, as well as the Public Company Accounting Oversight Board, Financial Industry Regulatory Authority, Municipal Securities Rulemaking Board, the Securities Investor Protection Corporation, and the Financial Accounting Standards Board. In addition, the SEC is responsible for selectively reviewing the disclosures and financial statements of more than 8,800 reporting companies. As the SEC Chairman testified to in June 2017, registered investment advisers now manage "more than $70 trillion in assets, which is more than three times 2001 levels."[2]

Since 2014, we have reported that the SEC has identified as a challenge the immediate and pressing need for ensuring sufficient examination coverage of registered investment advisers. According to the SEC's 2016 Agency Financial Report,[3] the SEC's Office of Compliance Inspections and Examinations (OCIE) enhanced its National Exam Program risk assessment efforts to focus limited time and resources on those firms presenting the highest risk. OCIE has also hired staff and transitioned resources from other areas to its program for investment advisers and investment companies. In his June 2017 congressional testimony, the SEC

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[1] U.S. Securities and Exchange Commission, *Fiscal Year 2018 Congressional Budget Justification, Annual Performance Plan, and Fiscal Year 2016 Annual Performance Report*.

[2] SEC Chairman Jay Clayton, *Testimony on the Fiscal Year 2018 Budget Request of the U.S. Securities and Exchange Commission*, before the Subcommittee on Financial Services and General Government, Committee on Appropriations, United States Senate; June 27, 2017.

[3] U.S. Securities and Exchange Commission, *Agency Financial Report, Fiscal Year 2016*.

Chairman stated that, as a result of this shift and the introduction of efficiencies, the SEC was on track to deliver a 20 percent increase in the number of investment adviser examinations in FY 2017. Furthermore, the Chairman stated that, for FY 2018, OCIE anticipates being able to deliver an additional 5 percent increase in the number of investment adviser exams. The Chairman expected that, for at least the next several years, the SEC will need to do more each year to increase its examination coverage of investment advisers in light of continuing changes in the markets.

To assess the agency's progress in this area, in FY 2016, we initiated an audit to determine whether OCIE established effective controls over its investment adviser examination completion process to improve compliance with Federal securities laws, prevent fraud, inform policy, and monitor risk. We also sought to determine whether OCIE effectively used findings from examinations and Corrective Action Reviews as part of its risk-based, data-driven examination selection process. In our report titled *Audit of the Office of Compliance Inspections and Examinations' Investment Adviser Examination Completion Process* (Report No. 541, issued July 21, 2017), we reported that controls over OCIE's investment adviser examination completion process were generally effective but improvements were needed to ensure OCIE staff appropriately review and consistently document investment adviser examination results and risk assessments. Doing so could help ensure staff can effectively consider the results of examinations during evaluations of risk for future examinations. Moreover, we found that OCIE can improve its investment adviser examination completion process and internal controls by updating or documenting policies and procedures consistent with the *Standards for Internal Control in the Federal Government*.[4]

We recommended that OCIE (1) design control activities related to the review and approval of examination work products to require adequate segregation of duties, (2) update National Exam Program policies and procedures to more clearly define the requirements for documenting examination meetings and interviews, and (3) develop and disseminate to OCIE staff guidance for assigning final examination risk ratings before closing examinations. Management concurred with the recommendations, which will be closed upon completion and verification of corrective action.

In addition, the SEC depends on the provision of accurate, truthful information from the people and entities it regulates. To this end, the Office of Inspector General (OIG) conducts investigations of individuals who provide false or misleading information to the SEC during its examinations and enforcement actions. In one such case, the former president of a financial services company entered a guilty plea and was sentenced in Federal court to 1 year of probation, with 4 months to be served in home detention, and a fine of $4,000. The sentencing followed an OIG investigation that determined the official obstructed an SEC investigation into allegations that he concealed secret and improper referral payments he made to a lawyer in order to secure the business of a wealthy client.

Leveraging Technology To Keep Pace With Advances in Regulatory Areas. The SEC continues to modernize its information technology (IT) systems and seek ways to leverage technology to keep pace with the increasing size and complexity of capital markets that are often driven by advances in technology. The agency's FY 2018 budget request relied on

[4] U.S. Government Accountability Office, *Standards for Internal Control in the Federal Government* (GAO-14-704G, September 2014).

continued access to the Reserve Fund, created by the Dodd-Frank Wall Street Reform and Consumer Protection Act, to further the agency's goals in this area. As stated in the SEC Chairman's June 2017 congressional testimony:

> These funds, which have been dedicated to technology, have been important in our efforts to keep pace with the rapid technology advancements occurring in areas regulated by the SEC, as well as meeting emerging cybersecurity challenges. The continued availability of the Reserve Fund historically has allowed us to commit to critical, long-term technology initiatives that otherwise may have been more difficult for us to execute.

We note that the President's Budget for FY 2018 proposes to eliminate the Reserve Fund beginning in 2019.[5] As we have previously reported, the SEC's continuing key technology initiatives, funded by the Reserve Fund, include:

- expanding data analytics tools;
- improving the examination program through risk assessment and surveillance tools;
- enhancing systems that support the enforcement program;
- improving access and usefulness of information available to the public through the Electronic Data Gathering, Analysis, and Retrieval (EDGAR) system; and
- investing in further business process automation and enhancements.

The SEC is also increasing investments in cybersecurity, as discussed further on page 5 of this memorandum.

Recognizing the importance of technology in achieving the SEC's regulatory oversight responsibilities, we have continued assessing the SEC's progress in enhancing its technology. For example, in 2015, we issued a management letter that addressed the SEC's project to redesign the Tips, Complaints, and Referrals (TCR) system. The management letter (*Final Management Letter: Observations Noted During TCR System Audit Support Engagement*, issued May 20, 2015) identified various factors that led to schedule delays and cost increases in the SEC's TCR system redesign project and noted that, at the time, the SEC had not accepted the redesigned TCR system and a final user acceptance date had not been established. To follow-up on this important project, we conducted additional work and issued a second management letter in May 2017. Our May 2017 management letter on this subject (*Final Management Letter: Progress on the SEC's Tips, Complaints, and Referrals Intake and Resolution System Redesign and Vulnerability Remediation Efforts*, issued May 31, 2017) reported that the SEC had successfully tested and conditionally accepted the redesigned TCR system. However, the agency had not implemented the system, in part, because the system's multiple users considered new requirements and enhancements not previously required in the development effort. As of the date of our May 2017 management letter, the overall value of the SEC's contract to implement the system had increased by about $12.2 million (or

[5] Office of Management and Budget, *Budget of the U.S. Government, A New Foundation for American Greatness, Fiscal Year 2018*.

170 percent), and the SEC had obligated about $16.6 million and expended about $14.4 million of the total contract value (or twice the amount initially planned). Moreover, the SEC does not expect the redesigned TCR system to go-live until later this month (more than 3 years behind schedule).

Additionally, we reported that the most recent delays in accepting and implementing the redesigned TCR system were due, in part, to instability in the SEC's Oracle platform, which may have also impacted the agency's ability to test and deploy at least two other systems. At the same time, the SEC continued to operate the current TCR system but had not timely remediated some of the system's security vulnerabilities. In June 2017, SEC management provided a description of the actions the agency has taken or planned to take to address our concerns.

During FY 2017, we also assessed the SEC's progress in enhancing and redesigning the EDGAR system. In our report titled A*udit of the SEC's Progress in Enhancing and Redesigning the Electronic Data Gathering, Analysis, and Retrieval System* (Report No. 544, issued September 28, 2017), we reported that, since 2014, the SEC has made several improvements in its planning and governance of the program to redesign the EDGAR system while continuously enhancing the system in operation. Nonetheless, we identified opportunities for further improvement. Specifically, we determined that:

- the SEC's governance of EDGAR system enhancements, including the governance and operation of the EDGAR Requirements Subcommittee and the EDGAR system enhancement lessons learned process, needed improvement;
- the Office of Information Technology (OIT) did not consistently manage the scope of EDGAR system releases to ensure SEC needs were achieved;
- the SEC should improve its management of the EDGAR system engineering contract (discussed further on page 9 of this memorandum);
- OIT did not fully and consistently implement EDGAR system enhancements in compliance with Federal and SEC change management controls; and,
- although the SEC has taken steps to improve its ability to develop and implement a new electronic disclosure system that meets agency needs, further improvements can strengthen the agency's EDGAR redesign program governance and planning.

We made nine recommendations for corrective action. Management concurred with the recommendations, which will be closed upon completion and verification of corrective action.

For FY 2018, we are planning additional work to assess how well the SEC leverages technology and achieves its regulatory oversight responsibilities. Specifically, we plan to review the agency's management of (1) examinations intended to strengthen the technology infrastructure of the U.S. securities markets, (2) investments in infrastructure support services, and (3) data accessed from the database known as the consolidated audit trail. In addition, we plan to evaluate the Division of Economic and Risk Analysis' use of analytics and data in support of risk assessment and enforcement activities.

CHALLENGE: Ensuring an Effective Information Security Program

The SEC generates and collects commercially valuable, market sensitive, proprietary, and other non-public information. According to the agency's FY 2018 Congressional Budget Justification, the SEC is increasing investments in information security (including cybersecurity) to address, as a top priority, the ability to monitor and avoid advanced persistent threats, and to improve risk management and monitoring. In May 2017, the SEC Chairman initiated an assessment of the agency's cybersecurity risk profile and approach to cybersecurity from a regulatory and oversight perspective. As noted in the Chairman's September 20, 2017, statement on cybersecurity, components of the agency's cybersecurity initiative build on prior agency efforts and include establishing a senior-level cybersecurity working group to coordinate information sharing, risk monitoring, and incident response efforts throughout the agency.[6]

We closed the remaining two recommendations from our FY 2014 Federal Information Security Management Act evaluation report and the remaining four recommendations from our FY 2015 Federal Information Security Modernization Act (FISMA) audit because OIT took steps to improve key information security program areas. These steps included: (1) defining and documenting access methods for externally-hosted systems, (2) re-authorizing systems with expired authorizations to operate, (3) updating the OIT Risk Committee charter to address vacancies, (4) conducting OIT Risk Committee meetings in accordance with the updated charter, (5) implementing capabilities to more efficiently address plans of action and milestones, and (6) updating configuration management policies and procedures in support of rollback to previous versions of baseline configurations. Furthermore, OIT continues to enhance capabilities and develop tools in areas such as risk analytics and vulnerability management. However, we continue to identify and assess opportunities for improvement in the agency's information security controls.

Specifically, we completed our FY 2016 FISMA audit and reported opportunities for improvement in each of the eight assessment domains identified by the Department of Homeland Security (DHS). As stated in our report titled *Audit of the SEC's Compliance with the Federal Information Security Modernization Act for Fiscal Year 2016* (Report. No. 539, issued March 7, 2017), the SEC's information security program did not meet DHS' definition of "effective" as defined in the FY 2016 Inspector General FISMA Reporting Metrics. A summary of our observations for each of the eight assessment domains follows:

1. *Risk Management.* The SEC is taking steps to improve its risk management program, including updating Interconnection Security Agreement memorandums. However, these activities were not fully implemented in FY 2016, limiting the SEC's ability to effectively manage information security risk to organizational operations, organizational assets, individuals, and other organizations.

2. *Contractor Systems.* An ongoing agency project seeks to develop suggested security contract clauses for different types of contracts. However, we identified concerns in the Contractor Systems domain that could expose systems to unmitigated vulnerabilities.

[6] SEC Chairman Jay Clayton, *Statement on Cybersecurity*; September 20, 2017.

3. *Configuration Management.* The SEC is taking steps to strengthen its configuration management program, including leveraging the results of its participation in DHS's Cyber Hygiene Initiative, which aims to assist agencies in identifying critical vulnerabilities associated with public-facing assets. However, the SEC's configuration management program was not fully effective, which could expose SEC systems to configuration management vulnerabilities and exploitation.

4. *Identity and Access Management.* Although the SEC has established an identity and access management program, including policies and procedures, we identified areas for improvement. For example, access management processes did not ensure that 28 of 200 judgmentally sampled users requiring access to SEC information and information systems signed appropriate access agreements and participated in required training before gaining access.

5. *Security and Privacy Training.* The SEC has developed a security and privacy awareness and training program that includes comprehensive agency policies and procedures. However, we determined that OIT's practices did not ensure that SEC employees received privacy and information security awareness training annually as required by the Code of Federal Regulations. In addition, the SEC had not fully implemented a process to evaluate the skills of users with significant security and privacy responsibilities, and then provide those users with additional security and privacy training content or implement strategies to close any identified skills gaps as recommended by the National Institute of Standards and Technology.

6. *Information Security Continuous Monitoring.* The SEC is obtaining additional continuous monitoring tools and assistance as part of a DHS Continuous Diagnostics and Mitigation contract. However, the SEC did not have a mature and consistently implemented information security continuous monitoring program.

7. *Incident Response.* The SEC's incident response program is consistently implemented. To further mature the agency's incident response program, the SEC must ensure incident response activities are repeatable and metrics are used to measure and manage the implementation of the program, achieve situational awareness, and control ongoing risk.

8. *Contingency Planning.* The SEC has established a business continuity and disaster recovery policy to reduce the impact of a disruptive event or disaster. However, the SEC did not annually test its system-specific contingency plans and disaster recovery plan, in accordance with agency policy.

To improve the SEC's information security program, we made 21 recommendations. Management concurred with all 21 recommendations and provided evidence of corrective action taken for each one. We have closed 3 of the recommendations and are reviewing evidence of corrective action taken for the remaining 18 recommendations. In addition, our FY 2017 audit of the SEC's compliance with FISMA is ongoing.

In FY 2017, we also completed several investigations with information security implications. In one matter, we determined that an employee of one of the SEC's two data center facility service providers failed to follow the company's established access control procedures,

resulting in unauthorized access to the SEC's computer server space by an individual unaffiliated with the SEC. There was no evidence that the SEC's data center space was breached intentionally or that SEC servers were accessed. We issued a Management Implication Report to agency management recommending corrective action.

In two other investigations, we determined that SEC employees sent personally identifiable information or other non-public information to personal e-mail accounts. We reported the results of these investigations to SEC management to determine whether corrective administrative actions may be warranted.

As part of its audit of the SEC's FYs 2015 and 2016 financial statements, the U.S. Government Accountability Office (GAO) reported in July 2017 that the SEC improved the security controls over its key financial systems.[7] According to GAO, as of September 2016, the agency had resolved 47 of the 58 recommendations GAO had previously made that had not been implemented by the conclusion of GAO's FY 2015 audit. However, the SEC had not fully implemented the remaining 11 recommendations that included the following:

- consistently protecting its network boundaries from possible intrusions,
- identifying and authenticating users,
- authorizing access to resources,
- auditing and monitoring actions taken on its systems and network, and
- encrypting sensitive information while in transmission.

In addition, GAO reported that 15 newly identified control deficiencies limited the effectiveness of the SEC's controls for protecting the confidentiality, integrity, and availability of its information systems. For example, GAO found that the agency did not consistently control logical access to its financial and general support systems. In addition, although the agency enhanced its configuration management controls, it used unsupported software to process financial data. Furthermore, the SEC did not adequately segregate incompatible duties for one employee.

GAO found that these weaknesses existed, in part, because the SEC did not fully implement key elements of its information security program. For example, the SEC did not maintain up-to-date network diagrams and asset inventories in its system security plans for its general support system and its key financial system application to accurately and completely reflect the current operating environment. The agency also did not fully implement and continuously monitor those systems' security configurations.

GAO recommended that, in addition to the 11 prior recommendations that had not been fully implemented, the SEC should take 13 actions to address newly identified control deficiencies

[7] U.S. Government Accountability Office, *INFORMATION SECURITY SEC Improved Control of Financial Systems but Needs to Take Additional Actions* (GAO-17-469, July 27, 2017).

and 2 actions to more fully implement its information security program. Management concurred with GAO's recommendations and reported to us that the SEC has submitted to GAO evidence of corrective action taken for all prior year and newly identified recommendations.

In FY 2018, we will continue to leverage the expertise of OIG auditors, special agents, and IT specialists to assess the SEC's information security program. In particular, we will expand our digital extraction, forensic, and investigation capabilities in order to pursue complex IT crimes committed against the SEC and to provide digital forensics support during investigations and audits as needed.

CHALLENGE: Improving Contract Management

According to the SEC's 2016 Agency Financial Report, the Office of Acquisitions (OA) returned more than $40 million to the SEC by de-obligating funds from existing and expired contracts and agreements. OA also awarded enterprise agreements, reported one of the highest small-business participation levels across the Federal government, and began implementing an electronic filing system for contract and Contracting Officer's Representative (COR) files. In addition, OA reported that, in FY 2017, it would provide customized training to SEC CORs and continue to increase the number of certified program and project managers to improve contract management. However, as discussed below, we completed two audits in FY 2017 that assessed elements of the SEC's contract management and, during both audits, we identified areas of needed improvements, particularly regarding the performance and oversight of SEC CORs.

In 2016, we reported that OA improved the SEC's COR Program by sufficiently addressing all six recommendations from an OIG audit of the Program completed in 2015.[8] Nonetheless, in 2017, we completed our *Audit of the SEC's Management of Its Data Centers* (Report No. 543, issued September 29, 2017), and found that the SEC did not adequately manage or monitor its two data center contracts. Specifically, we found that CORs responsible for overseeing contractors who provide critical data center services[9] did not always validate contractor invoices. Moreover, the agency's data center contract files were incomplete and did not contain adequate support for key decisions, including cost increases and changes to data center infrastructure. Also, the SEC's data center contractors did not provide (and the SEC did not request) all required contract deliverables, such as annual security assessments and monthly reports, and the power consumption reports provided by one data center contractor were unusable.

We determined that the inadequate management and monitoring of the SEC's data center contracts was caused by (1) a lack of understanding and communication among key stakeholders in OA and OIT, including the Contracting Officer (CO) and CORs, and (2) insufficient oversight. Generally, the CORs did not fully understand their duties and responsibilities or the limits of their authority, and did not perform certain duties as required.

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[8] U.S. Securities and Exchange Commission, Office of Inspector General, *Audit of the SEC's Contracting Officer's Representative Program* (Report No. 530; September 18, 2015).

[9] The SEC's data centers house critical telecommunications, data, and computing resources, including EDGAR, which supports the financial reporting of public companies in the United States.

For example, a COR mistakenly thought he had the authority to waive deliverables required by the contracts. Furthermore, the CO did not provide effective oversight of the CORs' invoice validation process and never reviewed the COR contract files. The CO also did not ensure that the CORs monitored the contractors' compliance with the terms and conditions of the contracts. We observed similar deficiencies during our 2015 COR Program audit and our 2016 audit of the SEC's management of its protective security force contract.[10]

As a result of inadequate management and monitoring of the SEC's data center contracts, the SEC paid contractor invoices containing formula errors resulting in $217,159 in overpayments (which has since been refunded). We also determined that the agency paid about $2.8 million in unsupported costs.[11] If the SEC does not take the recommended corrective action to validate certain costs and if all contract options are exercised, the agency may incur additional costs of about $2.7 million in funds that could be put to better use over the remaining life of one of its data center contracts.[12] Moreover, the SEC paid for reports that the contractors did not provide or provided in unusable formats. Without these deliverables, we question how agency personnel could adequately monitor the contractors' performance to ensure SEC equipment and data was not vulnerable to damage, loss, or system disruptions, or maintain an up-to-date understanding of the security state and risk posture of information systems and data stored and processed at the agency's data centers.

We made 10 recommendations for corrective action, including that the SEC conduct comprehensive reviews of actions taken in 2012 and 2013 to relocate the agency's data centers and improve data center-related contract management. We also strongly encouraged the Director of OA to conduct a comprehensive review of the SEC's COR Program and ensure controls are developed or strengthened to improve the agency's contract management specific to activities performed by CORs and COs. Management concurred with the recommendations, which will be closed upon completion and verification of corrective action.

As stated on page 4 of this memorandum, we also reported in FY 2017 that the SEC should improve its management of the EDGAR system engineering contract. Specifically, in our report titled *Audit of the SEC's Progress in Enhancing and Redesigning the Electronic Data Gathering, Analysis, and Retrieval System* (Report No. 544, issued September 28, 2017), we reported that the SEC did not complete four of five required steps to ensure that the agency's contractor responsible for the EDGAR system engineering contract properly used earned value management to monitor the SEC's investments in EDGAR system enhancements, as required by the Office of Management and Budget (OMB).[13] In addition, OIT did not effectively use established contract performance metrics to manage the contractor's performance because

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[10] U.S. Securities and Exchange Commission, Office of Inspector General, *Management of the SEC's Protective Security Force Contract Needs Improvement* (Report No. 536; June 22, 2016).

[11] These costs resulted from a contract task order and a significant contract modification that, at the time of our audit, were not supported by adequate documentation. The term "unsupported cost" is defined in the Inspector General Act, as amended (Public Law 95–452; 5 U.S.C. App.).

[12] These costs are associated with a significant contract modification that we found, at the time of our audit, was not supported by adequate documentation. We recommended that the CO and COR validate the costs (See Recommendation 6 in OIG Report No. 543.). The term "recommendation that funds be put to better use" is defined in the Inspector General Act, as amended (Public Law 95–452; 5 U.S.C. App.).

[13] Office of Management and Budget, Memorandum M-05-23, *Improving Information Technology (IT) Project Planning and Execution* (August 2005).

OIT had not established processes or controls for each metric. Furthermore, the EDGAR system performance requirements specified in the contract were not consistent with requirements specified in another SEC contract. As a result, the SEC accepted unreliable earned value management data and did not monitor its investments in EDGAR system enhancements or the EDGAR system engineering contractor's performance as effectively as planned.

To improve the SEC's management of the EDGAR system engineering contract and the SEC's efforts to monitor agency investments in EDGAR system enhancements, we made four recommendations for corrective action. Management concurred with the recommendations, which will be closed upon completion and verification of corrective action.

We plan to perform work in FY 2018 to further assess the SEC's contract management. To better determine the nature and extent of progress and/or deficiencies in this area, we established standardized steps that we will use to obtain an understanding of the agency's contract management when contracting is central to answering an audit's or evaluation's objectives.

CHALLENGE: Ensuring Effective Human Capital Management

The SEC seeks to hire and retain a skilled and diverse workforce and to ensure that all decisions affecting employees and applicants are fair and ethical. Attracting, engaging, and retaining a technically proficient and diverse workforce is one of the agency's stated strategic objectives.[14] To that end, on April 6, 2017, the SEC's Chief Human Capital Officer (CHCO) testified before the House Subcommittee on Government Operations that the Partnership for Public Service recognized the SEC as the "most improved" of any mid-size agency based on the agency's 2016 Federal Employee Viewpoint Survey results. According to the CHCO, "These positive results reflect the culmination of a persistent, multi-year effort by employees, the National Treasury Employees Union (NTEU), and the SEC's leadership team in working together to create an environment that engages employees and supports their commitment to excellence on behalf of America's investors and our markets."[15] We noted that the SEC's Federal Employee Viewpoint Survey results improved again in 2017.

In addition, according to the SEC's 2016 Agency Financial Report, the agency's Aspiring Leaders Program (intended to promote and build leadership competencies of senior employees) continued in its second successful year. Also during 2016, the SEC's Office of Human Resources (OHR) collaborated with the Office of Personnel Management and internal stakeholders to develop the agency's first Workforce Plan. As we reported in 2016, the Workforce Plan "provides an overview of the current workforce; identifies critical workforce competencies for SEC mission critical occupations; and identifies perceived workforce competency gaps from supervisors/managers." Based on the identified competency gaps, the Plan establishes goals to reduce gaps in core/professional and technical competencies across mission-critical occupations, and increase leadership-ready talent pools across all grade

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[14] U.S. Securities and Exchange Commission Strategic Plan, Fiscal Years 2014 – 2018.

[15] Lacey Dingman, Director, Office of Human Resources and Chief Human Capital Officer, *Statement on "Best Places to Work Rankings,"* April 6, 2017, before the United States House of Representatives Subcommittee on Government Operations, Committee on Oversight and Government Reform.

levels. The Plan also outlines strategies to begin addressing the competency gaps and includes tasks that should be initiated or completed in the next 2 years. However, as stated in previous years, human capital management remains a challenge.

In December 2016, GAO issued its second triennial report on the SEC's personnel management required under the Dodd-Frank Wall Street Reform and Consumer Protection Act.[16] GAO surveyed all SEC staff, evaluated SEC policies and procedures, and analyzed information on the SEC's practices, and concluded that actions are needed to address limited progress in resolving long-standing personnel management challenges. GAO reported that, although employee views on the SEC's organizational culture have generally improved since 2013, GAO's survey indicated that the SEC still operates in a compartmentalized way and that there is little communication and collaboration between divisions. Moreover, although the SEC has addressed two of seven recommendations from GAO's 2013 report, GAO reported that the agency faces added challenges in cross-divisional collaboration and hiring and promotion. Specifically, GAO found that the SEC:

- continues to lack assurance that all staff have the necessary skills,
- lacks assurance that the new performance management system will perform better than the previous one, and
- has made little progress to address GAO's two recommendations related to improving cross-divisional collaboration.[17]

In addition, GAO found that because the SEC has not identified skills gaps among its hiring specialists, its training of these staff is limited. As a result, GAO concluded that the SEC lacks assurance that its hiring specialists have the necessary skills to hire and promote the most qualified applicants, in accordance with key principles of an effective control system. We note that, in its February 2017 update to its High-Risk Series, GAO recognized Strategic Human Capital Management as a high-risk area that continues to need attention by Congress and the Executive Branch. Specifically, GAO's 2017 report states that:

> Mission-critical skills gaps within the federal workforce pose a high risk to the nation. Regardless of whether the shortfalls are in such government-wide occupations as cybersecurity and acquisitions, or in agency-specific occupations such as nurses at the Veterans Health Administration (VHA), skills gaps impede the federal government from cost-effectively serving the public and achieving results.[18]

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[16] U.S. Government Accountability Office, *Securities and Exchange Commission, Actions Needed to Address Limited Progress in Resolving Long-Standing Personnel Management Challenges* (GAO-17-65, December 29, 2016).

[17] In response to a draft of GAO's report, the SEC disagreed with GAO's characterization of the state of the SEC's intra-agency communication and collaboration. The SEC stated, among other things, that significantly more progress has been made to resolve recommendations from GAO's 2013 report (addressing interdivisional communication and collaboration) than GAO's 2016 report recognizes.

[18] U.S. Government Accountability Office, *HIGH-RISK SERIES Progress Made on Many High-Risk Areas, While Substantial Efforts Needed on Others* (GAO-17-317, February 15, 2017).

GAO recommended that the SEC should (1) provide authority to the Chief Operating Officer or other official to enhance cross-divisional collaboration, and (2) develop and implement training for hiring specialists that is informed by a skills gap analysis. GAO also reiterated the need to address the remaining five prior unaddressed recommendations on workforce planning, performance management, and intra-agency collaboration. The SEC disagreed that enhancing the role of the Chief Operating Officer would be the optimal means to achieve further enhancements, but agreed with GAO's second recommendation.

In 2016, we reported that OHR did not have an effective method for assessing the timeliness of the SEC's hiring process, including maintaining reliable hiring data and monitoring hiring actions according to established timelines. Furthermore, we reported that OHR did not analyze quality-of-new-hire survey results to improve the SEC's hiring process. We urged OHR to implement an effective system based on reliable data to conduct comprehensive assessments of the SEC's hiring process, further improve the agency's hiring process, and increase the likelihood that SEC divisions and offices timely hire highly qualified candidates to meet mission requirements (*Final Closeout Memorandum: Audit of the SEC's Hiring Practices*, issued August 19, 2016). In response, management noted steps it has taken to improve the SEC's hiring process.

OHR has reported enhancing and streamlining the hiring process by eliminating the practice of hiring to a deadline and allowing for more fluid and timely hiring throughout the year. However, at the beginning of 2017, several factors outside the SEC's control created additional challenges in this area. Specifically, on January 23, 2017, the President imposed a Federal hiring freeze to halt the growth of the Federal workforce. Then, on April 12, 2017, OMB issued Memorandum M-17-22 (OMB 17-22),[19] which provides agencies guidance on fulfilling the requirements of the hiring freeze and an Executive Order to reorganize Executive Branch departments and agencies. OMB 17-22 also requires all agencies to:

- begin taking immediate actions to achieve near-term workforce reductions and cost savings, including planning for funding levels in the President's FY 2018 Budget Blueprint;
- develop a plan to maximize employee performance by June 30, 2017; and,
- in September 2017, submit to OMB (as part of the agency's FY 2019 budget submission to OMB) an Agency Reform Plan that includes long-term workforce reductions.

As a result, in May 2017, OHR notified all SEC divisions and offices that the SEC was voluntarily continuing the external hiring freeze while the agency developed plans in response to OMB 17-22.

In FY 2018, we will continue to monitor the SEC's human capital management, including its progress toward (1) addressing competency gaps identified by supervisors and managers, (2) meeting goals established in agency human capital and workforce plans, (3) addressing GAO's recommendations, and (4) complying with OMB 17-22.

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[19] Office of Management and Budget, Memorandum 17-22, *Comprehensive Plan for Reforming the Federal Government and Reducing the Federal Civilian Workforce*; April 12, 2017.

MANAGEMENT'S RESPONSE TO INSPECTOR GENERAL'S STATEMENT

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

OFFICE OF
THE CHAIRMAN

November 2, 2017

Mr. Carl W. Hoecker
Inspector General
U.S. Securities and Exchange Commission
Washington, D.C. 20549

Dear Mr. Hoecker:

Thank you for your "Statement on the SEC's Management and Performance Challenges," issued on October 5, 2017. We remain committed to enhancing the programmatic and operational effectiveness of the SEC and appreciate the Office of Inspector General's important role in this effort. We appreciate your assessment of the agency's progress in addressing the challenges.

The "Looking Forward" section of our Annual Financial Report provides a general overview of actions that the SEC has taken or is taking to better prepare the agency to address key management and performance challenges. In addition, below are more detailed comments concerning the actions the agency has taken, is taking, or intends to take to address the specific challenges identified in your statement. Of particular note, I recently announced the SEC's plans to create a new Chief Risk Officer role to lead an expansion of the agency's internal enterprise risk capabilities across its divisions and offices. This position will be focused full-time on assessing, coordinating, and spearheading the agency's various risk management efforts. We anticipate that this new position will strengthen the agency's ability to meet a broad range of new and emerging challenges facing the agency, including those mentioned in your statement.

Overseeing Evolving Markets

Examinations Completion Process. Your statement references the report titled "Audit of the Office of Compliance Inspections and Examinations' Investment Adviser Examination Completion Process," which was issued on July 21, 2017. The report found that the Office of Compliance Inspections and Examinations (OCIE) has generally effective controls over its investment adviser examination completion process. As discussed in detail in OCIE's July 14, 2017, response to a draft of the report, OCIE management is taking action to address the three recommendations contained in the report by (1) documenting controls pertaining to segregation of duties at intermediate phases of the exam process; (2) more clearly defining requirements related to documentation of examination meetings and interviews, including preliminary exit interviews; and (3) completing OCIE's review of the exam program's assignment of final examination risk ratings, and at the conclusion of this review, issuing guidance to staff.

Leveraging Technology to Keep Pace with Advances in Regulatory Areas

Tips, Complaints and Referrals System. Your statement notes that the SEC expected the redesigned TCR system to go-live on October 2, 2017 after significant delay. The agency has now revised this planned go-live date to the end of January 2018, in order to allow more time for obtaining, applying and testing important security patches. The agency expects to obtain the Authorization to Operate (ATO) for TCR 3.0 by the end of December 2017, and then the agency plans to complete final go-live activities such as systematic wind-down of the current TCR system and targeted communications regarding the transition to TCR 3.0, and ensure staff are trained and supported by updated documentation, policies and procedures.

EDGAR Enhancements. Your statement references the report titled "Audit of the SEC's Progress in Enhancing and Redesigning the Electronic Data Gathering, Analysis, and Retrieval System," which was issued on September 28, 2017. The agency during the past year made several significant changes in the oversight and governance of EDGAR system enhancements, and has planned or is taking a number of additional actions in response to the OIG's report. For instance, the SEC took action in 2017 to create a new EDGAR Program Office whose duties include coordinating and rationalizing the agency's enhancements and investments related to EDGAR, including modifications to conform with changes to Commission rules. In addition, the SEC has instituted an operational review of, and as necessary or appropriate, uplift of the EDGAR system, with a focus on cybersecurity. This includes assessing the types of data we take in through the EDGAR system and whether EDGAR is the appropriate mechanism to obtain that data. As appropriate, we plan to take actions to reduce EDGAR's risk profile and strengthen its security. Finally, the SEC is also taking action to address each of the specific recommendations contained in the OIG's audit report.

Information Security Program

Information security is an area that is vitally important to the SEC and our markets. The prominence of this issue and the heightened focus the agency has on it is the result of various factors, including (1) the increased use of and dependence on data and electronic communications; (2) the greater complexity of technologies present in the financial marketplace; and (3) the continually evolving threats from a variety of sources.

On September 20, 2017, I issued a press release and statement that, among other items, (1) discussed the Commission's cybersecurity risk profile; (2) reviewed our approach to oversight and enforcement; and (3) disclosed a 2016 intrusion into the EDGAR system that may have led to illicit trading. The press release and statement are part of an ongoing assessment of the SEC's cybersecurity risk profile and preparedness that I initiated upon joining the Commission. The initiative has various components, including the formation of a senior-level cybersecurity working group to coordinate information sharing, risk and threat monitoring, incident response and other cross-divisional and interagency efforts and an assessment of reporting and escalation procedures.

In subsequent public statements, I described the agency's response to the EDGAR intrusion as being organized into five principal work streams:

1. The review of the 2016 EDGAR intrusion by your office;

2. The investigation by our Division of Enforcement into the potential illicit trading resulting from the 2016 EDGAR intrusion;

3. A focused, operational review of and, as necessary or appropriate, uplift of our EDGAR system;

4. The more general assessment and uplift of our cybersecurity risk profile and efforts that we initiated shortly after my arrival at the Commission this past May, including, without limitation, the identification and review of all systems, current and planned (*e.g.*, the Consolidated Audit Trail (CAT)), that hold market sensitive data or personally identifiable information; and

5. The agency's internal review of the 2016 EDGAR intrusion to determine, among other things, the procedures followed in response to the intrusion. This review is being overseen by the Office of the General Counsel and has an interdisciplinary investigative team that includes personnel from regional offices and will involve outside technology consultants.

Each of these efforts is moving forward and, as is the nature of matters of this type, will require substantial time and effort to complete.

In addition, I authorized the immediate hiring of additional staff and outside technology consultants to aid in our efforts to protect the security of the agency's network, systems and data. I also directed the staff to take a number of steps designed to strengthen our cybersecurity risk profile, with an initial focus on EDGAR. As discussed above, this effort includes assessing the types of data we take in through the EDGAR system, and whether EDGAR is the appropriate mechanism to obtain that data. Another part of this effort includes reviewing the security systems, processes and controls we have in place to protect data submitted through EDGAR.

The staff will also conduct similar reviews of other systems we use at the SEC, assessing the types of data we keep and the related security systems, processes and controls. We will also work to enhance our escalation protocols for cybersecurity incidents in order to enable greater agency-wide visibility and understanding of potential cyber vulnerabilities and attacks.

Overall, by promoting effective cybersecurity practices in connection with both the Commission's internal operations and its external regulatory oversight efforts, it is our objective to contribute substantively to a financial market system that recognizes and addresses cybersecurity risks and, in circumstances in which these risks materialize, exhibits strong mitigation and resiliency.

Contract Management

Your statement discusses two reports released in September 2017, "Audit of the SEC's Management of its Data Centers" and "Audit of SEC's Progress in Enhancing and Redesigning the Electronic Data Gathering, Analysis, and Retrieval System." I appreciate that your statement acknowledges the improvements the SEC has made in contract management, and we intend to build upon those efforts. Both reports identified a number of lessons learned and I have been informed that we are working diligently to address the deficiencies noted. More specifically, the Office of Acquisitions is working on a variety of fronts to further promote effective contract management, including to improve communications between Contracting Officers and Contracting Officer Representatives, conduct annual reviews of contract files to make sure they contain all the appropriate documentation, and improve reporting. In parallel, the Office is addressing each of the particular OIG recommendations related to the data center and EDGAR contracts identified in the two OIG reports.

Human Capital Management

Your statement notes audit reports over the past year that have called attention to the need for continuing focus on personnel management matters, including the GAO's December 29, 2016 report on personnel management (GAO-17-65) and OIG's August 2016 report, "Final Closeout Memorandum: Audit of the SEC's Hiring Practices." In addition, your statement also notes several factors outside the SEC's control – such as the January 2017 government-wide hiring freeze – that have created additional challenges in this area.

The SEC continues to bring a strong focus to ensuring we are effective in managing our personnel. One of the key themes from the GAO's report is the need for continuing focus on internal communication and collaboration. The SEC strives to promote effective communication and collaboration in critical cross-agency business processes, such as those relating to internal operations, rulemaking, and enforcement, including through numerous formal and informal mechanisms for coordination, such as intra-agency governance committees and working groups. While the SEC still has progress to make, the results of the Office of Personnel Management's 2017 Federal Employee Viewpoint Survey (FEVS) shows that we are headed in the right direction. In this most recent survey, employees reported satisfaction levels with internal communication and collaboration that are approximately 20 percentage points higher than just five years ago.

The SEC also took several actions during the year to strengthen workforce planning and performance management. The SEC in 2017 conducted a training needs assessment for staff within the Office of Human Resources, and plans to conduct a competency assessment in 2018 for other key occupations not previously assessed. In 2016, the SEC engaged OPM to assess the effectiveness of the SEC's pilot performance management program, and used OPM's feedback

in collaboration with our collective bargaining unit, the National Treasury Employees' Union, to initiate a second pilot in 2017.

* * * *

I hope that the actions outlined in this letter demonstrate our commitment to strengthening internal control and improving the agency's performance. We look forward to working with you to further address these challenges.

Sincerely,

Jay Clayton
Chairman

SUMMARY OF FINANCIAL STATEMENT AUDIT AND MANAGEMENT ASSURANCES

Table 1.12 | Summary of Financial Statement Audit

Audit Opinion: Unmodified

Restatement: No

Material Weaknesses	Beginning Balance	New	Resolved	Consolidated	Ending Balance
Internal Control over Financial Reporting	—	—	—	—	—
Total Material Weaknesses	—	—	—	—	—

Table 1.13 | Summary of Management Assurances

Effectiveness of Internal Control over Financial Reporting (FMFIA § 2)

Statement of Assurance: Unmodified

Material Weaknesses	Beginning Balance	New	Resolved	Consolidated	Reassessed	Ending Balance
Internal Control over Financial Reporting	—	—	—	—	—	—
Total Material Weaknesses	—	—	—	—	—	—

Effectiveness of Internal Control over Operations (FMFIA § 2)

Statement of Assurance: Unmodified

Material Weaknesses	Beginning Balance	New	Resolved	Consolidated	Reassessed	Ending Balance
Total Material Weaknesses	—	1	—	—	—	1

Conformance with Financial Management System Requirements (FMFIA § 4)

Statement of Assurance: Systems Conform

Non-Conformances	Beginning Balance	New	Resolved	Consolidated	Reassessed	Ending Balance
Federal Financial Management System Requirements	—	—	—	—	—	—
Total Non-Conformances	—	—	—	—	—	—

IMPROPER PAYMENTS ELIMINATION AND RECOVERY ACT REPORTING DETAILS

The Improper Payments Information Act of 2002 (IPIA), as amended by the Improper Payments Elimination and Recovery Act of 2010 (IPERA), the Improper Payments Elimination and Recovery Improvement Act of 2012 (IPERIA), and the Federal Improper Payments Coordination Act of 2015, requires agencies to review all programs and activities they administer to identify those that may be susceptible to significant erroneous payments. For all programs and activities in which the risk of erroneous payments is significant, agencies are to estimate the annual amount of erroneous payments made in those programs. Guidance provided by the Office of Management and Budget (OMB) in Circular A-136, *Financial Reporting Requirements*, and Appendix C of Circular A-123, *Requirements for Effective Estimation and Remediation of Improper Payments*, requires agencies to report specific details about the SEC's Improper Payments Elimination Program, which are below. Additionally, the following link further explains improper payments and the information reported in previous AFRs that is not included in the FY 2017 AFR: https://paymentaccuracy.gov/.

Risk Assessment

In FY 2017, the SEC did not conduct a new risk assessment. IPERIA guidelines state that if an agency deems a program to be low risk for improper payments, the agency will re-assess that program's risk at least every three years. An agency is only required to conduct a formal risk assessment earlier than three years if the program experiences a significant change in legislation and/or a significant increase in funding level. Based on this, the SEC did not perform a risk assessment for FY 2017 and will not perform another risk assessment until FY 2019.

The SEC made this determination on the basis that for the FYs 2016 and 2015 risk assessments, none of its programs and activities were susceptible to significant improper payments at or above the threshold levels set by OMB based on the historically low volume of improper payments and the low risk of improper payments given the controls and processes in place.

To perform its risk assessment, the SEC instituted a systematic method of reviewing each program and activity by considering risk factors likely to contribute to significant improper payments. The risk assessment encompassed a review of existing data that included the Government Accountability Office and the SEC Office of Inspector General audit reports, prior internal controls over financial reporting assessments, and the results of improper payments testing performed in prior years. These risk assessments were performed for the following programs:

- Vendor payments (includes travel and credit card payments);
- Disgorgement and penalty distributions (made by the SEC to fund and tax administrators and directly to harmed investors);
- Returned deposits of registration filing fees under Section 6b of the Securities Act of 1933 and Sections 13 and 14 of the Securities Exchange Act of 1934;
- Payroll and benefit payments (includes base pay, overtime pay, and agency contributions to retirement plans, health plans, thrift savings plans, and supplemental retirement); and
- Whistleblower payments.

In FYs 2007 and 2008, the SEC's testing of its largest programs resulted in improper payment percentages that were well below one-half percent and less than $30,000 for each program. In FYs 2009 through 2014, the SEC performed a risk assessment and transaction testing on a sample basis for all programs and determined that its programs are not susceptible to significant erroneous payments. The SEC will conduct a follow-on review in FY 2018 of its programs and activities to determine whether the programs have experienced any significant changes in legislation or funding levels; if needed, the SEC will re-assess the program's risk susceptibility and make a statistically valid estimate of erroneous payments for any programs determined to be susceptible to significant erroneous payments.

Recapture of Improper Payments

In FY 2017, implementation of recapture auditing—if determined to be cost-effective—would apply to vendor payments, disgorgement and penalty distributions, refunds of registration filing fee deposits, payroll, and whistleblower payments. Because the definition of payment in the IPERA legislation is any payment or transfer of federal funds to any non-federal person or entity, the SEC is not required to review—and has not reviewed—intragovernmental transactions.

The SEC determined that implementing a payment recapture audit program for vendor payments, disgorgement and penalty distributions, refunds of registration filing fee deposits, payroll, and whistleblower payments is not cost-effective and notified OMB in September 2015. The benefits or recaptured amounts associated with implementing and overseeing the program do not exceed the costs, including staff time and payments to contractors, of a payment recapture audit program. In making this determination, the SEC considered its low improper payment rate based on testing conducted over the past eight years. For example, the SEC identified only $449 of vendor overpayment in FY 2014 from statistical sample testing under the IPIA. The SEC also considered whether sophisticated software and other cost-efficient techniques could be used to identify significant overpayments at a low cost per overpayment, or if labor intensive manual reviews of paper documentation would be required. In addition, the SEC considered the availability of tools to efficiently perform the payment recapture audit and minimize payment recapture audit costs.

The SEC will continue to monitor its improper payments across all programs and activities it administers and assess whether implementing payment recapture audits for each program is cost-effective. If the SEC determines, through future risk assessments, that a program is susceptible to significant improper payments and implementing a payment recapture program may be cost-beneficial, the SEC will implement a pilot payment recapture audit to gauge whether such audits would be cost-effective on a larger scale.

CIVIL MONETARY PENALTIES INFLATION ADJUSTMENT

The Federal Civil Penalties Inflation Adjustment Act of 1990 (FCPIA), 28 U.S.C. 2461 note, as amended by the Debt Collection Improvement Act of 1996 and the Federal Civil Penalties Inflation Adjustment Act Improvements Act of 2015 (2015 Act), requires agencies to annually adjust for inflation any civil monetary penalties that are assessed or enforced by that agency. This adjustment must be performed for any penalty where either the amount of the penalty or the maximum penalty is set by law. The 2015 Act replaces the inflation adjustment mechanism previously contained in the FCPIA and all previous inflation adjustments made pursuant to the FCPIA with a new mechanism for calculating the inflation-adjusted amount of civil monetary penalties. The 2015 Act implemented this change by first requiring that each agency perform a "catch-up adjustment" to be published by July 1, 2016. Thereafter, agencies are to adjust their penalty amounts every January, starting in January 2017.

The FCPIA also directs the Commission to include in its Agency Financial Report information about the civil monetary penalties within the jurisdiction of the agency, including the adjustment of civil monetary penalties for inflation under the FCPIA. Further, the FCPIA directs the Comptroller General of the United States to annually submit to Congress a report assessing agencies' compliance with the inflation adjustments required by the FCPIA.

The SEC administers four statutes that provide for civil monetary penalties:

- The Securities Act of 1933;
- The Securities Exchange Act of 1934;
- The Investment Company Act of 1940; and
- The Investment Advisers Act of 1940.

In addition, the Sarbanes-Oxley Act of 2002 provides the Public Company Accounting Oversight Board (PCAOB) authority to levy civil monetary penalties in its disciplinary proceedings. These penalties are established by federal law and are enforced by the Commission for purposes of the FCPIA because the Commission may by order affirm, modify, remand, or set aside civil monetary penalties imposed by the PCAOB and may enforce the PCAOB's civil monetary penalty orders in federal district court.

The Commission will adjust for inflation the maximum penalty amounts provided in these statutes as required by the FCPIA and will publish these adjustments in the Federal Register. The catch-up adjustment in July 2016 was published in the Federal Register, Volume 81, No. 127, on July 1, 2016 (81 FR 43042). The first annual adjustment in January 2017 was published in the Federal Register, Volume 82, No. 11, on January 18, 2017 (82 FR 5367).

BANK

APPENDICES

Appendix A: Chairman and Commissioner Biographies

Appendix B: Divisions and Offices

Appendix C: Glossary of Selected Terms

Appendix D: Acronyms and Abbreviations

APPENDIX A: CHAIRMAN AND COMMISSIONER BIOGRAPHIES

Jay Clayton
CHAIRMAN

Jay Clayton was nominated to chair the U.S. Securities and Exchange Commission on January 20, 2017 by President Donald Trump and sworn in on May 4, 2017, following confirmation by the U.S. Senate on May 2, 2017.

Prior to joining the Commission, Mr. Clayton was a partner at Sullivan & Cromwell LLP, where for over 20 years he advised public and private companies on a wide range of matters, including securities offerings, mergers and acquisitions, corporate governance, and regulatory and enforcement proceedings. His experience includes counseling companies in various industries and advising market participants on capital raising and trading matters in the United States and abroad, including while resident in Europe for five years.

Mr. Clayton has authored publications on securities law, cybersecurity, and other regulatory issues. From 2009 to 2017, he was an Adjunct Professor at the University of Pennsylvania Law School, teaching "M&A Through the Business Cycle" each spring semester as well as guest lecturing in other classes and at other institutions.

Prior to joining Sullivan & Cromwell, Mr. Clayton served as a law clerk for the Honorable Marvin Katz of the U.S. District Court for the Eastern District of Pennsylvania. A member of the New York and Washington, D.C. bars, Mr. Clayton studied and received degrees in engineering, economics, and law. He earned a B.S. in Engineering from the University of Pennsylvania, where he was the recipient of the Thouron Award for post-graduate study in the United Kingdom, enabling him to earn a B.A. and M.A. in Economics from the University of Cambridge. Mr. Clayton received a J.D. from the University of Pennsylvania Law School.

Kara M. Stein
COMMISSIONER

Kara M. Stein was appointed by President Barack Obama to the U.S. Securities and Exchange Commission (SEC) and was sworn in on August 9, 2013.

While at the Commission, Commissioner Stein has advocated for strong investor protections and for initiatives to further increase competition and facilitate capital formation. Commissioner Stein has focused on identifying ways to enhance our securities market structure to promote efficiency and resiliency. She also has advocated for updating the Commission's rules and practices for the Digital Age, including calling for the formation of a Digital Disclosure Task Force to aid in the Commission's assessment of the nature, timing, and delivery of information to a variety of investors and other market participants. In addition, Commissioner Stein has advocated for the formation of an Office of Data Strategy and a Chief Data Officer to concentrate on the governance and utilization of information in a data-driven environment. She is also a strong advocate for the timely completion of the consolidated audit trail (CAT); the shortening of the settlement cycle for equities and fixed income; enhanced clearing agency standards; and the further development of tools that facilitate the use of machine readable disclosures.

Commissioner Stein serves as the Commission's liaison to the North American Securities Administrators Association (NASAA), represents the Commission at meetings of the International Organization of Securities Commissions (IOSCO), and is an ardent supporter of furthering diversity and inclusion initiatives at the SEC. Currently, Commissioner Stein sponsors the SEC's LGBT and the Disability Interests Advisory Committees, and she serves as the Chair of the SEC's Diversity Council.

Commissioner Stein joined the Commission after serving as Senior Policy Advisor for securities and banking matters to U.S. Sen. Jack Reed. From 2009 to 2013, she was Staff Director of the Securities, Insurance, and Investment Subcommittee of the U.S. Senate Committee on Banking, Housing, and Urban Affairs. During that time, Commissioner Stein played an integral role in drafting and negotiating significant provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act.

During her tenure in the U.S. Senate, Commissioner Stein also served as Staff Director of the Banking Committee's Subcommittee on Housing and Transportation, as Legal Counsel to Sen. Jack Reed, and a Legislative Assistant to Sen. Chris Dodd.

Before working in the U.S. Senate, Commissioner Stein was an associate at the law firm of Wilmer, Cutler & Pickering, an assistant professor with the University of Dayton School of Law, an Advocacy Fellow with the Georgetown University Law Center, and a Skadden Public Interest Fellow.

Commissioner Stein received her B.A. from Yale College and J.D. from Yale Law School.

Michael S. Piwowar
COMMISSIONER

Michael S. Piwowar was first appointed to the U.S. Securities and Exchange Commission (SEC) by President Barack Obama and was sworn in on August 15, 2013. Dr. Piwowar was designated Acting Chairman of the Commission by President Donald Trump from January 23, 2017, to May 4, 2017.

Previously, Dr. Piwowar was the Republican chief economist for the U.S. Senate Committee on Banking, Housing, and Urban Affairs under Senators Mike Crapo (R-ID) and Richard Shelby (R-AL). He was the lead Republican economist on the four SEC-related titles of the Dodd-Frank Act and the JOBS Act. Dr. Piwowar also worked on a number of important SEC-related oversight issues under the jurisdiction of the Committee, such as securities, over-the-counter derivatives, investor protection, market structure, and capital formation.

During the financial crisis and its immediate aftermath, Dr. Piwowar served in a one-year fixed-term position at the White House as a senior economist at the President's Council of Economic Advisers (CEA) in both the George W. Bush and Barack Obama Administrations. While at the CEA, Dr. Piwowar also served as a staff economist for the Financial Regulatory Reform Working Group of the President's Economic Recovery Advisory Board.

Before joining the White House, Dr. Piwowar worked as a Principal at the Securities Litigation and Consulting Group (SLCG). At SLCG, he provided economic consulting to law firms involved in complex securities litigation and technical assistance on market structure, regulatory policy, and risk management issues to domestic and international securities regulators and market participants.

Dr. Piwowar's first tenure at the SEC was in the Office of Economic Analysis (now called the Division of Economic and Risk Analysis) as a visiting academic scholar on leave from Iowa State University and as a senior financial economist. In those roles, he provided economic analyses and other technical support to the Commission and other SEC Divisions and Offices on a wide range of rulemaking, compliance, and enforcement matters.

Dr. Piwowar was an assistant professor of finance at Iowa State University where he focused his research on market microstructure and taught undergraduate and graduate courses in corporate finance and investments. He published a number of articles in leading academic publications and received several teaching and research awards.

Dr. Piwowar received a B.A. in Foreign Service and International Politics from the Pennsylvania State University, an M.B.A. from Georgetown University, and a Ph.D. in Finance from the Pennsylvania State University.

APPENDIX B: DIVISIONS AND OFFICES

Headquarters

DIVISION OF CORPORATION FINANCE
William Hinman, Director
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DIVISION OF ECONOMIC AND RISK ANALYSIS
Jeffrey Harris, Director
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DIVISION OF ENFORCEMENT
Stephanie Avakian, Co-Director
Steven Peikin, Co-Director
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DIVISION OF INVESTMENT MANAGEMENT
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DIVISION OF TRADING AND MARKETS
Brett Redfearn, Director
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OFFICE OF ACQUISITIONS
Vance Cathell, Director
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OFFICE OF ADMINISTRATIVE LAW JUDGES
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Chief Administrative Law Judge
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OFFICE OF THE CHIEF ACCOUNTANT
Wesley Bricker, Chief Accountant
(202) 551-5300

OFFICE OF THE CHIEF OPERATING OFFICER
Kenneth A. Johnson, Acting Chief Operating Officer
(202) 551-2200

OFFICE OF COMPLIANCE INSPECTIONS AND EXAMINATIONS
Peter Driscoll, Director
(202) 551-6200

OFFICE OF CREDIT RATINGS
Jessica Kane, Acting Director
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OFFICE OF EQUAL EMPLOYMENT OPPORTUNITY
Peter Henry, Acting Director
(202) 551-6040

OFFICE OF THE ETHICS COUNSEL
Shira Pavis Minton, Ethics Counsel/
Designated Agency Ethics Official
(202) 551-5170

OFFICE OF FINANCIAL MANAGEMENT
Caryn Kauffmann, Acting Chief Financial Officer
(202) 551-7840

OFFICE OF THE GENERAL COUNSEL
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OFFICE OF HUMAN RESOURCES
Lacey Dingman,
Chief Human Capital Officer
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OFFICE OF INFORMATION TECHNOLOGY
Pamela Dyson, Director/Chief Information Officer
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OFFICE OF INSPECTOR GENERAL
Carl W. Hoecker, Inspector General
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OFFICE OF INTERNATIONAL AFFAIRS
Paul A. Leder, Director
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OFFICE OF THE INVESTOR ADVOCATE
Rick Fleming, Investor Advocate
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OFFICE OF INVESTOR EDUCATION AND ADVOCACY
Lori Schock, Director
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OFFICE OF LEGISLATIVE AND INTERGOVERNMENTAL AFFAIRS
Bryan Wood, Director
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OFFICE OF MINORITY AND WOMEN INCLUSION
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OFFICE OF MUNICIPAL SECURITIES
Rebecca Olsen, Acting Director
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OFFICE OF PUBLIC AFFAIRS
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OFFICE OF THE SECRETARY
Brent Fields, Secretary
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OFFICE OF STRATEGIC INITIATIVES
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OFFICE OF SUPPORT OPERATIONS
Barry Walters, Director/Chief FOIA Officer
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Note: As required by the SEC Small Business Advocate Act of 2016, the agency created the Office of the Advocate for Small Business Capital Formation in FY 2017. This office will be staffed in FY 2018.

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APPENDIX C: GLOSSARY OF SELECTED TERMS

Accountability of Tax Dollars Act of 2002
A federal law requiring most federal agencies that are not subject to the Chief Financial Officers Act of 1990 to prepare annual audited financial statements.

Annual Performance Report
Outlines the goals and intended outcomes of an agency's programs and initiatives.

Asset
A resource that embodies economic benefits or services that the reporting entity controls.

Broker-Dealers
A broker is any person engaged in the business of effecting transactions in securities for the account of others. A dealer is any person engaged in the business of buying and selling securities for his own account, through a broker or otherwise.

Chief Financial Officers Act of 1990
Legislation focused on improving the government's financial management, performance, and disclosure.

Clearing Agencies
Self-regulatory organizations that come in two types: clearing corporations and depositories. Clearing corporations compare member transactions (or report to members the results of exchange comparison operations), clear those trades and prepare instructions for automated settlement of those trades, and often act as intermediaries in making those settlements. Depositories hold securities certificates in bulk form for their participants and maintain ownership records of the securities on their own books.

Consolidated Audit Trail
A single, comprehensive database of orders to trade in National Market System securities and Over-the-Counter equities that enables regulators to more efficiently and thoroughly track all trading activity in the U.S. equity and options markets.

Custodial Activity
Revenue that is collected, and its disposition, by a federal agency on behalf of other entities is accounted for as a custodial activity of the collecting entity. SEC custodial collections include amounts collected from violators of securities laws as a result of enforcement proceedings.

Crowdfunding
A means of raising small amounts of equity capital without having to register with the SEC, as permitted by the Jumpstart Our Business Startups Act.

Cybersecurity
The steps taken to prevent illegal or unauthorized access to a computer system or network.

Deposit Fund
Consists of funds that do not belong to the federal government such as disgorgement, penalties, and interest collected and held on behalf of harmed investors, registrant monies held temporarily until earned by the SEC, and collections awaiting disposition or reclassification.

Derivative
A contract between two parties that specifies conditions (dates, resulting values of the underlying variables, and notional amounts) under which payments are to be made between the parties.

Disclosure
Information about a company's financial condition, results of operations and business that it makes public. Investors can use this information to make informed investment decisions about the company's securities.

Disgorgement
In civil court actions or in administrative hearings, the defendant (or respondent) can be ordered to pay disgorgement—a measure of the ill-gotten gains from the fraud. Where disgorgement is ordered, the judge or the Commission may also order that any money collected, including fines paid, be placed in a Fair Fund for distribution to investors who were the victims of the violation. Under this process, a plan for the administration and distribution of the funds will be developed. A claims administrator or disbursement agent often oversees the plan.

Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010
Legislation that enforces transparency and accountability while implementing rules for consumer protection.

Electronic Data Gathering, Analysis, and Retrieval System
The system that all public companies use to transmit required filings to the SEC.

Entity Assets
Assets that an agency is authorized to use in its operations.

Entity Accounts Receivable
Monies owed to the SEC generated from securities transaction fees and filing fees paid by registrants.

Exchange Revenue
Inflows of earned resources to an entity. Exchange revenues arise from exchange transactions, which occur when each party to the transaction sacrifices value and receives value in return. Examples include the sale of goods and services, entrance fees, and most interest revenue.

Exchanges
A place (physical or virtual) where stock traders come together to decide on the price of securities.

Exchange-Traded Fund
SEC-registered investment companies that offer investors a way to pool their money in a fund that invests in stocks, bonds, or other assets.

Fair Fund
A fund created by the SEC to return money to harmed investors.

Federal Accounting Standards Advisory Board
Develops the generally accepted accounting principles for the federal government.

Federal Civil Penalties Inflation Adjustment Act
Requires agencies to adjust its civil monetary penalties for inflation and requires them to make adjustments at least once every four years thereafter.

Federal Information Security Management Act
Requires federal agencies to conduct annual assessments of their information security and privacy programs; develop and implement remediation efforts for identified weaknesses and vulnerabilities; and report on compliance to the Office of Management and Budget.

Financial Industry Regulatory Authority
A private corporation that acts as a self-regulatory organization.

Foreign Corrupt Practices Act
Addresses transparency requirements under the Securities Exchange Act of 1934, and improper payments to foreign officials.

Fund Balance with Treasury
The amount of funds in the entity's accounts with the U.S. Treasury for which the entity is authorized to make expenditures and pay liabilities, and that have not been invested in federal securities.

Funds from Dedicated Collections
Accounts containing specifically identified revenues—often supplemented by other financing sources, that are required by statute to be used for designated activities, benefits, or purposes, and must be accounted for separately from the government's general revenues.

Gatekeepers
Professionals—such as attorneys, accountants, and other consultants—who are enlisted to help protect investors through the detection and prevention of compliance breakdowns and fraudulent schemes that cause investor harm.

General Funds—Salaries and Expenses
Appropriations by Congress that are used to carry out the agency's mission and day-to-day operations that may be used in accordance with spending limits established by Congress.

Generally Accepted Accounting Principles (GAAP)
A framework of accounting standards, rules, and procedures defined by the professional accounting industry.

Imputed Financing
Financing provided to the reporting entity by another federal entity covering certain costs incurred by the reporting entity.

Insider Trading
The purchase or sale of a security by someone who has access to material, nonpublic information about the security.

Intragovernmental Costs
Costs that arise from the purchase of goods and services from other components of the federal government.

Investment Advisers Act of 1940
The federal law that was created to regulate the actions of investment advisers. Advisers must register with the SEC in an effort to protect investors.

Investor Protection Fund
A fund established by the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 to pay awards to eligible whistleblowers who voluntarily provide the Commission with original information about a violation of federal securities laws. The program requires the Commission to pay an award, under regulations prescribed by the Commission and subject to certain limitations, to eligible whistleblowers who voluntarily provide the Commission with original information about a violation of federal securities laws that leads to the successful enforcement of a covered judicial or administrative action, or a related action.

Jumpstart Our Business Startups (JOBS) Act
A federal law enacted on April 5, 2012, intended to encourage small businesses within the United States by easing securities regulations for those businesses.

Liability
A present obligation of the reporting entity to provide assets or services to another entity at a determinable date, when a specified event occurs, or on demand.

Market Based Treasury Securities
Debt securities that the U.S. Treasury issues to federal entities without statutorily determined interest rates.

Microcap Fraud
Fraud involving microcap companies.

Miscellaneous Receipt Account
A fund used to collect non-entity receipts from custodial activities that the SEC cannot deposit into funds under its control or use in its operations. These amounts are forwarded to the U.S. Treasury General Fund and are considered to be non-entity assets of the SEC.

Money Market Fund
A type of mutual fund registered under the Investment Company Act of 1940 and regulated pursuant to rule 2a-7 under the Act. Money market funds generally limit their investments to short-term high-quality debt securities that fluctuate very little in value under normal market conditions.

Municipal Advisor
A person (who is not a municipal entity or an employee of a municipal entity) that: (1) provides advice to or on behalf of a municipal entity or obligated person with respect to municipal financial products or the issuance of municipal securities, including advice with respect to the structure, timing, terms, and other similar matters concerning such financial products or issues or (2) undertakes a solicitation of a municipal entity. This definition includes financial advisors, guaranteed investment contract brokers, third-party marketers, placement agents, solicitors, finders, and swap advisors that provide municipal advisory services, unless they are statutorily excluded.

Municipal Securities Rulemaking Board
Writes investor protection rules and other rules regulating broker-dealers and banks in the U.S. municipal securities market, including tax-exempt and taxable municipal bonds, municipal notes, and other securities issued by states, cities, and counties or their agencies to help finance public projects or for other public policy.

Nationally Recognized Statistical Rating Organization
Credit rating agencies that have registered with the Commission, and meet certain disclosure, governance, internal controls, conflict of interest, and recordkeeping requirements.

Non-Entity Assets
Assets that are held by an entity but are not available to the entity. Examples of non-entity assets are disgorgement, penalties, and interest collected and held on behalf of harmed investors.

Office of Inspector General (OIG) SEC Employee Suggestion Program
As required by Section 966 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, this program allows employees to submit suggestions concerning improvements in the SEC's work efficiency, effectiveness, productivity, and use of its resources. The OIG also receives allegations by employees of waste, abuse, misconduct, or mismanagement within the SEC through the program.

Office of Management and Budget
Helps the President oversee the federal budget and supervise federal agencies.

OMB Circular A-123, *Management's Responsibility for Enterprise Risk Management and Internal Control*

Defines management's responsibilities for enterprise risk management and internal financial controls, including administrative and program activities as well as financial activities.

OMB Circular A-136, *Financial Reporting Requirements*

Establishes a central point of reference for all federal financial reporting guidance.

Performance and Accountability Report

An annual report that provides program performance and financial information that enables Congress, the President, and the public to assess an agency's performance and accountability over entrusted resources.

Ponzi Scheme

A fraudulent scheme in which returns are paid to established investors with funds from new investors rather than from profits.

Public Company Accounting Oversight Board

A nonprofit corporation established by Congress to oversee the audits of public companies in order to protect the interests of investors and further the public interest in the preparation of informative, accurate, and independent audit reports. The Board also oversees the audits of broker-dealers, including compliance reports filed pursuant to federal securities laws, to promote investor protection.

Pump-and-Dump Schemes

An investment scheme in which promoters tout a company's stock through false or misleading statements that often includes claiming to have inside information. Once the stock price is "pumped," the promoters sell—or "dump"—their shares, thus dropping the overall value.

Pyramid Scheme

A scheme in which participants attempt to make money solely by recruiting new participants into the program. The hallmark of these schemes is the promise of sky-high returns in a short period of time for doing nothing other than handing over your money and getting others to do the same.

Regulation A

An exemption of the Securities Act of 1933 that requires registration for offerings of up to $50 million of securities in a 12-month period.

Regulation S-K

The central repository for the SEC's non-financial statement disclosure requirements.

Regulation Systems Compliance and Integrity (Regulation SCI)

Aims to strengthen the technology structure of the securities market.

Reserve Fund

A fund established by the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 that may be used by the SEC to obligate amounts up to $100 million in one fiscal year as the SEC determines is necessary to carry out its functions.

Sarbanes-Oxley Act of 2002

Legislation aimed at enhancing corporate responsibility and financial disclosures, and fighting corporate and accounting fraud that created the Public Company Accounting Oversight Board.

Section 31 Fees

Transaction fees paid to the SEC based on the volume of securities that are sold on various markets. These fees recover the costs incurred while supervising and regulating the securities markets and securities professionals.

Securities Act of 1933
One of the primary federal securities laws, its basic objectives are to require that investors receive financial and other significant information about securities being offered for public sale, and to prohibit deceit, misrepresentation, and other fraud in the sale of securities.

Securities Exchange Act of 1934
A law governing the secondary trading of securities (stocks, bonds, and debentures) in the United States. It was this piece of legislation that established the SEC.

Self-Regulatory Organization
An organization that exercises some degree of regulatory authority over an industry or profession. The regulatory authority could be applied in addition to some form of government regulation, or it could fill the vacuum of an absence of government oversight and regulation. The ability of a self-regulatory organization to exercise regulatory authority does not necessarily derive from a grant of authority from the government.

Statement of Cash Flows
Reports a company's inflows and outflows of cash over time by classification.

Strategic Plan
Defines an agency's mission, long-term goals, strategies planned, and the approaches it will use to monitor its progress in addressing specific national problems, needs, challenges, and opportunities related to its mission.

Tick Size Pilot
A data-driven assessment of securities for companies with smaller capitalization.

Transfer Agent
A trust company, bank, or similar financial institution assigned by a corporation to maintain records of investors and account balances; as such, the transfer agent issues and cancels certificates to reflect changes in ownership and handles lost, destroyed, or stolen certificates.

Whistleblower
A person who, alone or jointly with others, provides the Commission with information pursuant to the procedures set forth in Rule 21F-9(a) under the Exchange Act, and the information relates to a possible violation of the federal securities laws (including any rules or regulations thereunder) that have occurred, are ongoing, or are about to occur. A whistleblower must be an individual. A company or another entity is not eligible to be a whistleblower.

eXtensible Business Reporting Language (XBRL)
XBRL defines or "tags" data using standard definitions to establish a consistent structure of identity and context for financial information, which can then be recognized and processed by a variety of different software applications.

APPENDIX D: ACRONYMS AND ABBREVIATIONS

AFR	Agency Financial Report
APR	Annual Performance Report
CAT	Consolidated Audit Trail
CFO	Chief Financial Officer
CM	Continuous Monitoring Program
COR	Contracting Officer's Representative
CSRS	Civil Service Retirement System
DHS	U.S. Department of Homeland Security
DOL	U.S. Department of Labor
EDGAR	Electronic Data Gathering, Analysis, and Retrieval System
ETF	Exchange-Traded Funds
FASAB	Federal Accounting Standards Advisory Board
FBWT	Fund Balance with Treasury
FCPA	Foreign Corrupt Practices Act
FCPIA	Federal Civil Penalties Inflations Adjustment Act
FECA	Federal Employees' Compensation Act
FERS	Federal Employees Retirement System
FEVS	Federal Employee Viewpoint Survey
FFMIA	Federal Financial Management Improvement Act
FINRA	Financial Industry Regulatory Authority
FISMA	Federal Information Security Management Act
FMFIA	Federal Managers' Financial Integrity Act of 1982
FOIA	Freedom of Information Act
FSSP	Federal Shared Service Provider
FTC	Federal Trade Commission
FTE	Full-Time Equivalents
FY	Fiscal Year
GAAP	Generally Accepted Accounting Principles
GAO	U.S. Government Accountability Office
GPRA	U.S. Government Performance and Results Act
GSA	U.S. General Services Administration
ICFR	Internal Control over Financial Reporting
IOSCO	International Organization of Securities Commissions
IPERA	Improper Payments Elimination and Recovery Act of 2010
IPERIA	Improper Payments Elimination and Recovery Improvement Act of 2012
IPIA	Improper Payments Information Act of 2002
IPO	Initial Public Offering
IRA	Individual Retirement Account
IT	Information Technology
JOBS	Jumpstart Our Business Startups Act

MSRB	Municipal Securities Rulemaking Board
NEP	National Examination Program
NIST	National Institute of Standards and Technology
NMS	National Market System
NRSRO	Nationally Recognized Statistical Rating Organization
OMB	Office of Management and Budget
OPM	Office of Personnel Management
POA&Ms	Plans of Actions and Milestones
PCAOB	Public Company Accounting Oversight Board
PII	Personally Identifiable Information
S&P	Standard & Poor
S/L	Straight-Line
SBR	Statement of Budgetary Resources
SEC	U.S. Securities and Exchange Commission
SFFAS	Statement of Federal Financial Accounting Standards
SIPA	Securities Investor Protection Act of 1970
SIPC	Securities Investor Protection Corporation
SRO	Self-Regulatory Organization
TCP	Technology Controls Program
TCR	Tips, Complaints, and Referrals
TSP	Thrift Savings Plan
XBRL	eXtensible Business Reporting Language

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To comment on this report, please send an email to SECAFR@sec.gov.

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