United States Government Accountability Office

GAO

Report to the Chairman, U.S. Securities and Exchange Commission

November 2009

FINANCIAL AUDIT

Securities and Exchange Commission's Financial Statements for Fiscal Years 2009 and 2008

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Accountability * Integrity * Reliability

GAO-10-250

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Highlights

Highlights of GAO-10-250, a report to the Chairman, U.S. Securities and Exchange Commission

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FINANCIAL AUDIT

Securities and Exchange Commission's Financial Statements for Fiscal Years 2009 and 2008

Why GAO Did This Study

Established in 1934 to enforce the securities laws and protect investors, the United States Securities and Exchange Commission (SEC) plays an important role in maintaining the integrity of the U.S. securities markets.

Pursuant to the Accountability of Tax Dollars Act of 2002, SEC is required to prepare and submit to Congress and the Office of Management and Budget audited financial statements. GAO agreed, under its audit authority, to perform the audit of SEC's financial statements to determine whether (1) the financial statements are fairly stated, and (2) SEC management maintained effective internal control. GAO also tested SEC's compliance with selected provisions of significant laws and regulations.

What GAO Recommends

In connection with our prior audits, GAO has made numerous recommendations to SEC to address the internal control issues that continued to persist during fiscal year 2009. GAO will continue to monitor SEC's progress in implementing the recommendations that remain open as of the date of this report.

SEC stated it is committed to making the resolution of the six significant deficiencies identified this fiscal year a high priority, and is developing a plan to remediate the resulting aggregate material weakness over information systems and related financial controls in order to strengthen SEC's financial reporting.

View GAO-10-250 or key components.
For more information, contact James R. Dalkin at (202) 512-9406 or dalkinj@gao.gov.

What GAO Found

In GAO's opinion, SEC's fiscal years 2009 and 2008 financial statements are fairly presented in all material respects. However, in GAO's opinion, SEC did not have effective internal control over financial reporting as of September 30, 2009. Recommendations for corrective action will be included in a separate report.

During this year's audit, we identified six significant deficiencies that collectively represent a material weakness in SEC's internal control over financial reporting. The significant deficiencies involve SEC's internal control over (1) information security, (2) financial reporting process, (3) fund balance with Treasury, (4) registrant deposits, (5) budgetary resources, and (6) risk assessment and monitoring processes. These internal control weaknesses give rise to significant management challenges that have reduced assurance that data processed by SEC's information systems are reliable and appropriately protected; impaired management's ability to prepare its financial statements without extensive compensating manual procedures; and resulted in unsupported entries and errors in the general ledger.

As we reported last year, SEC's ability to sustain effective internal control over financial reporting was at risk due to its continued reliance on processes and systems that were not designed to provide the accurate, complete, and timely transaction-level financial information that management needs to make well-informed decisions, or to accumulate and report reliable financial information without extensive manual workarounds and compensating controls. During this year's audit, the nature of the errors and related internal control deficiencies we found indicate that SEC was unable to sustain the level of effort and resources needed to compensate for these deficient processes and systems to achieve effective internal control over financial reporting.

These deficiencies are likely to continue to exist until SEC's general ledger system is either significantly enhanced or replaced, key accounting activity is fully integrated with the general ledger at the transaction level, information security controls are strengthened, and appropriate resources are dedicated to maintaining effective internal controls. In the interim, SEC will need to place greater emphasis on monitoring the current risks and vulnerabilities, along with the related compensating procedures, to determine whether these risks are being adequately mitigated on an ongoing basis. Successfully addressing these issues is critical to maintaining SEC's credibility given its important role in the financial reporting process of registrants, and is vital to achieving SEC's stated vision to be the standard against which federal agencies are measured.

Contents

Abbreviations

EDGAR	Electronic Data Gathering, Analysis, and Retrieval
FBWT	Fund Balance with Treasury
FMFIA	Federal Managers' Financial Integrity Act
FMS	Financial Management Service
OMB	Office of Management and Budget
SAS	Statement on Auditing Standards
SEC	United States Securities and Exchange Commission

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Accountability * Integrity * Reliability

United States Government Accountability Office
Washington, DC 20548

November 16, 2009

The Honorable Mary Schapiro
Chairman
United States Securities
and Exchange Commission

Dear Ms. Schapiro:

The accompanying report presents the results of our audits of the financial statements of the United States Securities and Exchange Commission (SEC) as of, and for the fiscal years ending, September 30, 2009, and 2008. The Accountability of Tax Dollars Act of 2002 requires that SEC prepare and submit audited financial statements to Congress and the Office of Management and Budget (OMB). We agreed, under our audit authority, to audit SEC's financial statements.

This report contains our (1) unqualified opinions on SEC's financial statements, (2) opinion that SEC's internal control over financial reporting was not effective as of September 30, 2009, and (3) conclusion that we found no reportable compliance issues during fiscal year 2009. The accompanying report also discusses other significant issues that we identified in performing our audit that we believe warrant the attention of SEC management and users of SEC's financial statements.

We are sending copies of this report to the Chairmen and Ranking Members of the Senate Committee on Banking, Housing, and Urban Affairs; the Senate Committee on Homeland Security and Governmental Affairs; the House Committee on Financial Services; and the House Committee on Oversight and Government Reform. We are also sending copies to the Secretary of the Treasury, the Director of OMB, and other interested parties. In addition, this report will be available at no charge on our Web site at http://www.gao.gov.

If you have questions about this report, or if I can be of further assistance, please contact me at (202) 512-9406 or dalkinj@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report.

Sincerely yours,

James R. Dalkin
Director
Financial Management and Assurance

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United States Government Accountability Office
Washington, DC 20548

To the Chairman of the United States Securities and Exchange Commission

In our audits of the United States Securities and Exchange Commission (SEC) for fiscal years 2009 and 2008, we found

- the financial statements as of and for the fiscal years ended September 30, 2009, and 2008, including the accompanying notes, are presented fairly, in all material respects, in conformity with U.S. generally accepted accounting principles;
- SEC's internal control over financial reporting was not effective as of September 30, 2009; and
- no reportable noncompliance with laws and regulations we tested.

SEC was able to produce financial statements that were fairly stated in all material respects for the sixth consecutive year since SEC began preparing audited financial statements. However, over these 6 years, SEC has struggled with material weaknesses[1] and significant deficiencies[2] in internal control that we have reported at various times since 2004. We have also reported that, notwithstanding the periodic efforts and significant resources SEC has expended to compensate for these deficiencies, these efforts were not always permanent effective solutions and SEC's ability to sustain effective internal control over financial reporting remained at risk. For example, in fiscal year 2008, SEC undertook a significant initiative to address previously reported weaknesses in its financial reporting process. This initiative, which included general ledger system enhancements and the implementation of new control processes, involved significant resources and an intensive focus on compensating measures from SEC to reasonably assure reliable financial reporting during 2008. However, during this year's audit, the nature of the errors and related internal control deficiencies we found in SEC's financial reporting process indicate that SEC was unable to sustain

[1]A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

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

the level of effort and resources needed to compensate for these deficiencies to maintain effective internal control over financial reporting.

As discussed in more detail later in this report, the internal control deficiencies that we identified in fiscal year 2009 collectively represent a material weakness in SEC's internal control over financial reporting and give rise to significant management challenges that have (1) increased the risk that data processed by SEC's information systems are not reliable or appropriately protected, (2) impaired management's ability to prepare its financial statements without extensive manual procedures, and (3) resulted in unsupported entries and errors in the general ledger. This material weakness is primarily caused by SEC's continued reliance on processes and systems that were not designed to provide the accurate, complete, and timely transaction-level financial information that management needs to make well-informed decisions, or to accumulate and report reliable financial information without extensive manual workarounds and compensating controls. These problems are likely to continue to exist until SEC's general ledger system is either significantly enhanced or replaced, key accounting activity is fully integrated with the general ledger at the transaction level, information security controls are strengthened, and appropriate resources are dedicated to maintaining effective internal controls. In the interim, SEC will need to place greater emphasis on monitoring the current risks and vulnerabilities, along with the related compensating procedures, in order to determine whether these risks are being adequately mitigated on an ongoing basis. Successfully addressing these issues is critical to maintaining SEC's credibility given its role in the financial reporting process of SEC registrants, and is vital to achieving SEC's stated vision to be the standard against which federal agencies are measured.

The following sections discuss in more detail these conclusions as well as our conclusions on Management's Discussion and Analysis and other supplementary information. They also present information on the objectives, scope, and methodology of our audit and our discussion of SEC management's comments on a draft of this report.

Opinion on Financial Statements

SEC's financial statements, including the accompanying notes, present fairly, in all material respects, in conformity with U.S. generally accepted accounting principles, SEC's assets, liabilities, and net position as of September 30, 2009, and September 30, 2008; and net costs, changes in net position, budgetary resources, and custodial activity for the fiscal years then ended.

Opinion on Internal Control

Because of the material weakness in internal control discussed below, SEC did not maintain, in all material respects, effective internal control over financial reporting as of September 30, 2009, and thus did not provide reasonable assurance that losses, misstatements, or noncompliance material in relation to the financial statements would be prevented or detected and corrected on a timely basis. Our opinion is based on criteria established under 31 U.S.C. sec. 3512(c), (d), commonly known as the Federal Managers' Financial Integrity Act of 1982 (FMFIA).

During this year's audit, we identified six significant deficiencies that collectively represent a material weakness in SEC's internal control over financial reporting. SEC's own evaluation of the effectiveness of its internal controls during fiscal year 2009 identified and reported a similar material weakness in internal control over financial reporting.[3] This material weakness gives rise to significant management challenges that have (1) reduced assurance that data processed by SEC's information systems are reliable and appropriately protected, (2) impaired management's ability to prepare its financial statements without extensive compensating manual procedures, and (3) resulted in unsupported entries and errors in the general ledger. The issues that we have identified and discuss further in appendix I of this report relate to SEC's control deficiencies concerning (1) ineffective controls over information security, (2) ineffective financial reporting controls and general ledger system reporting limitations, (3) the lack of timely reconciliations of its fund balance with Treasury and support for making adjusting entries to resolve differences, (4) untimely reviews and recognition of revenue in the correct period pertaining to registrant deposits, (5) ineffective processes and related documentation concerning budgetary transactions, and (6) inadequate assessment of its risks relevant to the preparation of financial statements and ineffective monitoring of its financial reporting internal controls. We reported on some of these issues last year[4] and in prior audits.

[3]SEC conducted an evaluation of its internal controls in accordance with the Office of Management and Budget's Circular No. A-123, *Management's Responsibility for Internal Control*, based on criteria established under FMFIA.

[4]GAO, *FINANCIAL AUDIT: Securities and Exchange Commission's Financial Statements for Fiscal Years 2008 and 2007*, GAO-09-173 (Washington, D.C.: Nov. 14, 2008).

In our last year's audit, we reported a significant deficiency in SEC's property and equipment controls. During fiscal year 2009, SEC improved its controls over the receipt and acceptance of property acquisitions and the controls for recording internal-use software projects and acquisition costs such that we no longer consider this to be a significant deficiency at September 30, 2009.

Despite its material weakness in internal control, SEC was able to prepare financial statements that were fairly stated in all material respects for fiscal years 2009 and 2008. However, the material weakness in SEC's internal control over financial reporting noted above may adversely affect any decision by SEC's management that is based, in whole or in part, on information that is inaccurate because of this weakness. In addition, unaudited financial information reported by SEC may also contain misstatements resulting from this weakness. We considered the material weakness identified above in determining the nature, timing, and extent of our audit procedures on SEC's fiscal years 2009 financial statements. We caution that misstatements may occur and not be detected by our tests and that such testing may not be sufficient for other purposes.

We will be reporting additional details concerning this material weakness separately to SEC management, along with recommendations for corrective actions. We also identified other deficiencies in SEC's system of internal control which we do not consider to be material weaknesses or significant deficiencies but which merit SEC management's attention and correction. We have communicated these matters to SEC management informally and as appropriate, will be reporting them in writing to SEC separately.

Compliance with Laws and Regulations

Our tests of SEC's compliance with selected provisions of laws and regulations for fiscal year 2009 disclosed no instances of noncompliance that would be reportable under U.S. generally accepted government auditing standards. The objective of our audit was not to provide an opinion on overall compliance with laws and regulations. Accordingly, we do not express such an opinion.

Consistency of Other Information

SEC's Management Discussion and Analysis and other accompanying information contain a wide range of data, some of which are not directly related to the financial statements. We did not audit and we do not express an opinion on this information. However, we compared this information for consistency with the financial statements and discussed the methods of measurement and presentation with SEC officials. On the basis of this limited work, we found no material inconsistencies with the financial statements, U.S. generally accepted accounting principles, or the Office of Management and Budget Circular No. A-136, *Financial Reporting Requirements*.

Objectives, Scope, and Methodology

SEC management is responsible for (1) preparing the financial statements in conformity with U.S. generally accepted accounting principles; (2) establishing and maintaining effective internal control over financial reporting, and evaluating its effectiveness; and (3) complying with applicable laws and regulations. SEC management evaluated the effectiveness of SEC's internal control over financial reporting as of September 30, 2009, based on the criteria established under FMFIA. SEC management's assertion based on its evaluation is presented in its Management Discussion and Analysis included in this report.

We are responsible for planning and performing the audit to obtain reasonable assurance and provide our opinion about whether (1) the SEC's financial statements are presented fairly, in all material respects, in conformity with U.S. generally accepted accounting principles; and (2) SEC management maintained, in all material respects, effective internal control over financial reporting as of September 30, 2009. We are also responsible for (1) testing compliance with selected provisions of laws and regulations that have a direct and material effect on the financial statements, and (2) performing limited procedures with respect to certain other information accompanying the financial statements.

In order to fulfill these responsibilities, we

- examined, on a test basis, evidence supporting the amounts and disclosures in the financial statements;
- assessed the accounting principles used and significant estimates made by SEC management;
- evaluated the overall presentation of the financial statements;
- obtained an understanding of SEC and its operations, including its internal control over financial reporting;

- considered SEC's process for evaluating and reporting on internal control over financial reporting that is required by FMFIA;
- assessed the risk that a material misstatement exists in the financial statements and the risk that a material weakness exists in internal control over financial reporting;
- evaluated the design and operating effectiveness of internal control over financial reporting based on the assessed risk;
- tested relevant internal control over financial reporting;
- tested compliance with selected provisions of the following laws and regulations: the Securities Exchange Act of 1934, as amended; the Securities Act of 1933, as amended; the Antideficiency Act; laws governing the pay and allowance system for SEC employees; the Debt Collection Improvement Act of 1996; the Prompt Payment Act; the Federal Employees' Retirement System Act of 1986; the Continuing Appropriations Resolution, 2009, as amended; the Financial Services and General Government Appropriations Act, 2009; and the Supplemental Appropriations Act, 2009; and
- performed such other procedures as we considered necessary in the circumstances.

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

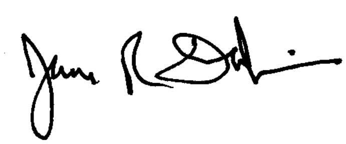
We did not evaluate all internal controls relevant to operating objectives as broadly established under FMFIA, such as those controls relevant to preparing statistical reports and ensuring efficient operations. We limited our internal control testing to controls over financial reporting. Because of inherent limitations, internal control may not prevent or detect and correct misstatements due to error or fraud, losses, or noncompliance. We also caution that projecting any evaluation of effectiveness to future periods is subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

We did not test compliance with all laws and regulations applicable to SEC. We limited our tests of compliance to selected provisions of laws and regulations that have a direct and material effect on the financial statements for the fiscal year ended September 30, 2009. We caution that noncompliance may occur and not be detected by these tests and that such testing may not be sufficient for other purposes.

We performed our audit in accordance with U.S. generally accepted government auditing standards. We believe our audit provides a reasonable basis for our opinions and other conclusions.

SEC Comments and Our Evaluation

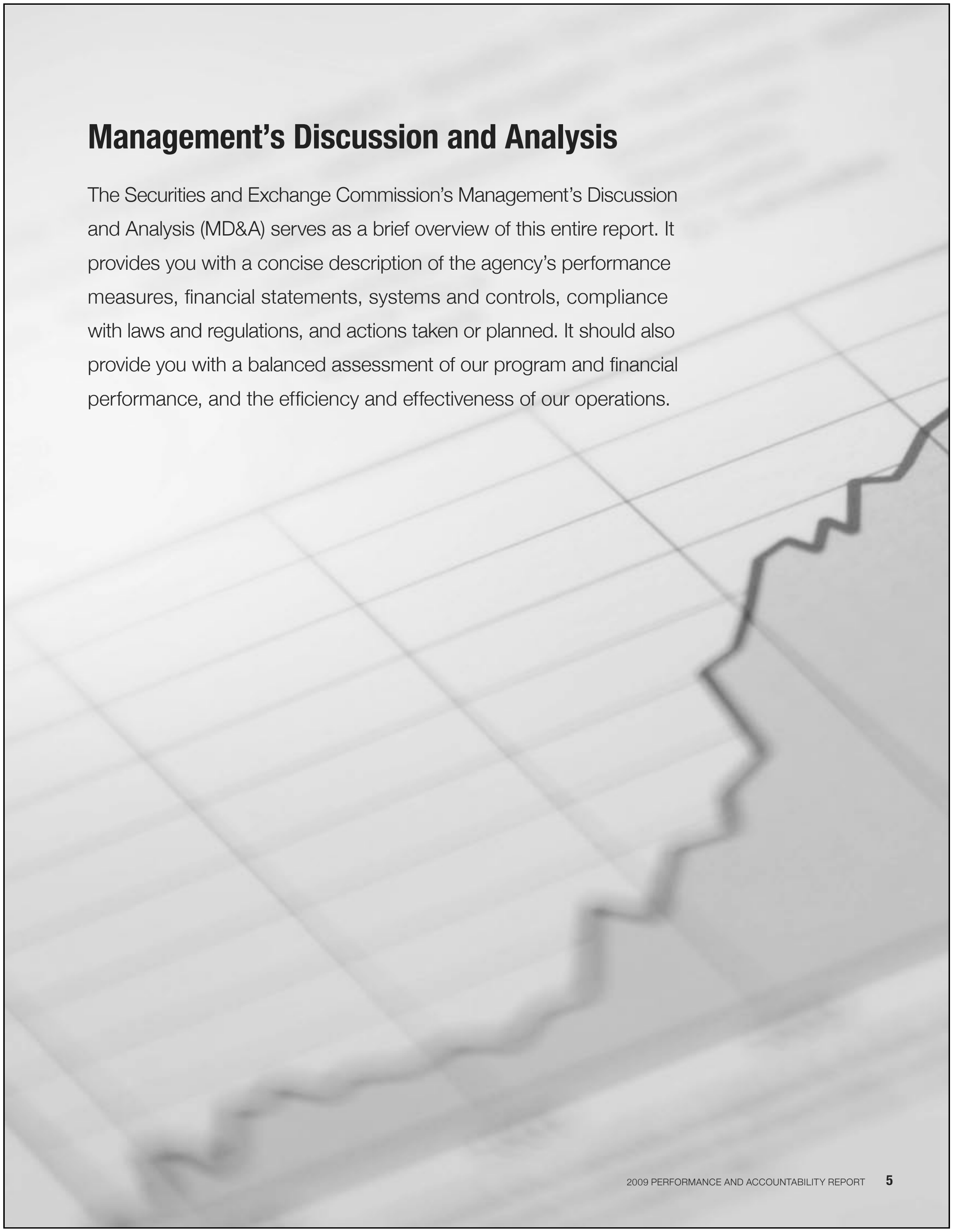
In commenting on a draft of this report, SEC's Chairman stated that SEC is committed to making the resolution of the six significant control deficiencies GAO has identified a high priority, and is developing a plan to remediate the resulting aggregate material weakness over information systems and related financial controls. She also stated that, over the next couple of months, SEC will tackle the identified systems, controls, and operational issues in order to strengthen the reliability of its financial reporting. The complete text of SEC's response is reprinted in appendix II.



James R. Dalkin
Director
Financial Management and Assurance

November 16, 2009

Management's Discussion and Analysis



Management's Discussion and Analysis

The Securities and Exchange Commission's Management's Discussion and Analysis (MD&A) serves as a brief overview of this entire report. It provides you with a concise description of the agency's performance measures, financial statements, systems and controls, compliance with laws and regulations, and actions taken or planned. It should also provide you with a balanced assessment of our program and financial performance, and the efficiency and effectiveness of our operations.

Vision, Mission, Values, and Goals

Vision

The SEC's vision is to strengthen the integrity and soundness of U.S. securities markets for the benefit of investors and other market participants, and to conduct its work in a manner that is as sophisticated, flexible, and dynamic as the securities markets it regulates.

Mission

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

Values

In managing the evolving needs of a complex marketplace and in pursuing its mission, the SEC embraces the following values:

- Integrity
- Accountability
- Fairness
- Resourcefulness
- Teamwork
- Commitment to Excellence

During 2009, managers and staff from across the Securities and Exchange Commission worked to prepare a new strategic plan covering FYs 2010–2015. The draft plan addresses the agency's mission, vision, values, strategic goals, major initiatives, and performance measures. In October, the plan was made available for public comment and can be accessed on the SEC's Web site at http://www.sec.gov/about/secstratplan1015.pdf.

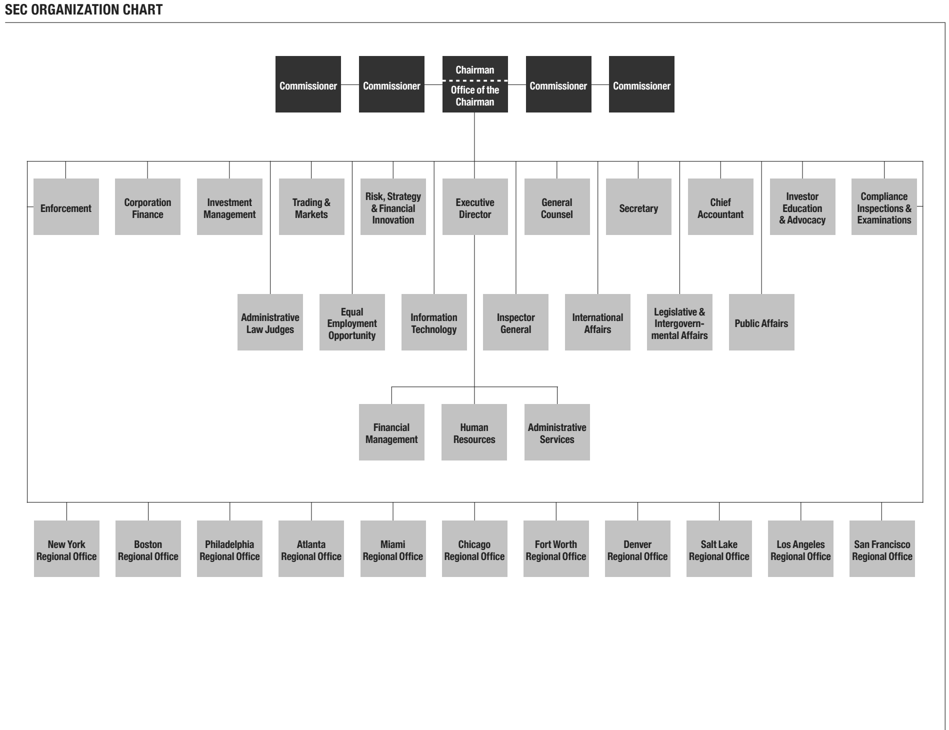
Goals

- **Enforce compliance with federal securities laws**
  The Commission seeks to detect problems in the securities markets, prevent and deter violations of federal securities laws, and alert investors to possible wrongdoing. When violations occur, the SEC aims to take prompt action to halt the misconduct, sanction wrongdoers effectively, and, where possible, return funds to harmed investors.
- **Promote healthy capital markets through an effective and flexible regulatory environment**
  The savings and investments of every American are dependent upon healthy capital markets. The Commission seeks to sustain an effective and flexible regulatory environment that will facilitate innovation, competition, and capital formation to ensure that our economy can continue to grow and create jobs for our nation's future. Enhancing the productivity of America is a key goal that the SEC works to achieve by increasing investor confidence in the capital markets.
- **Foster informed investment decision making**
  An educated investing public ultimately provides the best defense against fraud and costly mistakes. The Commission works to promote informed investment decisions through two main approaches: reviewing disclosures of companies and mutual funds to ensure that clear, complete, and accurate information is available to investors; and implementing a variety of investor education initiatives.
- **Maximize the use of SEC resources**
  The investing public and the securities markets are best served by an efficient, well-managed, and proactive SEC. The agency strives to improve its organizational effectiveness by making sound investments in human capital and new technologies, and by enhancing internal controls.

Organizational Structure and Resources

The U.S. Securities and Exchange Commission (SEC) is an independent federal agency established pursuant to the Securities Exchange Act of 1934 (Exchange Act). It is headed by a bipartisan five-member Commission, comprised of the Chairman and four Commissioners, who are appointed by the President and confirmed by the Senate (see *Appendix A: Chairman and Commissioners).* The Chairman serves as the chief executive officer (CEO). The SEC is organized into five main divisions: Enforcement; Corporation Finance; Investment Management; Trading and Markets; and Risk, Strategy, and Financial Innovation. The SEC's headquarters are in Washington, D.C., and it has 11 regional offices located throughout the country. In Fiscal Year (FY) 2009, the SEC received budget authority of $970 million consisting of current-year offsetting collections in the amount of $894 million, a two-year direct appropriation of $10 million, and $66 million in funds carried over from prior fiscal years. At September 30, 2009, the agency employed 3,642 Full-time Equivalents (FTE), including 3,584 permanent and 58 temporary FTE.

CHART 1.1
SEC ORGANIZATION CHART



FY 2009 Year in Review

Responses to Economic Crisis

The confidence of American investors was shaken over the past 18 months by a deep financial crisis, a pronounced decline in asset values, and a deterioration of the world economy. This confidence was further shaken by the revelation of the massive fraud perpetrated over many years by Bernard L. Madoff. Under the leadership of new Chairman Mary L. Schapiro, the SEC has worked to restore confidence by redoubling efforts to protect investors through vigilant and comprehensive examinations and enforcement activity, and by embarking on a series of reforms designed to make our markets stronger, safer, and more transparent. These reforms include working to close regulatory gaps, strengthening shareholder rights, and improving the quality of disclosures provided to investors. The reforms also include improvements to the internal operations of the SEC designed to enhance the ability of the agency to detect wrongdoing, punish violators quickly when it occurs, and identify and address as early as possible emerging problems that may threaten investors and the vitality of the capital markets.

Strengthening Enforcement and Examinations

In January 2009, the SEC launched a series of initiatives to enable enforcement efforts to proceed more swiftly and decisively against alleged securities law violators. To ensure that subpoena power is available to the staff as soon as it is needed, the Commission delegated the authority to initiate formal orders of investigation to the Division of Enforcement. In February, the SEC began a comprehensive review of its internal procedures to improve the way the agency tracks and handles the high volume of tips, complaints, and referrals received each year, and the Commission is now in the process of revamping this system. The new system will centralize this information so it can be analyzed and utilized in a more effective way to identify valuable leads for potential enforcement action and compliance exams. We are also creating an Office of Market Intelligence, within the Division of Enforcement, to improve the handling of tips and complaints.

A number of organizational reforms are also being implemented within Enforcement, as further ways to increase effectiveness. These reforms include creating units specializing in mission critical areas such as structured products and asset management, and streamlining the management structure.

To assist the Enforcement Division in identifying and bringing actions against wrongdoers, the SEC has asked Congress for expanded authority to reward whistleblowers who bring forward substantial evidence to the agency about significant federal securities law violations. Under proposed legislation, money collected from wrongdoers that is not otherwise distributed to investors would be used to establish a fund to reward whistleblowers whose contributions lead to successful enforcement actions.

The Office of Compliance Inspections and Examinations (OCIE) launched a variety of initiatives in 2009 designed to significantly improve compliance by registered broker-dealers, investment advisers, and credit rating agencies with the federal securities laws, and to improve the ability of OCIE to identify fraud and other serious wrongdoing. The Senior Specialized Examiner program was created in order to deepen the expertise available to the agency. Positions in this program are being filled by industry professionals with specialized experience in areas such as trading, portfolio management, valuation, complex products, sales, compliance, and forensic accounting. The SEC also worked to enhance the skill level of existing examination staff through certification as Certified Fraud Examiners, Chartered Financial Analysts, or Chartered Alternative Investment Analysts. The agency also conducted training sessions on complex issues such as options trading, and credit default swaps (CDS), hedge funds, and specialized programs on uncovering potential frauds and establishing third-party verification of customer assets.

Combating Abusive Short Selling

The SEC has taken significant action in FY 2009 to address issues surrounding short selling, particularly the problems raised by potentially abusive "naked" short selling.

In October 2008, the SEC adopted temporary rules to address concerns about the sudden and unexplained declines in the prices of equity securities and the deterioration in investor confidence in the U.S. financial markets. This crisis of confidence can impair the liquidity and ultimate viability of an entity, with potentially broad market consequences. A preliminary study by the SEC's Office of Economic Analysis found that these Commission actions had their intended effect—failures to deliver securities have decreased by approximately 57 percent across all equity securities. In July 2009, the Commission adopted the provisions of the temporary rule in a permanent rule designed to help maintain this reduction in failures to deliver securities and to help further address abusive practices in this area.

In addition to rulemaking, the SEC also brought two cases against broker-dealers and options traders for violations of Regulation SHO, the Commission's primary short sale regulation. In these actions, the SEC alleged that the respondents improperly claimed that they were entitled to an exception to the Regulation SHO requirements that broker-dealers must locate a source of borrowable shares prior to selling short, and that they circumvented the requirement to deliver securities sold short by a specified closeout date.

In April 2009, the Commission proposed short sale price test and circuit breaker rules. In May and September 2009, the SEC hosted roundtables to examine short selling practices. Topics included discussions on investor confidence and the necessity and effectiveness of short sale price tests and short sale circuit breakers, potential pre-borrow and disclosure requirements related to short selling, the operational and compliance issues raised by the SEC's recently proposed regulatory approaches in the area of short selling, and what empirical data say about short sale price tests and short sale circuit breakers. Completion of this rulemaking will be a high priority in early calendar year 2010.

Filling Regulatory Gaps

During FY 2009, the SEC took several steps to encourage central counterparties to clear CDS. The SEC worked closely with the Federal Reserve Board and the Commodity Futures Trading Commission (CFTC) to facilitate the establishment of central counterparties for over-the-counter CDS. Between December 2008 and July 2009, the Commission approved temporary exemptions allowing a number of entities to operate as central counterparties for clearing CDS. These central counterparties reduce counterparty risk in the CDS market.

The Administration has requested legislative authority to permit the SEC to require advisers to hedge funds and other private pools of capital to register with the Commission. If enacted, this oversight will better protect U.S. financial markets and enable investors, regulators, and the marketplace to have more complete and meaningful information about private fund advisers, the funds they manage, and their market activities.

Creation of New Division of Risk, Strategy, and Financial Innovation

In September 2009, the Commission created a new Division of Risk, Strategy, and Financial Innovation. The division combines the Office of Economic Analysis and the Office of Risk Assessment to provide the Commission with sophisticated analysis that integrates economic, financial, and legal disciplines. The new division will focus on strategic and long-term analysis, identifying new developments and trends in financial markets and systemic risk, and recommending ways to adjust Commission policies and practices to adapt to these new developments and trends.

In addition, the Commission created the Industry and Market Fellows Program in order to hire highly seasoned financial experts who will enhance the agency's expertise and perspectives on emerging issues and trends in the securities markets.

Major Enforcement Cases

The SEC pursued significant cases during FY 2009 that brought lawbreakers to justice, returned money to harmed investors, and sent a clear message of deterrence.

In December 2008, the SEC charged Bernard Madoff with securities fraud for a multibillion dollar Ponzi scheme he perpetrated on advisory clients of his firm for many years. The SEC filed emergency motions to freeze assets and appoint a receiver, and worked to return as much money as possible to harmed investors. In March 2009, the Commission charged the auditors of Madoff's broker-dealer firm with committing securities fraud by falsely representing that they had conducted legitimate audits. In June, the SEC charged a New York-based broker-dealer and four individuals with securities fraud, alleging that they collectively raised billions of dollars from investors for Madoff's Ponzi scheme. Additionally, the Commission charged Madoff's chief financial officer (CFO), Frank DiPascali, with securities fraud for overseeing the mechanics of Madoff's fictitious investment strategy and creating millions of phony documents and trading records to conceal the fraud from investors and regulators.

In August and September 2009, the SEC's Office of Inspector General (OIG) issued three reports on the Madoff fraud, including one entitled *Investigation of Failure of the SEC to Uncover Bernard Madoff's Ponzi Scheme.* The reports have been closely analyzed by the SEC. Even before the release of these reports, major efforts were underway—as discussed previously in this section—to make improvements and address the shortcomings that were identified in the reports, including insufficient expertise, training, experience, and supervision by management; inadequate internal communication and coordination among and within various SEC divisions; deficiencies in investigative planning and prioritization; failure to follow through on leads; and insufficient resources.

Credit Crisis-Related Cases

The SEC charged the former CEO of Countrywide Financial and two other former executives with fraud for allegedly misleading investors about the significant risks the company was undertaking. The SEC charged that Countrywide portrayed itself as underwriting mainly prime quality mortgages, while privately describing as "toxic" certain loans it was extending. The SEC's complaint also charged the former CEO with insider trading.

In other mortgage-related cases, the SEC brought actions against former mortgage-lending company executives alleging accounting fraud and making false and misleading disclosures relating to the risk of the mortgages originated and held by the company as the credit crisis began to unfold. The SEC sued registered representatives of a broker-dealer firm for allegedly making false statements in marketing investments in mortgage-backed securities as safe and suitable for retirees and others with conservative investment goals. The SEC also charged a registered investment adviser and its affiliate with overstating the value of a mutual fund that invested primarily in mortgage-backed securities and for selectively disclosing problems with the fund to favored investors, allowing them to bail out early to avoid losses.

In the matter of the Reserve Primary Fund, the SEC charged the managers of the $62 billion money market fund with allegedly failing to properly disclose to the fund board all material facts relating to the value of the fund's investments in Lehman Brothers, Inc. The Reserve Primary Fund net asset value per share fell below $1.00, or "broke the buck," caused in part by investments in Lehman-backed assets. Part of the basis for the SEC's action was to request a pro-rata distribution of assets so that shareholders could have their money distributed to them as quickly and equitably as possible.

Ponzi Schemes

The SEC investigates and prosecutes many Ponzi scheme cases each year both to prevent new victims from being harmed and to maximize the recovery of assets to investors. The majority of such cases are brought as emergency actions, which seek a temporary restraining order and an asset freeze. During FY 2009, the SEC filed a significantly higher number of enforcement actions involving Ponzi schemes or Ponzi-like payments compared to the previous year.

The Commission charged Robert Allen Stanford and his companies—Antiguan-based Stanford International Bank, Houston-based broker-dealer and investment adviser

Stanford Group Company, and investment adviser Stanford Capital Management—with allegedly conducting an $8 billion Ponzi scheme. The SEC also charged Leroy King, the administrator and CEO of Antigua's Financial Services Regulatory Commission, with allegedly accepting bribes to ignore the Stanford Ponzi scheme and supply Stanford with confidential information about the SEC's investigation.

Other Cases

As part of the more than $50 billion in auction rate securities (ARS) settlements for tens of thousands of investors, the SEC in February announced a settlement that would provide more than $7 billion in liquidity from Wachovia Securities, LLC to thousands of customers who invested in ARS before the market for those securities collapsed. Other ARS actions announced this year include settled charges against TD Ameritrade for making inaccurate statements when selling ARS to customers, and charges filed against broker-dealer Morgan Keegan & Company, Inc. for allegedly misleading thousands of investors about the liquidity risks associated with ARS.

Working with the New York State Attorney General, the SEC pursued New York's former Deputy Comptroller, a top political adviser, and others for allegedly extracting kickbacks from investment management firms seeking to manage the assets of New York's largest pension fund, the New York State Common Retirement Fund.

The SEC charged a former portfolio manager at hedge fund investment adviser Millennium Partners and a salesman at Deutsche Bank alleging insider trading in the CDS of international holding company VNU. In addition, the SEC filed a civil injunctive action late last year against four individuals for allegedly engaging in a fraudulent scheme to overvalue the commodity derivatives trading portfolio at Bank of Montreal and thereby inflate the bank's publicly reported financial results.

Among the cases of accounting fraud filed by the SEC this year, the Commission charged General Electric (GE) with using improper accounting methods to increase its reported earnings or revenues and avoid reporting negative financial results. The SEC also charged Terex Corporation with accounting fraud for making material misstatements in its financial reports to investors, as well as aiding and abetting a fraudulent accounting scheme at United Rentals, another public company.

Under authority provided by the Foreign Corrupt Practices Act (FCPA), the Commission this year filed a civil injunctive action charging Siemens AG (Siemens), a Munich, Germany-based manufacturer, with violations of the anti-bribery, books and records, and internal controls provisions of the FCPA. Siemens offered to pay $350 million in disgorgement to settle the SEC's charges. In total, the company agreed to $1.6 billion in combined sanctions to simultaneously settle actions brought by the U.S. Department of Justice, the Office of the Prosecutor General in Munich, and the SEC, which is the largest settlement in the history of the FCPA since it became law in 1977.

During FY 2009, the SEC filed numerous insider trading cases. In one case, the Commission charged a former Citigroup investment banker and seven others with allegedly engaging in a widespread insider trading scheme that involved repeated tips about upcoming merger deals. In another case, the SEC charged two mergers and acquisitions professionals at UBS Investment Bank and Blackstone Advisory Services, L.P. with allegedly tipping off five individuals, including a portfolio manager for a Jefferies Group, Inc. hedge fund, with material nonpublic information about three impending corporate acquisitions.

Disgorgement and Fair Funds

In the Fair Funds provision of the Sarbanes-Oxley Act, Congress granted the SEC increased authority to help harmed investors by allowing both ill-gotten gains and civil money penalties to be distributed to them directly. Previously, only ill-gotten gains could be distributed to investors. The SEC has already returned approximately $6.6 billion in Disgorgement and Fair Fund distributions to injured investors since the 2002 passage of the Sarbanes-Oxley Act. This important work continued in 2009, as the SEC distributed more than $2.1 billion to injured investors.

Investor Protection and Outreach

In 2009, the Commission launched a series of initiatives intended to strengthen investor protection.

The economic crisis has focused renewed attention on the accountability borne by boards of directors for the decisions they make. In May 2009, the Commission proposed a comprehensive series of rule amendments to facilitate the exercise by shareholders of their state law right to nominate directors to the corporate boards of the companies they own. The Commission is continuing to consider whether and how the federal proxy rules may be impeding the ability of shareholders to exercise their fundamental state law rights in this area.

In July 2009, the Commission acted on measures to better inform and empower investors to improve corporate governance and help restore investor confidence. Consistent with congressional legislation, the Commission proposed rules implementing the requirement that public companies receiving money from the Troubled Asset Relief Program provide a shareholder vote on executive pay in their proxy solicitations. The Commission proposed other significant proxy enhancements, including new disclosure requirements regarding board oversight of risk, and the relationship of compensation to risk. The Commission also approved a New York Stock Exchange (NYSE) rule change to prohibit brokers from voting proxies in corporate elections without instructions from their customers.

In May 2009, the Commission proposed rule amendments to substantially increase protections for investors who entrust their money to investment advisers. The proposals are intended to help ensure that investment advisers who have custody of clients' funds and securities are handling those assets properly. The additional safeguards proposed by the SEC would include a yearly "surprise exam" of investment advisers performed by an independent public accountant to verify client assets. In addition, when an adviser or an affiliate directly holds client assets, the adviser or the affiliate must obtain a written report including an opinion of the qualified custodian's controls relating to the custody of client assets from an accounting firm registered with and inspected by the Public Company Accounting Oversight Board (PCAOB). The proposed rule amendments are designed to strengthen custody requirements and enable independent public accountants to provide an additional check on the safeguards of the assets.

In September, the Commission proposed a rule amendment that would effectively prohibit the practice of "flashing" marketable orders. A flash order enables certain market participants with sophisticated trading technology the opportunity to interact with the order for a sub-second period of time before the public is given an opportunity to trade with those orders. The Commission is concerned, among other things, that flash orders may create a "two-tiered" market because only certain market participants can effectively access this valuable market information, as well as that they may erode public price discovery in the markets generally by reducing the incentive to display orders. The proposed amendment would effectively prohibit all markets, including equity exchanges, options exchanges, and alternative trading systems, from using marketable flash orders.

In October, the Commission proposed measures intended to address discrete issues related to liquidity. The growth of dark pools over the past few years has raised concerns that their lack of transparency could lead to a "two-tiered" market that deprives the public of information about stock prices and liquidity. Consequently, the proposals would require that certain information about an investor's interest in buying or selling a stock be made publicly available. In addition, the proposals would require real-time disclosure of the identity of the dark pool that executed the trade.

In addition, the Commission proposed measures intended to curtail "pay-to-play" practices by investment advisers that seek to manage money for state and local governments. The measures are designed to prevent an adviser from making political contributions or hidden payments to influence selection decisions by government officials.

In July, the Commission proposed amendments to SEC Rule 15c2-12 intended to help investors make more knowledgeable investment decisions regarding municipal securities, effectively manage and monitor their investments, and avoid fraud as well as assist broker-dealers in carrying out their responsibilities under the securities laws. Specifically, the proposed amendments would expand the Rule to cover additional municipal securities, improve disclosure of tax risk, strengthen and expand disclosure of important events, and establish a more specific filing deadline.

In order to give investors a greater voice in the SEC's work, the agency established an Investor Advisory Committee composed of prominent and highly respected members of the retail and institutional investor communities. The Committee has three subcommittees focusing on investor education, investor protection, and shareholder voting and corporate governance. The Committee is tasked with advising the Commission on matters of concern to investors in the securities markets and providing the Commission with information and recommendations regarding its regulatory programs from the point of view of investors.

Fair, Efficient, and Effective Markets

Transparency and Accountability at Nationally Recognized Statistical Rating Organizations (NRSROs)

In September 2009, the Commission took several rulemaking actions to bolster oversight of credit rating agencies by enhancing disclosure and improving the quality of credit ratings. The Commission adopted rules to provide greater information concerning ratings performance and requirements to enable competing credit rating agencies to offer unsolicited ratings for structured finance products, by granting them access to the necessary underlying data for structured products. The Commission also adopted amendments to its rules and forms to remove certain references to credit ratings issued by NRSROs.

Another proposal includes new rules that would require enhanced disclosure of information by issuers, including what a credit rating covers and any material limitations on the scope of the rating and whether any "preliminary ratings" were obtained from other rating agencies—in other words, whether there was "ratings shopping." The SEC also voted to seek public comment on whether to amend Commission rules to subject NRSROs to liability when a rating is used in connection with a registered offering. Other amendments proposed by the Commission would seek to strengthen compliance programs through requiring annual compliance reports and to enhance disclosure of potential sources of revenue-related conflicts.

Money Market Fund Regulation

In June 2009, the Commission proposed rule amendments that would significantly strengthen the regulatory framework for money market funds in order to increase their resilience in times of economic stress and reduce the risks of runs on the funds. The proposals would require money market funds to maintain a portion of their portfolios in highly liquid investments, reduce their exposure to long-term debt, and limit their investments to only the highest quality portfolio securities. The proposals also would require the monthly reporting of portfolio holdings, and permit the suspension of redemptions if a fund "breaks the buck" to allow for the orderly liquidation of fund assets.

Study of Fair Value Accounting

In December 2008, the Commission delivered a report to Congress mandated by the Emergency Economic Stabilization Act of 2008 that recommended against the suspension of fair value accounting standards. In the report, SEC staff recommended improvements to existing practice, including recommendations to continue to focus on the needs of investors in the development of accounting standards and recommendations to the Financial Accounting Standards Board and the International Accounting Standards Board to work together to simplify the accounting for financial instruments.

Among key findings, the staff noted that investors generally believe fair value accounting increases financial reporting transparency and facilitates better investment decision making. The staff also observed that fair value accounting did not appear to play a meaningful role in the bank failures that occurred in 2008. The staff indicated that bank failures in the United States appeared to be the result of growing probable credit losses, concerns about asset quality, and in certain cases, eroding lender and investor confidence.

Target Date Funds

In June 2009, the Commission and the U.S. Department of Labor (DOL) held a joint hearing examining target date funds, a popular investment vehicle for investors focused on retirement planning. Target date funds allocate their investments among various asset classes and automatically shift that allocation to more conservative investments as a target date for retirement approaches and thereafter. This shift in asset allocation, often referred to as a fund's "glide path," may differ significantly among funds with the same target date. Topics discussed at the joint hearing included issues related to how target date fund managers determine asset allocations and changes to asset allocations over the course of a fund's operation; how they select and monitor underlying investments; how the foregoing and related risks are disclosed to investors; the approaches or factors for comparing and evaluating target date funds; and the utilization of target date funds in defined contribution plans.

Mutual Fund Disclosure Reform

In January 2009, the Commission issued rule amendments to implement an improved mutual fund disclosure framework. The amendments require key information to appear in plain English in a standardized order at the front of the mutual fund prospectus. The amendments also permit a fund or underwriter to satisfy its prospectus delivery obligations by sending or giving a "summary prospectus" and providing the statutory prospectus and other information on an Internet Web site or, on request, in paper format.

SEC and CFTC Joint Meetings

In September 2009, the SEC and the CFTC hosted joint meetings to discuss harmonization of rules and oversight. The meetings solicited views from members of the investor community, academics, industry experts, and market participants on the current regulatory scheme, harmonization of the agencies' rules, and recommendations for changes to statutes and regulations. In October 2009, the agencies issued a joint report which includes 20 recommendations to enhance enforcement powers, strengthen market and intermediary oversight, and improve operational coordination.

Sarbanes-Oxley Study

In September 2009, the Commission completed a study on implementation of Section 404 of the Sarbanes-Oxley Act. Data were collected through an extensive survey of companies, along with supplemental outreach to investors and other users of financial statements, to evaluate the effectiveness and efficiency of Section 404 and related reforms before non-accelerated filers begin to comply with Section 404(b). The report documents how costs of compliance vary with company size and experience. Costs generally decreased after the Commission's 2007 release of Management Guidance and the PCAOB's adoption of a new audit standard (Auditing Standard 5), and that both companies and investors attribute improvements in the financial reporting processes to compliance with Section 404.

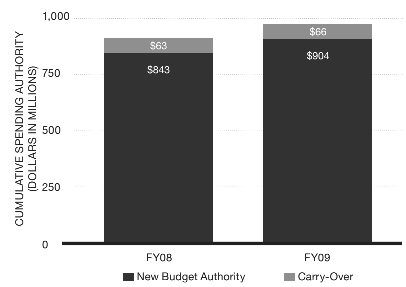
Financial and Performance Highlights

This section provides key financial and performance information for FY 2009. It summarizes the SEC's efforts to manage resources efficiently and responsibly while accomplishing the agency's mission.

In FY 2009, the SEC was authorized by Congress to spend $970 million, a 7 percent increase over the $906 million authorized in FY 2008. The funding included $894 million in offsetting collections, a $10 million two-year supplemental appropriation issued by Congress to use for investigating securities fraud, and $66 million of prior years' carry-over of unobligated balances and recoveries from prior year obligations. The SEC's spending authority by source is illustrated in *Chart 1.2, Spending Authority by Source.* Additional discussion can be found in *Note 1.R. Budgets and Budgetary Accounting* on page 73.

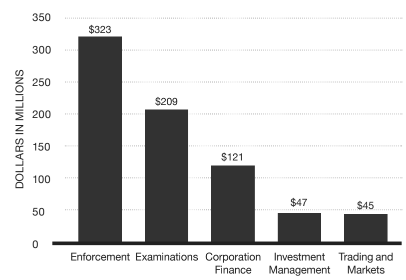
The SEC employed a total of 3,642 FTE in FY 2009. This represents an increase of 131 FTE over FY 2008. The increase in FTE from FY 2008 to FY 2009 is explained in part by a much lower attrition rate. The attrition rate for FY 2009 was 4 percent, down significantly from the FY 2008 rate of about 6 percent.

CHART 1.2
SPENDING AUTHORITY BY SOURCE



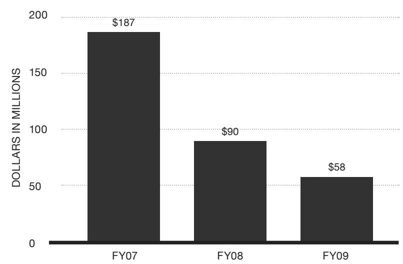
The agency devoted nearly 55 percent of its FY 2009 funding to the enforcement and examination programs, as shown in *Chart 1.3, Top Programs by Budget.*

CHART 1.3
TOP PROGRAMS BY BUDGET



Of the $960 million authority from offsetting collections, carry-over, and recoveries in FY 2009, approximately $958 million was obligated during the fiscal year. Rigorous oversight and management of budgetary resources are evidenced by the steady decrease in unobligated balances brought forward, as illustrated in *Chart 1.4, Unobligated Balance, Brought Forward.* As reported on the Statement of Budgetary Resources (SBR) on page 67, in FY 2009 there was a $32 million decrease on the Unobligated Balance Brought Forward, October 1 line and a $40 million decrease on the Unobligated Balance Not Available line. Additional discussion can be found in *Note 1.R. Budgets and Budgetary Accounting* on page 73.

CHART 1.4
UNOBLIGATED BALANCE, BROUGHT FORWARD

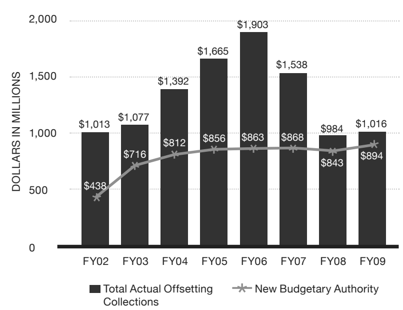


In order to meet the FY 2008 offsetting collections target set forth by the Investor and Capital Markets Fee Relief Act, the rates used to calculate the fees collected for securities transactions on the exchanges and certain over-the-counter markets were reduced. The lower fee rates were in effect throughout the first and second quarters of FY 2009 while the SEC operated under a continuing resolution. When the appropriations bill was signed on March 11, 2009, the SEC announced increases in the filing fee rate and the exchange transaction fee rate in order to reach the FY 2009 offsetting collections target. *Chart 1.5, Offsetting Collections vs. New Budget Authority,* presents the budget authority and offsetting collections from FY 2002 through FY 2009.

Despite a decrease in the volume of securities transactions on the exchanges between FY 2008 and FY 2009, a substantial rate increase to $25.70 per million in the third quarter of FY 2009 generated higher Exchange Revenues as seen on the Earned Revenue Not Attributed to Programs line of the Statement of Net Cost (SNC) on page 65 and the Spending Authority from Offsetting Collections Earned and Collected line of the SBR on page 67. While the SEC collected $32 million more in offsetting collections in FY 2009 as compared to FY 2008, the increased authority of the SEC resulted in a lower amount reported on the Temporarily not Available Pursuant to Public Law line of the SBR on page 67. The higher fee rate also contributed to an increase in accounts receivable reported on the Balance Sheet on page 64.

Additional discussion of the fees collected by the SEC can be found in *Note 1.Q. Revenue and Other Financing Sources* and *Note 14. Exchange Revenues.*

CHART 1.5
OFFSETTING COLLECTIONS VS. NEW BUDGET AUTHORITY



16 2009 PERFORMANCE AND ACCOUNTABILITY REPORT

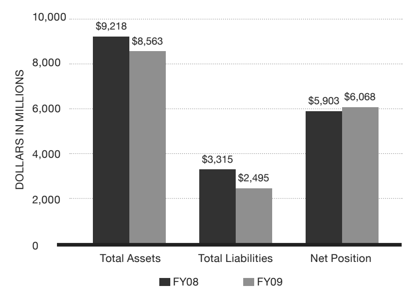
As of September 30, 2009, Total Assets decreased by $655 million compared to the FY 2008 ending balance, as illustrated in *Chart 1.6, Assets, Liabilities, and Net Position.* There was a corresponding decrease of $820 million in Total Liabilities and a $165 million increase in Net Position.

The decrease in Total Assets is largely attributable to the SEC's efforts to accelerate distributions to harmed investors, resulting in a $1 billion decrease in Investments. Significant distributions during the period of October 1, 2008 through September 30, 2009 were made to harmed investors in relation to cases involving Alliance Capital Management, Bear Stearns & Co., and Millennium Partners. There was a corresponding decrease of $811 million in the Liability for Disgorgement and Penalties. This was offset by a $206 million increase in disgorgement and penalties receivable largely as a result of the UBS AG and Real Estate Partners, Inc. cases and a higher collectability on receivables established in FY 2009.

The SEC also had a decrease in registrant deposit account balances compared to FY 2008 which contributed to the decrease in Total Liabilities. Registrant deposit accounts are maintained by the SEC for filers to facilitate the filing process. The funds are drawn down as filings are submitted and filers can replenish their deposit account as desired. The decrease is largely attributed to approximately $6.6 million from dormant accounts returned to the depositors and $4.3 million in drawdowns.

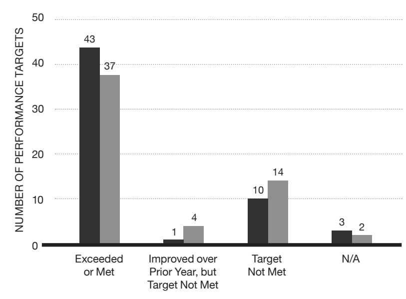
As illustrated on the Statement of Custodial Activity on page 68, the SEC had a large increase in custodial revenue in FY 2009, which was primarily the result of the following settlements: Siemens, a combined case with Halliburton and KBR for violating the FCPA, the E*Trade settlement for trading violations, and the GE case for accounting fraud. These cases totaled $611 million, accounting for 98 percent of the increase in custodial collections. The remaining 2 percent is related to collections from smaller cases. Additional disclosure of custodial revenues can be found in *Note 16. Custodial Revenues.*

CHART 1.6
ASSETS, LIABILITIES, AND NET POSITION



Due to sustained efforts of SEC staff, about 65 percent of the agency's performance targets were either met or exceeded in FY 2009, as illustrated in *Chart 1.7, Results by Performance Level.* Additional details related to the performance of SEC programs can be found in the *Performance Results Summary* on page 19 and the *Performance Section* beginning on page 27.

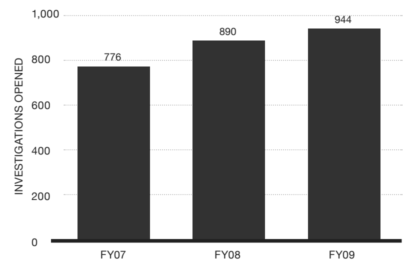
CHART 1.7
RESULTS BY PERFORMANCE LEVEL



In FY 2009, the Commission removed procedural barriers to the staff's investigative and litigation practices and eliminated a layer of management to put more investigators and attorneys on the front lines. Additionally, in order to keep pace with the complexity of market practices, the division created five national specialized investigative groups comprised of staff with practical trading, market, and other specialized skills. Staff assigned to these specialized units will receive training customized to reflect market developments and particular investigative challenges in those subject areas.

The Enforcement Division's efforts toward specialization and reducing process and administrative burdens in FY 2009 improved investigative planning and execution. In FY 2009, the SEC opened about 6 percent more investigations when compared to FY 2008 and about 22 percent more investigations when compared to FY 2007 *(Chart 1.8, Number of Investigations Opened).*

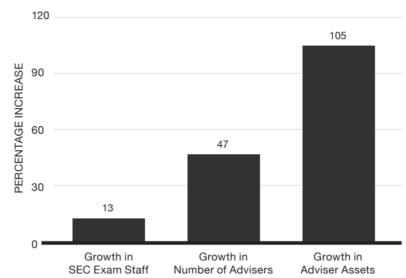
CHART 1.8
NUMBER OF INVESTIGATIONS OPENED



In FY 2009, OCIE instituted a number of significant reforms. In order to strengthen examination procedures and internal controls, OCIE began reviewing its written procedures and internal guidance to make sure it provides clear and consistent practices across the examination program. OCIE placed an emphasis on fraud detection in addition to the program's overall goal of identifying potential violations of specific securities laws and rules, and increased expertise through enhanced training and widespread participation in certified training programs.

In recent years, the number of registered advisers has increased by nearly 50 percent and the assets under management by these advisers have nearly doubled *(Chart 1.9, Percentage of Growth in SEC Adviser/Fund Exam Staff and Registered Advisers, FY03–FY09).* While OCIE staff has not increased proportionally, OCIE continues to target high-risk firms and activities as resources permit. During the past year, OCIE examined the operations, or some portion thereof, of nearly 10 percent of all registered advisers and 30 percent of all registered fund complexes.

CHART 1.9
PERCENTAGE OF GROWTH IN SEC ADVISER/FUND EXAM STAFF AND REGISTERED ADVISERS, FY03–FY09



Performance Results Summary

TABLE 1.1
PERFORMANCE RESULTS SUMMARY

In FY 2009, the SEC exceeded or met 37 planned performance targets out of 57 for the agency's 35 performance measures. Several of the performance measures are comprised of multiple planned performance targets. A comparison of the SEC's performance results for FY 2008 and FY 2009, organized by goal, is presented in this *Table 1.1.* A discussion of the agency's program achievements and detailed performance results is located in the *Performance Section.*

Key: Level of Performance Attained

Exceeded/Met	Performance target exceeded or met	Improved	Performance improved over prior year, but target not met	Indicator	Denotes an indicator; does not have performance targets
Not Met	Performance target not met	N/A	New performance measure in FY 2008, target was not set or data is not available		

Goal 1
ENFORCE COMPLIANCE WITH THE FEDERAL SECURITIES LAWS

	Performance FY 2008	Performance FY 2009
1. Percentage of firms receiving deficiency letters that stated they took or would take corrective action in response to all exam findings	Not Met	Improved
2. Percentage of advisers deemed "high risk" examined during the year	Exceeded/Met	Not Met
3. Percentage of registrant population examined during the year:		
Investment advisers	Exceeded/Met	Exceeded/Met
Investment companies	Exceeded/Met	Exceeded/Met
Broker-dealers (exams by SEC and SROs)	Exceeded/Met	Not Met
4. Percentage of (non-sweep) exams that are concluded within 120 days	Not Met	Not Met
5. Percentage of attendees at CCOutreach that rated the program as "Useful" or "Extremely Useful" in their compliance efforts	Exceeded/Met	Not Met
6. Percentage of exams with "significant" findings	Indicator	Indicator
7. Percentage of first enforcement cases filed within two years	Exceeded/Met	Exceeded/Met
8. Maintaining an effective distribution of cases across core enforcement areas	Exceeded/Met	Exceeded/Met
9. Percentage of enforcement cases successfully resolved	Exceeded/Met	Exceeded/Met
10. Percentage of debts where either a payment has been made, or a collection activity has been initiated within six months of the due date of the debt	Exceeded/Met	Exceeded/Met
11. Percentage of Fair Funds and disgorgement dollars designated for distribution that are distributed to investors within 12 months	N/A	N/A
12. Volume of enforcement activity: investigations opened, cases filed, and investigations closed	Indicator	Indicator
13. Assets frozen abroad in SEC cases through coordination with foreign regulators	Indicator	Indicator

Goal 2
PROMOTE HEALTHY CAPITAL MARKETS THROUGH AN EFFECTIVE AND FLEXIBLE REGULATORY ENVIRONMENT

	FY 2008	FY 2009
14. Percentage of SRO rule filings closed in less than 60 days from filing	Exceeded/Met	Exceeded/Met
15. Average daily share volume (in billions of shares) on the NYSE and Nasdaq exchanges:		
NYSE	Not Met	Exceeded/Met
Nasdaq	Exceeded/Met	Not Met
16. Percentage of transaction dollars settled on time each year	Exceeded/Met	Exceeded/Met
17. Percentage of market outages at SROs and ECNs that are corrected within targeted timeframes:		
Within 2 hours	Exceeded/Met	Exceeded/Met
Within 4 hours	Exceeded/Met	Exceeded/Met
Within 24 hours	Exceeded/Met	Exceeded/Met
18. Equity portfolio holdings of U.S. investment companies as a percentage of total U.S. stock market capitalization	Exceeded/Met	Exceeded/Met
19. Number of new foreign private issuers and dollar amount of registered securities	Indicator	Indicator

TABLE 1.1
PERFORMANCE RESULTS SUMMARY *(continued)*

Goal 2 *(continued)* PROMOTE HEALTHY CAPITAL MARKETS THROUGH AN EFFECTIVE AND FLEXIBLE REGULATORY ENVIRONMENT	Performance FY 2008	FY 2009
20. Percentage of regulated entities representing a single point of failure that meet the continuity of operations standards of the White Paper, the Policy Statement, and the Automated Review Program:		
White Paper analysis	Exceeded/Met	Exceeded/Met
Policy Statement analysis	Not Met	Not Met
21. Timeliness of SEC responses to written no-action letter, exemptive applications, and interpretive requests:		
Trading and Markets: No-action letter, exemptive, and interpretive requests (combined figure)	Not Met	Exceeded/Met
Investment Management: No-action letter and interpretive requests	Exceeded/Met	Exceeded/Met
Investment Management: Exemptive applications	Exceeded/Met	Exceeded/Met
Corporation Finance: No-action letter and interpretive requests	Not Met	Improved
Corporation Finance: Shareholder proposals	Exceeded/Met	Exceeded/Met
22. Percentage of U.S. households owning mutual fund shares	Exceeded/Met	Exceeded/Met
23. Percentage of U.S. households investing in the securities market either through direct share ownership or ownership of mutual funds	Not Met	N/A
24. Mutual fund share of total retirement assets	Exceeded/Met	Exceeded/Met

Goal 3 FOSTER INFORMED INVESTMENT DECISION MAKING	FY 2008	FY 2009
25. Percentage of Exchange Act reporting companies reviewed by the SEC:		
Corporations	Exceeded/Met	Exceeded/Met
Investment company portfolios	Exceeded/Met	Exceeded/Met
26. Average time to issue initial comments on Securities Act filings	Exceeded/Met	Exceeded/Met
27. Percentage of investment company disclosure reviews for which initial comments are completed within timeliness goals:		
Initial registration statements	Exceeded/Met	Exceeded/Met
Post-effective amendments	Exceeded/Met	Exceeded/Met
Preliminary proxy statements	Exceeded/Met	Exceeded/Met
28. Percentage of forms and submissions filed electronically and in a structured format:		
Forms: Total percentage in electronic format	Exceeded/Met	Not Met
Filings received: Total percentage in electronic format	Exceeded/Met	Exceeded/Met
29. Number of searches for filings on www.sec.gov	Not Met	Exceeded/Met
30. Demand for investor education information, and average cost per thousand investors reached:		
Total number of investors reached (in millions, with Web visits)	N/A	Exceeded/Met
Average cost per thousand investors reached (with Web visits)	N/A	Exceeded/Met
31. Percentage of investor complaints and inquiries completed within 7 and 30 business days:		
Closed within 7 days	Exceeded/Met	Not Met
Closed within 30 days	Exceeded/Met	Not Met
32. Investor assistance and public information telephone inquiries:		
Investor assistance	Exceeded/Met	Not Met
Public information	Exceeded/Met	Not Met
33. Responses to Freedom of Information Act requests	Exceeded/Met	Exceeded/Met

TABLE 1.1
PERFORMANCE RESULTS SUMMARY *(continued)*

Goal 4 MAXIMIZE THE USE OF SEC RESOURCES	Performance FY 2008	Performance FY 2009
34. Staff turnover rate	Exceeded/Met	Exceeded/Met
35. Maintain a top five ranking among the Best Places to Work in Government	Exceeded/Met	Not Met
36. Percentage of the time that www.sec.gov and EDGAR are operable:		
www.sec.gov	Exceeded/Met	Exceeded/Met
EDGAR	Exceeded/Met	Exceeded/Met
37. Number of OIG and GAO information security-related recommendations outstanding for more than 18 months:		
GAO recommendations	Improved	Improved
OIG recommendations	Exceeded/Met	Exceeded/Met
38. Percentage of major systems that have been certified and accredited, and given a privacy impact assessment, within required timeframes:		
Major systems certified and accredited	Not Met	Exceeded/Met
Major systems with privacy impact assessment completed	Not Met	Improved
39. Financial audit results:		
Unqualified opinion	Exceeded/Met	Exceeded/Met
Material weaknesses	Exceeded/Met	Not Met
Significant deficiency	Exceeded/Met	Not Met

Chairman's Assurance Statement

The management of the SEC is responsible for establishing and maintaining effective internal control and financial management systems that meet the objectives of the Federal Managers' Financial Integrity Act of 1982 (FMFIA). Internal control is an integral component of the agency's management that provides reasonable assurance that the following objectives are being achieved: effectiveness and efficiency of operations, reliability of financial reporting, and compliance with laws and regulations. The SEC is able to provide a qualified statement of assurance that the internal controls and financial management systems meet the objectives of FMFIA, with the exception of a material weakness resulting from an aggregation of significant deficiencies related to information systems and related financial reporting controls.

The SEC conducted its evaluation of internal control over the effectiveness and efficiency of operations and compliance with applicable laws and regulations in accordance with the Office of Management and Budget (OMB) Circular No. A-123, *Management's Responsibility for Internal Control.* Based on the results of this evaluation, the SEC identified a material weakness resulting from an aggregation of significant deficiencies related to information systems security and controls and related financial reporting controls. Other than the exception noted, the internal controls were operating effectively and no other material weaknesses were found in the design or operation of the internal control over the effectiveness and efficiency of operations and compliance with applicable laws and regulations as of September 30, 2009.

The SEC'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 (GAAP), and assets are safeguarded against loss from unauthorized acquisition, use, or disposition; and (2) transactions are executed in accordance with the laws governing the use of budget authority and other laws and regulations that could have a direct and material effect on the financial statements.

SEC management is responsible for establishing and maintaining effective internal control over financial reporting. SEC management evaluated the effectiveness of the SEC's internal control over financial reporting as of September 30, 2009, based on the criteria established under the FMFIA. Based on the results of this evaluation, the SEC identified a material weakness resulting from an aggregation of significant deficiencies related to information systems and related financial reporting controls. Because of this material weakness, SEC management concludes that the agency's internal controls over financial reporting were not effective as of September 30, 2009.

Mary L. Schapiro

Mary Schapiro
Chairman
November 16, 2009

Management Assurances

Federal Managers' Financial Integrity Act

The FMFIA is implemented by OMB Circular No. A-123, revised, *Management's Responsibility for Internal Control.*

Section 2 of the FMFIA requires federal agencies to report, on the basis of annual assessments, any material weaknesses that have been identified in connection with its internal and administrative controls. The reviews that took place during FY 2009 provide qualified assurance that SEC systems and management controls comply with the requirements of the FMFIA, with the exception of a material weakness in internal control over information systems and related financial reporting controls.

Section 4 of the FMFIA requires that agencies annually evaluate and report on whether financial management systems conform to government-wide requirements. The SEC evaluated its financial management systems for the fiscal year ending September 30, 2009, in accordance with the Federal Financial Management Improvement Act of 1996 (FFMIA) and OMB Circular No. A-127, *Financial Management Systems,* as applicable.

The SEC conducted its annual assessment of the effectiveness of internal control in accordance with the requirements of OMB Circular No. A-123. The agency completed the Internal Control Evaluation Checklist, which was based on the *GAO-01-1008G Internal Control Management and Evaluation Tool,* to evaluate controls and structure the support for providing assurance. In accordance with guidance issued by the SEC's Office of the Executive Director and the Office of the Chief Financial Officer, 33 directors and office heads conducted reviews of their financial, administrative, and program management controls in FY 2009. This process ensures comprehensive coverage of SEC offices.

Each director and office head provided an assurance statement identifying management challenges. These statements were based on information gathered from various sources, including, among other things:

- Management's personal knowledge gained from the daily operation of the office;
- Internal management reviews, self-assessments, and tests of internal controls;
- Completion of the Internal Control Evaluation Checklist;
- Government Accountability Office (GAO) and OIG reports;
- Annual performance plans and reports;
- Reports and other information from Congress or OMB; and
- Additional reviews relating to the office's operations, including those discussed in the *Other Reviews* section below.

Each year, the agency's Financial Management Oversight Committee (FMOC) evaluates the FMFIA Section 2 and 4 submissions, recommendations from OIG, and other supplemental sources of information. Based on this review, the FMOC advises the Chairman as to whether the SEC had any internal control or system design deficiencies serious enough to be reported as a material weakness or non-conformance.

Review of Internal Control Over Financial Reporting

Management reviewed internal control over financial reporting from a top-down, risk-based approach. Material financial statement line items and business processes relevant to the line items were mapped to the relevant controls. The following elements were documented in this risk and control matrix for each business process area: high-level key risks; financial reporting assertions; safeguarding of assets and compliance with laws and regulations; control objectives and activity; key and secondary controls; and frequency of controls.

Other Reviews

Also during the year, the Office of Information Technology (OIT) in conjunction with system owners, completed certification and accreditation activities for 20 reportable systems in FY 2009. As a result, the SEC has now certified and accredited a total of 50 reportable systems in accordance with the appropriate guidance from OMB and the National Institute of Standards and Technology. OIT also completed contingency testing on the majority of the SEC's accredited systems in conjunction with several of its disaster recovery exercises.

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

Status of Internal Control Over Financial Reporting

During the SEC's assessment of the effectiveness of its internal controls, management identified six significant deficiencies, which in the aggregate were deemed to represent a material weakness over information systems and related financial controls. The audit standards for federal agencies established by GAO define "material weakness" as a significant control deficiency or aggregation of deficiencies that result in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected. Although none of the significant deficiencies identified were determined to present a risk of a material misstatement individually, the SEC considered the combination of the following control deficiencies to collectively constitute a material weakness:

- **Information security and control:** The SEC has not fully implemented adequate controls to ensure integrity and reliability of the data within its financial systems and financial sub-processes. Management assessment of control deficiencies identified weaknesses in system security: access control, segregation of duties, and configuration management.
- **Financial reporting processes:** Due to limitations of its financial systems, the SEC is heavily dependent on manual processes that are inherently inefficient and more susceptible to human error, increasing the possibility that controls will not be effective. Lack of integration between several automated systems requires extensive compensating controls and labor-intensive accounting procedures, which complicates review of financial data and increases the risk of error.
- **Accounting for budgetary resources:** Software problems identified in the general ledger system required making adjusting journal entries that elevate the risk of misstatement. Additionally, insufficient documentation was provided of authorization of downward adjustments to obligations.
- **Risk assessment and monitoring process:** The SEC's formal process to evaluate the effectiveness of its internal control environment, implemented for the first time this year, was not as comprehensive as it should be with respect to identification of risk or evaluation of the adequacy of controls.
- **Liability for registrant deposits:** The SEC identified design deficiencies in the sub-system that maintains information related to registrant deposits and filing fee revenue. These deficiencies impede a correct accounting of a registrant's deposits across multiple filing types, resulting in the need to implement manual controls. After review this year, the controls designed to compensate for system deficiencies were not deemed effective.
- **Reconciliation of Fund Balance with Treasury:** Certain reconciliations were not performed consistently and differences were not resolved, or documented, in a timely manner.

Corrective Action Planned

The SEC has already begun to develop a remediation plan; some deficiencies are likely to be resolved during the first half of FY 2010, while others—which have been the result of long-term and growing constraints affecting our information technology and human resources—will take longer to fully resolve. Moving toward the full integration of core and subsidiary financial systems will be a critical component of the corrective action to be taken in the coming year. The agency will move forward on the design and implementation of improvements to financial and mixed systems to address lack of automated control. The design deficiencies in SEC systems used to record filing fee revenue and manage registrant deposits will be of particular focus.

Action will also be taken to tighten controls and improve functionality and efficiency in existing financial system components. The remediation plan will include actions to improve access control, segregation of duties, and configuration management. The SEC has begun the process of defining security roles in the core financial system and developing implementation guidelines for separating incompatible functions to ensure proper segregation of duties and monitoring. Early in FY 2010, the SEC will revisit the configuration management issues relative to database logging or otherwise providing an audit trail of security events within the core financial system to ensure that only authorized changes are made to production.

The SEC also intends to significantly enhance its risk assessment and control monitoring processes. The agency expects to retain an independent outside expert to assist in this important endeavor.

Financial Management System Conformance

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

The process used by the SEC changed significantly this year due to the January 9, 2009, revision of OMB Circular A-127, including a new FFMIA risk model, which ranks risks from nominal to significant. Although the circular's revision is not effective until October 1, 2009, early implementation was encouraged, and the SEC has elected to implement the new requirements in FY 2009. Based on the results of the review, the SEC can provide qualified assurance that its financial management systems substantially conform with federal financial management system requirements except for the internal control finding reported under Section 2 of FMFIA discussed above.

Federal Information Security Management Act (FISMA)

FISMA requires federal agencies to conduct annual assessments of their information technology security and privacy programs, to develop and implement remediation efforts for identified weaknesses and vulnerabilities, and to report compliance to OMB. As of this writing, the SEC's Inspector General (IG), Chief Information Officer, and Privacy Officer are performing a joint review of the agency's compliance with FISMA requirements during 2009, and will submit the report to OMB on November 18, 2009, as required.

During the year, additional steps were taken to enhance the overall information security and privacy programs at the SEC, including additional reviews at regional offices, as well as improving policies and procedures related to information management; conducting a privacy review of 20 new systems, for a total 60 systems; and revising several privacy-related policies and procedures in accordance with requirements to reflect the importance of protecting personally identifiable information. The agency strengthened a range of technical, management, and operational controls by deploying a new intrusion detection system; redesigning and implementing new infrastructure; reviewing system access and audit logs; improving change management policies and procedures; and enhancing database security features.

Limitations of the Financial Statements

The principal financial statements included in this report have been prepared to report the financial position and results of operations of the SEC, pursuant to the requirements of 31 U.S.C. 3515(b). While the statements have been prepared from the books and records of the SEC in accordance with GAAP for federal entities and the formats prescribed by OMB, the statements are in addition to the financial reports used to monitor and control budgetary resources, which are prepared from the same books and records. The statements should be read with the understanding that they are for a component of the U.S. Government, a sovereign entity.

Financial Statements

Financial Section

This section of the Performance and Accountability Report contains the Agency's financial statements, required supplementary information and related Independent Auditor's Report, as well as other information on the Agency's financial management. Information presented here satisfies the reporting requirements of OMB Circular A-136, *Financial Reporting Requirements,* as well as the Accountability of Tax Dollars Act of 2002.

The first portion of this section contains Principal Financial Statements. The statements provide a comparison of FY 2009 and FY 2008 data. The SEC prepares the following required financial statements:

- Balance Sheet—presents, as of a specific time, amounts of future economic benefits owned or managed by the reporting entity exclusive of items subject to stewardship reporting (assets), amounts owed by the entity (liabilities), and amounts which comprise the difference (net position).
- Statement of Net Cost—presents the gross cost incurred by the reporting entity less any exchange revenue earned from its activities. The SEC also prepares a Statement of Net Cost by Goal to provide cost information at the strategic goal level.
- Statement of Changes in Net Position—reports the change in net position during the reporting period. Net position is affected by changes to Cumulative Results of Operations.
- Statement of Budgetary Resources—provides information about how budgetary resources were made available as well as their status at the end of the period.
- Statement of Custodial Activity—reports collection of non-exchange revenue for the General Fund of the Treasury. The SEC, as the collecting entity, does not recognize these collections as revenue. Rather, the Agency accounts for sources and disposition of the collections as custodial activities on this statement.

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

The accompanying *Notes to Financial Statements* provide a description of significant accounting policies as well as detailed information on select statement lines. These notes and the principal statements are audited by the GAO.

Message from the Chief Financial Officer

Kristine M. Chadwick
CHIEF FINANCIAL OFFICER AND ASSOCIATE EXECUTIVE DIRECTOR

I am pleased to join Chairman Schapiro in presenting the SEC's FY 2009 Performance and Accountability Report, which provides information relative to the SEC's budgetary integrity, operating performance, stewardship, and systems and control. In a year marked by market turmoil and far-reaching changes, I am grateful for the dedicated SEC staff who worked diligently to ensure accountability for financial resources and the results of the SEC's programs and activities.

In 2009, the SEC once again received an unqualified audit opinion on its financial statements. Over the past year, the SEC successfully addressed 21 of the 43 security weaknesses in information system controls identified by GAO, as well as 36 of the 43 financial recommendations that were open as of the end of the FY 2008 financial statement audit. Nevertheless, this year GAO found repeat conditions in the area of information security and control and accounting for budgetary resources, as well as significant deficiencies in the areas of financial reporting, internal control risk assessment and monitoring processes, and liability for registrant deposits. In the aggregate, these significant deficiencies were determined to represent a material weakness in internal control over information system security and related financial controls. This determination prevents the SEC from reporting full compliance with federal financial systems requirements. These results were disappointing as improving internal control has been, and continues to be, one of our highest priorities. Nonetheless, these findings will spur us on to further strengthen our financial performance. The SEC has already begun to develop a remediation plan; some deficiencies are likely to be resolved during the first half of FY 2010, while others—which have been the result of long-term and growing constraints affecting our information technology and human resources—will take longer to fully resolve.

Our actions during the past year, and anticipated action over the coming year, are summarized below.

- In FY 2010, the SEC will continue to execute our long-term strategy to achieve fully automated integration of financial systems in order to address deficiencies caused by manual integration of systems supporting material balances.
- The SEC undertook several initiatives in FY 2009 that improved the SEC's budgetary accounting control. However, GAO identified the same types of problems in the SEC's accounting for budgetary activities as were reported in the prior year. The SEC will strive to improve discipline in this area in the short term, and the implementation of an integrated procurement system planned for 2010 will provide preventative control.
- In the short term, the weakness related to registrant deposits will be addressed by dedicated staffing assigned to resolve the backlog of aged balances pending review and analysis. Underlying the problem are issues related to the aging EDGAR systems, which are currently under consideration and will be addressed in the forthcoming plan of action.

- In FY 2010, the SEC will move to implement a more robust internal control risk assessment and monitoring process. Increased oversight over treasury and cash management functions, including reconciliation processes, will be supported by structural realignment within the Office of Financial Management expected in the first half of FY 2010.
- Actions taken over the past year resulted in the resolution of the significant deficiency previously found in property and equipment controls.

I look forward to further financial management improvements in FY 2010 to increase the efficiency, transparency, and accountability of the SEC's financial systems and operations.

Sincerely,

Kristine M. Chadwick
Chief Financial Officer and
Associate Executive Director, Finance
November 16, 2009

U.S. SECURITIES AND EXCHANGE COMMISSION

Balance Sheet

As of September 30, 2009 and 2008

(DOLLARS IN THOUSANDS)	FY 2009	FY 2008
ASSETS (Note 2):		
Intragovernmental:		
Fund Balance with Treasury (Note 3)	$6,083,307	$6,011,310
Investments, Net (Notes 4 and 12)	1,959,611	2,982,542
Accounts Receivable (Note 5)	188	45
Advances and Prepayments	2,284	3,936
Total Intragovernmental	8,045,390	8,997,833
Accounts Receivable, Net (Note 5)	434,033	135,470
Advances and Prepayments	1,273	1,032
Property and Equipment, Net (Note 6)	82,435	84,007
Total Assets	$8,563,131	$9,218,342
LIABILITIES (Note 7):		
Intragovernmental:		
Accounts Payable	$ 9,080	$ 15,588
Employee Benefits	5,213	4,433
Unfunded FECA and Unemployment Liability	1,441	1,340
Custodial Liability (Note 16)	4	2
Liability for Non-Entity Assets	1	—
Other	157	—
Total Intragovernmental	15,896	21,363
Accounts Payable	34,084	39,122
Accrued Payroll and Benefits	27,131	22,970
Accrued Leave	42,696	38,829
Registrant Deposits	40,898	51,793
Actuarial FECA Liability (Note 8)	6,178	5,604
Liability for Disgorgement and Penalties (Notes 12 and 18)	2,297,741	3,108,367
Contingent Liabilities (Note 11.B)	9,500	—
Other Accrued Liabilities (Note 9)	20,922	27,005
Total Liabilities	2,495,046	3,315,053
Commitments and Contingencies (Note 11)		
NET POSITION (Note 12):		
Unexpended Appropriations—Other Funds	9,860	—
Cumulative Results of Operations—Earmarked Funds	6,058,225	5,903,289
Total Net Position	$6,068,085	$5,903,289
Total Liabilities and Net Position	$8,563,131	$9,218,342

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

U.S. SECURITIES AND EXCHANGE COMMISSION

Statement of Net Cost

For the years ended September 30, 2009 and 2008

(DOLLARS IN THOUSANDS)	FY 2009	FY 2008
COSTS BY STRATEGIC GOAL (Note 13)		
Enforce compliance with federal securities laws		
Total Gross Cost	$ 615,414	$595,327
Promote healthy capital markets through an effective and flexible regulatory environment		
Total Gross Cost	93,716	102,822
Foster informed investment decision making		
Total Gross Cost	168,436	133,487
Maximize the use of SEC resources		
Total Gross Cost	103,399	99,267
Total Entity		
Total Gross Program Cost	980,965	930,903
Less: Earned Revenue Not Attributed to Programs (Note 14)	1,109,891	956,317
Net (Income) from Operations (Note 17)	$ (128,926)	$ (25,414)

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

U.S. SECURITIES AND EXCHANGE COMMISSION

Statement of Changes in Net Position

For the years ended September 30, 2009 and 2008

	FY 2009		
(DOLLARS IN THOUSANDS)	**Earmarked Funds**	**All Other Funds**	**Consolidated Total**
CUMULATIVE RESULTS OF OPERATIONS:			
Beginning Balances	$5,903,289	$ —	$5,903,289
Budgetary Financing Sources:			
Appropriations Used	—	140	140
Other Financing Sources:			
Imputed Financing (Note 10)	25,955	—	25,955
Other	—	(85)	(85)
Total Financing Sources	25,955	55	26,010
Net Income (Cost) from Operations	128,981	(55)	128,926
Net Change	154,936	—	154,936
Cumulative Results of Operations (Note 12)	6,058,225	—	6,058,225
UNEXPENDED APPROPRIATIONS:			
Budgetary Financing Sources:			
Appropriations Received	—	10,000	10,000
Appropriations Used	—	(140)	(140)
Total Unexpended Appropriations	—	9,860	9,860
Net Position, End of Period	$6,058,225	$ 9,860	$6,068,085

	FY 2008		
(DOLLARS IN THOUSANDS)	**Earmarked Funds**	**All Other Funds**	**Consolidated Total**
CUMULATIVE RESULTS OF OPERATIONS:			
Beginning Balances	$5,853,768	$ —	$5,853,768
Budgetary Financing Sources:			
Appropriations Used	—	—	—
Other Financing Sources:			
Imputed Financing (Note 10)	24,107	—	24,107
Other	—	—	—
Total Financing Sources	24,107	—	24,107
Net Income (Cost) from Operations	25,414	—	25,414
Net Change	49,521	—	49,521
Cumulative Results of Operations (Note 12)	5,903,289	—	5,903,289
UNEXPENDED APPROPRIATIONS:			
Budgetary Financing Sources:			
Appropriations Received	—	—	—
Appropriations Used	—	—	—
Total Unexpended Appropriations	—	—	—
Net Position, End of Period	$5,903,289	$ —	$5,903,289

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

U.S. SECURITIES AND EXCHANGE COMMISSION

Statement of Budgetary Resources

For the years ended September 30, 2009 and 2008

(DOLLARS IN THOUSANDS)	FY 2009	FY 2008
BUDGETARY RESOURCES:		
Unobligated Balance, Brought Forward, October 1	$ 57,696	$ 90,012
Recoveries of Prior Year Unpaid Obligations	28,982	38,384
Budget Authority:		
Appropriation	10,000	—
Spending Authority from Offsetting Collections:		
Earned		
Collected	1,017,763	985,997
Change in Receivables from Federal Sources	143	45
Change in Unfilled Customer		
Advance Received	157	—
Without Advance from Federal Sources	1	122
Subtotal	1,028,064	986,164
Temporarily not Available Pursuant to Public Law	(122,101)	(141,039)
Total Budgetary Resources	$ 992,641	$ 973,521
STATUS OF BUDGETARY RESOURCES:		
Obligations Incurred:		
Direct (Note 15)	$ 964,640	$ 915,422
Reimbursable (Note 15)	1,236	403
Subtotal	965,876	915,825
Unobligated Balance Available:		
Realized and Apportioned for Current Period	9,968	687
Unobligated Balance Not Available	16,797	57,009
Total Status of Budgetary Resources	$ 992,641	$ 973,521
CHANGE IN OBLIGATED BALANCE:		
Obligated Balance, Net		
Unpaid Obligations, Brought Forward, October 1	$ 250,974	$ 254,660
Uncollected Customer Payments from Federal Sources, Brought Forward, October 1	(167)	—
Total Unpaid Obligated Balance, Net	250,807	254,660
Obligations Incurred Net	965,876	915,825
Gross Outlays	(951,469)	(881,127)
Recoveries of Prior Year Unpaid, Obligations Actual	(28,982)	(38,384)
Change in Uncollected Customer Payments from Federal Sources	(144)	(167)
Obligated Balance, Net, End of Period		
Unpaid Obligations	236,399	250,974
Uncollected Customer Payments from Federal Sources	(311)	(167)
Total, Unpaid Obligated Balance, Net, End of Period (Note 11)	$ 236,088	$ 250,807
NET OUTLAYS:		
Net Outlays:		
Gross Outlays	$ 951,469	$ 881,127
Offsetting Collections	(1,017,920)	(985,997)
Distributed Offsetting Receipts	(702)	(3,779)
Net Outlays/(Collections)	$ (67,153)	$(108,649)

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

U.S. SECURITIES AND EXCHANGE COMMISSION

Statement of Custodial Activity

For the years ended September 30, 2009 and 2008

(DOLLARS IN THOUSANDS)	FY 2009	FY 2008
REVENUE ACTIVITY:		
Sources of Cash Collections:		
Disgorgement and Penalties (Note 18)	$815,802	$192,958
Other	10	111
Net Collections	815,812	193,069
Accrual Adjustments	4	(2)
Total Custodial Revenue (Note 16)	815,816	193,067
DISPOSITION OF COLLECTIONS:		
Amounts Transferred to:		
Department of the Treasury	815,812	193,069
Change in Liability Accounts	4	(2)
Total Disposition of Collections	815,816	193,067
NET CUSTODIAL ACTIVITY	$ —	$ —

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

Notes to Financial Statements

As of September 30, 2009 and 2008

NOTE 1. Summary of Significant Accounting Policies

A. Reporting Entity

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

The agency's programs protect investors and promote the public interest by fostering and promoting compliance with the federal securities laws; establishing an effective regulatory environment that promotes high-quality disclosure, prevents abusive practice by market participants, and provides for fair, efficient, transparent, and competitive capital formation and innovation; and facilitating access to information that investors need to make informed investment decisions.

B. Basis of Presentation and Accounting

The accompanying financial statements present the financial position, net cost of operations, changes in net position, budgetary resources, and custodial activities of the SEC's core business activities as required by the Accountability of Tax Dollars Act of 2002. The statements may differ from other financial reports submitted pursuant to the OMB directives for the purpose of monitoring and controlling the use of the SEC budgetary resources. The SEC's books and records serve as the source of the information presented in the accompanying financial statements. The agency classified 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 earned revenues are collections or accruals due from other federal entities. Intragovernmental costs are payments or accruals due to other federal entities.

The SEC's financial statements have been prepared on the accrual basis of accounting in conformity with GAAP for the federal government. 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 from which the SBR is prepared. The differences relate primarily to the capitalization and depreciation of property and equipment, as well as the recognition of other long-term assets and liabilities. The statements were also prepared in conformity with OMB Circular No. A-136, *Financial Reporting Requirements.*

C. Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities. These estimates and assumptions include the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results may differ from those estimates. Estimates are also used in the allocation of costs to the SEC strategic goals presented in the SNC.

D. Intra- and Inter-Agency Relationships

The SEC is comprised of a single federal bureau. Therefore, the current organizational structure does not give rise to the need for intra-entity eliminations.

E. Fund Accounting Structure

The SEC accounts for financial activities by Treasury Appropriation Fund Symbol (TAFS), summarized as follows:

- General Fund—Salaries and Expenses (0100 and X0100) consist of earmarked funds for use in carrying out the SEC's mission and functions and revenues collected by the SEC in excess of appropriated funds for FY 2004 (0100) and FY

2005 through FY 2009 (X0100). In addition to these TAFS, the SEC received a supplemental appropriation of $10 million for use in FY 2009 and FY 2010; the supplemental appropriation will be accounted for in TAFS 09/10 0100 and is not earmarked. (Refer to *Note 1.F. Earmarked Funds, Note 3. Fund Balance with Treasury,* and *Note 12. Earmarked, Other, Disgorgement and Penalties, and Non-Entity Funds).*

Other Funds:

- Deposit and Suspense Funds (F3875, X6561, and X6563) carry 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.
- Miscellaneous Receipt Accounts (1099 and 3220) hold non-entity receipts and accounts receivable from custodial activities that the SEC cannot deposit into funds under its control. These accounts include receipts, pursuant to SEC enforcement actions, that will be sent to the Treasury.

The SEC does not have lending or borrowing authority, except as discussed in *Note 11. Commitments and Contingencies.* The SEC has custodial responsibilities, as disclosed in *Note 16. Custodial Revenues.*

F. Earmarked Funds

Earmarked funds are financed by specifically identified revenues, often supplemented by other financing sources, which remain available over time. The SEC collects such funds, which statutes require the SEC to use for designated activities, benefits, or purposes; and to account for them separately from the government's general revenues. The SEC accounts for these as offsetting collections and deposits amounts collected in TAFS 0100, Salaries and Expenses as detailed in *Note 12. Earmarked, Other, Disgorgement and Penalties, and Non-Entity Funds.*

G. Entity/Non-Entity Assets

Assets that an agency is authorized to use in its operations are entity assets. Assets that an agency holds on behalf of another federal agency or a third party and are not available for the agency's use are non-entity assets. The SEC's non-entity assets include the following: (i) disgorgement, penalties, and interest collected or to be collected and held or invested by the SEC pending distribution to harmed investors (disgorgement funds); (ii) accounts receivable in respect to Freedom of Information Act (FOIA) fees; and (iii) excess filing fees remitted by registrants (registrant deposits).

H. Fund Balance with Treasury

Fund Balance with Treasury (FBWT) includes certain funds held on behalf of third parties. These include registrant deposits and uninvested disgorgement funds. FBWT also includes undisbursed account balances with Treasury and balances in excess of appropriated amounts that are unavailable to the SEC. The SEC conducts all of its banking activity in accordance with directives issued by Treasury's Financial Management Service (FMS). The SEC deposits all revenue and receipts in commercial bank accounts maintained by the FMS, or wires them directly to a Federal Reserve Bank. Treasury processes all disbursements made by the SEC. The Federal Reserve Bank transfers all monies maintained in commercial bank accounts on the business day following the day of deposit.

I. Investments

The SEC invests disgorgement funds in short-term Treasury securities, whenever practicable. Disgorgement funds may also include civil penalties collected under the "Fair Fund" provision of the Sarbanes-Oxley Act of 2002. As the funds are collected, the SEC holds them in a deposit fund account and may invest them in overnight and short-term market-based Treasury bills through a facility provided by the Bureau of the Public Debt, pending their distribution to investors. The SEC adds interest earned to the funds and these funds are subject to taxation under Treasury Regulation section 1.468B-2. Additional details regarding SEC investments are provided in *Note 4. Investments, Net.*

J. Accounts Receivable and Allowance for Uncollectible Accounts

Both SEC's entity and non-entity accounts receivable consist primarily of amounts due from the public. Entity accounts receivable are amounts that the SEC will retain upon collection. These generally include claims arising from: (i) securities transaction fees paid by exchanges, (ii) filing fees paid by registrants, (iii) goods or services that the SEC has provided to another federal agency pursuant to an inter-agency agreement, (iv) host reimbursement of employee travel, and (v) employee-related debt. Entity accounts receivable represent a small volume of the SEC's business activities because agency fee legislation generally requires payment of filing fees at the time of filing, and SRO 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 by the SROs to the SEC for activity during the month of September.

Non-entity accounts receivable are amounts that the SEC will not retain upon collection. These mainly include disgorgement, penalties, and interest assessments. The SEC recognizes these accounts receivable when an order of the Commission or a court designates it to collect the assessed disgorgement, penalties, and interest. The SEC does not recognize interest as accounts receivable, unless specified by the court or an administrative order.

The SEC is also party to court orders directing violators of federal securities laws to pay the court or a receiver to collect the disgorgement, penalties, and interest assessed against them. These orders are not recognized as accounts receivable by the SEC because the debts are payable to another party. However, these debts are subject to change based on, for example, future orders issued by the presiding court that could result in the SEC recognizing a receivable. In the cases where the court order or other legally binding instrument requires the debtor to remit funds to the SEC, a receivable is recorded.

The SEC uses a two-tiered methodology to calculate the allowance for loss on accounts receivable. Previously, the SEC identified the 25 largest disgorgement and penalty receivable balances and made an individual collection assessment for each of these cases. For disgorgement and penalty receivable balances that fell below the "Top 25" threshold, the SEC applied an overall allowance percentage calculated from historical data to estimate uncollectible balances.

For the year ended September 30, 2009, the SEC enhanced the criteria used to determine accounts subject to an individual collectability assessment. Rather than using a "Top 25" population, which provided coverage over the portfolio ranging from 79 percent to 86 percent, the SEC used a specified 90 percent coverage threshold. In regard to the group of accounts that comprise the remainder of the portfolio, the SEC applied a rate based on a recent study of historical collection data. The SEC considers this to be a change in accounting estimate and will account for these changes on a prospective basis.

The SEC bases the allowance for uncollectible amounts and the related provision for estimated losses for filing fees and other accounts receivable on analysis of historical collection data. No allowance for uncollectible amounts or related provision for estimated losses have been established for fees payable by SROs, as these gross accounts receivable are deemed to represent their net realizable value based on historical experience.

K. Advances and Prepayments

The SEC may prepay amounts in anticipation of receiving future benefits such as training and supplemental health benefits for the SEC employees. The agency expenses these payments when the goods are received or services are performed. The SEC also may advance funds to its personnel for travel costs. The SEC expenses these amounts when the expense voucher is processed.

L. Property and Equipment, Net

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

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

M. Liabilities

The SEC records liabilities for amounts that are likely to be paid as a result of events that have occurred as of the relevant balance sheet dates. The SEC's liabilities consist of routine operating accounts payable, accrued payroll and benefits, registrant deposit accounts, liabilities for disgorgement and penalties, and custodial liabilities for amounts held on behalf of Treasury.

Liability for disgorgement and penalties represents the largest portion of the SEC's 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, which may be returned to harmed investors. When the Commission or court issues an order, the SEC establishes an account receivable due to the SEC. When collected, the SEC holds receipts in FBWT or invests in Treasury securities pending distribution to harmed investors. The SEC reports an equal and offsetting liability for assets held at Treasury as a non-entity liability on the balance sheet.

The SEC recognizes liabilities covered by three types of resources: realized budgetary resources, unrealized budgetary resources that become available without further congressional action, and amounts held that do not require the use of budgetary resources. Realized budgetary resources include obligated balances that fund existing liabilities and unobligated balances as of the relevant balance sheet dates. Unrealized budgetary resources represent fee collections in excess of amounts appropriated for current fiscal year spending. The SEC uses these resources to cover liabilities when appropriation language makes these unrealized budgetary resources available in the fiscal year without further congressional action.

N. Employee Retirement Systems and Benefits

The SEC's employees may participate in either the Civil Service Retirement System (CSRS) or the Federal Employees Retirement System (FERS), depending on when they started working for the federal government. Pursuant to Public Law 99-335, FERS and Social Security automatically cover most employees hired after December 31, 1983. Employees who are rehired after a break in service of more than one year and who had five years of federal civilian service prior to 1987 are eligible to participate in the CSRS offset retirement system or may elect to join FERS.

The SEC does not report CSRS or FERS assets or accumulated plan benefits that may be applicable to its employees in its financial statements. The U.S. Office of Personnel Management reports them. Although the SEC reports no liability for future payments to employees under these programs, the federal government is liable for future payments to employees through the various agencies administering these programs. The SEC does not fund post-retirement benefits such as the Federal Employees Health Benefit Program and the Federal Employees Group Life Insurance Program. The SEC is also not required to fully fund CSRS pension liabilities. Instead, the financial statements of the SEC recognize an imputed financing source and corresponding expense that represent the SEC's share of the cost to the federal government of providing pension, post-retirement health, and life insurance benefits to all eligible SEC employees. 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. The SEC contributes a matching amount to the Social Security Administration under the Federal Insurance Contributions Act, which fully covers FERS participating employees. Employees participating in CSRS do not receive matching contributions to their TSP.

O. Injury and Post-employment Compensation

The Federal Employees' Compensation Act (FECA), administered by the DOL, addresses all claims brought by SEC employees for on-the-job injuries. The DOL bills each agency annually as its claims are paid, but payment on these bills is deferred for two years to allow for funding through the budget process. Similarly, employees that the SEC terminates without cause may receive unemployment compensation benefits under the unemployment insurance program also administered by the DOL, which bills each agency quarterly for paid claims.

P. Annual, Sick, and Other Leave

The SEC accrues annual leave and compensatory time as earned and reduces the accrual when leave is taken. Each month, the SEC makes an adjustment so that the balances in the accrued leave accounts reflect current leave balances and pay rates. No portion of this liability has been obligated. Future financing sources provide funding to the extent that current or prior year funding is not available to pay for leave earned but not taken. The SEC expenses sick leave and other types of non-vested leave as used.

Q. Revenue and Other Financing Sources

The SEC's revenue and financing sources include exchange revenues, which are generated from arm's-length transactions, and non-exchange revenues, which arise from the government's ability to demand payment. The SEC's exchange revenue mainly consists of collections from security transaction fees. The SEC's non-exchange revenue consists of amounts collected in enforcement proceedings from violators of securities laws, as described below.

The SEC's funding is primarily through the collection of securities transaction fees from SROs and securities registration, tender offer, merger, and other fees from registrants. The fee rates are 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. When received, the SEC records these fees as exchange revenue. The SEC is permitted by law to include these amounts in its obligational authority or to offset its expenditures and liabilities upon collection, up to authorized limits. The SEC records all amounts remitted by registrants in excess of the fees for specific filings as liabilities in deposit accounts until earned by the SEC from registrant filings or returned to the registrant pursuant to the SEC's policy, which calls for the return of registrant deposits when an account is dormant for six months.

The SEC also receives collections from proceedings that result in the assessment of disgorgement, penalties, and interest against violators of federal securities laws. When the SEC collects these funds, it transfers the funds to a SEC deposit account at Treasury. The disgorged funds may be later returned to injured investors or paid to a SEC receipt account or returned to the general fund of the Treasury. Non-exchange revenue is recognized by the SEC when the funds are moved to a receipt account, and once those funds are transferred, they are reported in the SCA. The SEC does not record amounts collected and held by another government entity, such as a court registry, or a non-government entity, such as a receiver.

R. Budgets and Budgetary Accounting

The SEC is subject to certain restrictions on its use of statutory fees. The SEC deposits all fee revenues in a designated account at Treasury. However, the SEC may use funds from this account only as authorized by Congress, made available by OMB apportionment, and upon issuance of a Treasury warrant. Revenue collected in excess of appropriated amounts is restricted for use by the SEC.

The SEC can use fees other than the restricted excess fees from its operations, subject to an annual congressional limitation, which were $894.4 million and $842.7 million for the budget FY 2009 and FY 2008, respectively. In addition, Congress made available approximately $65.6 million and $63 million for FY 2009 and FY 2008, respectively. Funds appropriated that the SEC does not use in a given fiscal year are maintained in a designated account for use in future periods in accordance with the appropriation requirements. Previously mentioned in *Note 1.E. Fund Accounting Structure,* the SEC received a supplemental appropriation for $10 million from the general fund of the Treasury for use in FY 2009 and FY 2010. Unlike the annual appropriation, the supplemental funds are not offset by fees collected by the SEC.

Each fiscal year, the SEC receives Category A apportionments, which are quarterly distributions of budgetary resources made by OMB. The SEC also receives a small amount of Category B funds for reimbursable activity, which are exempt from quarterly apportionment.

S. Disgorgement and Penalties

The SEC maintains non-entity assets related to disgorgements and penalties ordered pursuant to civil injunctive and administrative proceedings and which, upon collection and further order, the SEC may distribute to harmed investors. The SEC also recognizes an equal and offsetting liability for these assets as discussed in *Note 1.M. Liabilities.*

These assets consist of disgorgement, penalties, and interest assessed against securities law violators where the Commission, administrative law judge, or in some cases, a court, has determined that the SEC should return such funds to harmed investors. The SEC holds such funds as non-entity assets pending distribution to harmed investors pursuant to an approved distribution plan. The SEC does not record on its financial statements any asset amounts another government entity such as a court, or a non-governmental entity, such as a receiver, has collected or will collect. Additional details regarding disgorgement and penalties are presented in *Note 12. Earmarked, Other, Disgorgement and Penalties, and Non-Entity Funds* and *Note 18. Disgorgement and Penalties.*

NOTE 2. Non-Entity Assets

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

(DOLLARS IN THOUSANDS)	FY 2009	FY 2008
Intragovernmental		
Fund Balance with Treasury:		
Registrant Deposits	$ 40,898	$ 51,793
Disgorgement and Penalties (Note 18)	43,622	37,707
Investments, Net:		
Disgorgement and Penalties (Note 18)	1,959,611	2,982,542
Total Intragovernmental Non-Entity Assets	2,044,131	3,072,042
Accounts Receivable, Net:		
Disgorgement and Penalties (Note 18)	294,508	88,118
Custodial	4	2
Other Non-Entity Assets	1	—
Total Non-Entity Assets	2,338,644	3,160,162
Total Entity Assets	6,224,487	6,058,180
Total Assets (Note 12)	$8,563,131	$9,218,342

NOTE 3. Fund Balance with Treasury

FBWT by type of fund as of September 30, are as follows:

(DOLLARS IN THOUSANDS)	FY 2009	FY 2008
Fund Balances:		
General Funds	$5,998,787	$5,921,810
Other Funds	84,520	89,500
Total Fund Balance with Treasury	6,083,307	6,011,310
Status of Fund Balance with Treasury:		
Unobligated Balance		
Available	9,968	687
Unavailable	16,797	57,009
Obligated Balance not yet Disbursed	236,088	250,807
Non-Budgetary Fund Balance with Treasury	5,820,454	5,702,807
Total Fund Balance with Treasury	$6,083,307	$6,011,310

NOTE 4. Investments, Net

The SEC invests funds in overnight and short-term market-based Treasury bills. Treasury bills are securities traded in the primary and secondary U.S. Treasury markets. Originally, the U.S. government auctions Treasury bills directly in the primary U.S. Treasury market and subsequently investors trade them in the secondary U.S. Treasury market. In accordance with GAAP, the SEC records the value of its investments in Treasury bills at cost and amortizes the discount on a straight-line basis through the maturity date of these securities. The market value is determined by the secondary U.S. Treasury market and represents the value an individual investor is willing to pay for these securities, at a given point in time.

At September 30, 2009, investments consisted of the following:

(DOLLARS IN THOUSANDS)	Cost	Amortization Method	Amortized (Premium) Discount	Investment Net	Market Value Disclosure
Non-Marketable Market Based Securities	$1,959,163	S/L	$448	$1,959,611	$1,959,810

At September 30, 2008, investments consisted of the following:

(DOLLARS IN THOUSANDS)	Cost	Amortization Method	Amortized (Premium) Discount	Investment Net	Market Value Disclosure
Non-Marketable Market Based Securities	$2,976,912	S/L	$5,630	$2,982,542	$2,988,672

NOTE 5. Accounts Receivable, Net

At September 30, 2009, accounts receivable consisted of the following:

(DOLLARS IN THOUSANDS)	Gross Receivables	Allowance	Net Receivables
Intragovernmental Entity Accounts Receivable:			
Reimbursable Activity	$ 188	$ —	$ 188
Subtotal Intragovernmental Accounts Receivable	188	—	188
Entity Accounts Receivable:			
Exchange Fees	138,654	—	138,654
Filing Fees	720	116	604
Other	283	21	262
Non-Entity Accounts Receivable:			
Disgorgement and Penalties (Note 18)	713,851	419,343	294,508
Other	7	2	5
Subtotal Non-Intragovernmental Accounts Receivable	853,515	419,482	434,033
Total Accounts Receivable	$853,703	$419,482	$434,221

At September 30, 2008, accounts receivable consisted of the following:

(DOLLARS IN THOUSANDS)	Gross Receivables	Allowance	Net Receivables
Intragovernmental Entity Accounts Receivable:			
Reimbursable Activity	$ 45	$ —	$ 45
Subtotal Intragovernmental Accounts Receivable	45	—	45
Entity Accounts Receivable:			
Exchange Fees	46,480	—	46,480
Filing Fees	569	66	503
Other	368	1	367
Non-Entity Accounts Receivable:			
Disgorgement and Penalties (Note 18)	434,193	346,075	88,118
Other	2	—	2
Subtotal Non-Intragovernmental Accounts Receivable	481,612	346,142	135,470
Total Accounts Receivable	$481,657	$346,142	$135,515

The SEC writes off receivables aged two or more years by removing the debt amounts from the gross accounts receivable and any related allowance for uncollectible accounts. For the year ended September 30, 2009, the SEC enhanced the criteria used to estimate the allowance for loss on disgorgement and penalties accounts receivable. Refer to *Note 1.J. Accounts Receivable and Allowance for Uncollectible Accounts* for methods used to estimate allowances.

NOTE 6. Property and Equipment, Net

At September 30, 2009, 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	Book Value
Furniture and Equipment	S/L	$ 15	$ 50	3–5	$ 57,399	$ 43,358	$14,041
Software	S/L	300	300	3–5	85,145	67,737	17,408
Leasehold Improvements	S/L	300	N/A	10	80,891	29,905	50,986
Total					$223,435	$141,000	$82,435

At September 30, 2008, 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	Book Value
Furniture and Equipment	S/L	$ 15	$ 50	3-5	$ 60,844	$ 50,534	$10,310
Software	S/L	300	300	3–5	76,069	57,046	19,023
Leasehold Improvements	S/L	300	N/A	10	76,700	22,026	54,674
Total					$213,613	$129,606	$84,007

NOTE 7. Liabilities Not Covered by Budgetary Resources

The SEC's liabilities include amounts that will not require the use of budgetary resources. These liabilities consist of registrant deposit accounts; accounts receivable for disgorgement, penalties, and interest assessed against securities laws violators; and invested and uninvested assets held by the SEC on behalf of harmed investors.

At September 30, liabilities consisted of the following:

(DOLLARS IN THOUSANDS)	FY 2009	FY 2008
Liabilities Not Covered by Budgetary Resources		
Intragovernmental		
Unfunded FECA and Unemployment Liability	$ 1,441	$ 1,340
Total Intragovernmental Liabilities	1,441	1,340
Accrued Leave	42,696	38,829
Actuarial Liability	6,178	5,604
Contingent Liability	9,500	—
Other Accrued Liabilities—Recognition of Lease Liability (Note 9)	12,513	15,768
Total Liabilities Not Covered by Budgetary Resources	72,328	61,541
Liabilities Not Requiring Budgetary Resources		
Intragovernmental		
Custodial Liability	4	2
Liability for Non-Entity Assets	1	—
Total Intragovernmental Liabilities	5	2
Registrant Deposits	40,898	51,793
Liability for Disgorgement and Penalties	2,297,741	3,108,367
Total Liabilities Not Requiring Budgetary Resources	2,338,644	3,160,162
Liabilities Covered by Budgetary Resources		
Intragovernmental		
Accounts Payable	9,080	15,588
Employee Benefits	5,213	4,433
Other	157	—
Total Intragovernmental Liabilities	14,450	20,021
Accounts Payable	34,084	39,122
Accrued Payroll and Benefits	27,131	22,970
Other Accrued Liabilities	8,409	11,237
Total Liabilities Covered by Budgetary Resources	84,074	93,350
Total Liabilities	$2,495,046	$3,315,053

NOTE 8. Actuarial FECA Liability

FECA 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. Claims incurred for benefits under FECA for the SEC's employees are administered by the DOL and ultimately paid by the SEC when funding becomes available.

The SEC bases its estimate for FECA actuarial liability on the DOL's FECA model. The model considers the average amount of benefit payments incurred by the SEC for the past three fiscal years, multiplied by the medical and compensation liability to benefits paid (LBP) ratio for the whole FECA program. The SEC uses the overall average percentages of the LBP ratios summarized in the table below.

For FY 2009, the LBP ratios were as follows:

LBP Category	Medical	Compensation
Highest	9.90%	12.20%
Overall Average	9.30%	11.00%
Lowest	8.40%	10.10%

For FY 2008, the LBP ratios were as follows:

LBP Category	Medical	Compensation
Highest	9.30%	12.50%
Overall Average	8.00%	11.70%
Lowest	7.10%	11.40%

For FY 2009 and FY 2008, the SEC used the overall average LBP ratios to calculate the $6.2 million and $5.6 million FECA actuarial liabilities for those years, respectively.

NOTE 9. Leases

The SEC has the authority to negotiate long-term leases for office space. At September 30, 2009, the SEC leased office space at 16 locations under operating lease agreements that expire between FY 2010 and FY 2021. The SEC paid $82.8 million and $83.0 million for rent for FY 2009 and FY 2008, respectively. In FY 2008, the SEC signed supplemental lease agreements that led to an increase in future lease payments. Under existing commitments, minimum lease payments through FY 2015 and thereafter are as follows:

Fiscal Year *(DOLLARS IN THOUSANDS)*	Minimum Lease Payments
2010	$ 77,534
2011	77,551
2012	68,288
2013	60,563
2014	58,846
2015 and thereafter	287,580
Total Future Minimum Lease Payments	$630,362

The total future minimum lease payments summarized includes a continuing liability, until March 31, 2012, for space leased during FY 2005 in New York. To facilitate surrender of the SEC lease obligations for the previously occupied space, the SEC and U.S. General Services Administration (GSA) entered into separate agreements with the lessor of that space whereby GSA agreed to rent the office space for the next five years of the SEC's lease, with an option to renew for an additional five years which would, unless terminated early, overlap the remaining 17 months of the SEC's lease. As part of the SEC's agreement with the previous lessor, the SEC was responsible for the estimated $18 million difference between its annual lease liability and the annual lease liability negotiated by GSA with that lessor. The GSA exercised the 5 year renewal option in July 2009, so as of September 30, 2009, the SEC is responsible for 13 more months covered by the GSA original lease and then less than two additional years, at a reduced rate, through March 31, 2012; this liability amounts to $6.4 million of lease payments that end in FY 2012. Required lease payments through FY 2012 are as follows:

Fiscal Year *(DOLLARS IN THOUSANDS)*	Required Lease Payments New York
2010	$2,722
2011	2,469
2012	1,192
Total Future Estimated Lease Payments	$6,383

In addition to the lease liability above, during FY 2005, the SEC moved into temporary office space in New York due to renovations in the new leased office space. This temporary space was being provided to the SEC for only the lessor's operating costs, and therefore the SEC did not make rent payments for the New York office for five months of the fiscal year. The SEC attributed rent expense on a straight-line basis over the life of the new lease and recorded rent expense and an unfunded liability estimated at $8 million in FY 2005 and FY 2006. Since FY 2006, the SEC has recorded a reduction in the unfunded lease liability in the amount of $1.9 million and currently has a remaining balance of $6.1 million. The yearly future amortization amounts are shown in the table below. Refer to *Note 7. Liabilities Not Covered by Budgetary Resources.*

Fiscal Year (DOLLARS IN THOUSANDS)	Future Amortization Amounts
2010	$ 533
2011	533
2012	533
2013	533
2014	533
2015 and thereafter	3,465
Total Future Amortization Amounts	$6,130

NOTE 10. Imputed Financing

The SEC recognizes an imputed financing source and corresponding expense to represent its share of the cost to the federal government of providing pension and post-retirement health and life insurance benefits (Pension/Other Retirements Benefits) to all eligible SEC employees. For September 30, 2009 and 2008, the total amount of imputed financing amounted to approximately $26 million and $24 million, respectively.

NOTE 11. Commitments and Contingencies

A. Commitments

The Securities Investor Protection Act of 1970 (SIPA), as amended, created the Securities Investor Protection Corporation (SIPC) to provide certain financial protections to customers of insolvent registered securities brokers, dealers, firms, and members of national securities exchanges for up to $500,000 per customer. SIPA authorizes the SIPC to create a fund to maintain all monies received and disbursed by the SIPC. SIPA also gives the SIPC the authority to borrow funds from the SEC in an amount not to exceed, in the aggregate, $1 billion in the event that the SIPC Fund is or may appear insufficient for purposes of SIPA. For this to occur, 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. The Treasury would make these funds available to the SEC through the purchase of notes or other obligating instruments issued by the SEC. Such notes or other obligating instruments would bear interest at a rate determined by the Secretary of the Treasury. As of September 30, 2009, 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 amounts of customer property and customer claims in the Bernard L. Madoff Investment Securities LLC and Lehman Brothers Inc. liquidations, the current size of the SIPC Fund and the SIPC's ongoing assessments on brokers would provide sufficient funds to cover payments relating to the Madoff and Lehman matters. However, depending on other losses or claims, SIPC may determine that it needs to seek a loan from the Commission.

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, 2009, net obligations for all of the SEC's activities were $236.1 million, of which $83.6 million was delivered and unpaid. As of September 30, 2008, net obligations for all of SEC's activities were $250.8 million, of which $93.5 million was delivered and unpaid.

B. Contingencies

The SEC recognizes contingent liabilities when a past event or exchange transaction has occurred, a future outflow or other sacrifice of resources is probable, and the future outflow or sacrifice of resources is measurable. The SEC is party to various routine administrative proceedings, legal actions, and claims brought against it, including threatened or pending litigation involving labor relations claims, some of which may ultimately result in settlements or decisions against the federal government. As of September 30, 2009, the SEC has accrued $500,000 for claims of this type. In the prior fiscal year, there were no contingencies which required an accrual.

In a separate legal issue, on June 12, 2009, the Court of Appeals affirmed the decision of the Federal Labor Relations Authority (FLRA) and upheld the award on *SEC v. FLRA,* No. 08-1256, 08-1294 (D.C.Cir.). This matter involves a complaint filed by the National Treasury Employees Union (NTEU) before FLRA. No specific amount was claimed by the NTEU. As of September 30, 2009, the SEC has estimated a range of $9 million to $12 million for this award liability. In accordance with the Statement of Federal Financial Accounting Standards (SFFAS) 5, *Accounting for Liabilities of the Federal Government,* the SEC accrued the minimum amount in the range, $9 million for FY 2009, because no amount in the estimated range is considered more probable than any other amount within the range.

NOTE 12. Earmarked, Other, Disgorgement and Penalties, and Non-Entity Funds

The SEC's earmarked funds arise from offsetting collections from securities transaction fees, registration fees, and other fees authorized by the Securities Act and the Exchange Act. As such, the SEC identified and separately displayed activity in this fund on the Statement of Changes in Net Position (SCNP) and the Balance Sheet in accordance with the provisions of SFFAS 27, *Identifying and Reporting Earmarked Funds. Note 1.F. Earmarked Funds* displays additional details regarding the SEC's earmarked funds.

As discussed in *Note 1.E. Fund Accounting Structure,* the SEC received supplemental appropriations for use in FY 2009 and FY 2010. These funds are not earmarked and are presented under Other Entity Funds. For FY 2009, the assets, liabilities, net position, and net income from operations relating to earmarked, other, disgorgement and penalties, and non-entity funds consisted of the following:

(DOLLARS IN THOUSANDS)	Earmarked	Other Entity Funds	Disgorgement and Penalties	Non-Entity Funds	Total
Balance Sheet as of September 30, 2009					
ASSETS					
Fund Balance with Treasury	$5,988,927	$ 9,860	$ 43,622	$40,898	$6,083,307
Investments, Net	—	—	1,959,611	—	1,959,611
Accounts Receivable, Net	139,708	—	294,508	5	434,221
Advances and Prepayments	3,557	—	—	—	3,557
Property and Equipment, Net	82,435	—	—	—	82,435
Total Assets (Note 2)	$6,214,627	$ 9,860	$2,297,741	$40,903	$8,563,131
LIABILITIES					
Accounts Payable	$ 43,164	$ —	$ —	$ —	$ 43,164
Accrued Payroll and Benefits	32,344	—	—	—	32,344
FECA and Unemployment Liability	7,619	—	—	—	7,619
Accrued Leave	42,696	—	—	—	42,696
Custodial Liability	—	—	—	4	4
Liability for Non-Entity Assets	—	—	—	1	1
Registrant Deposits	—	—	—	40,898	40,898
Liability for Disgorgement and Penalties	—	—	2,297,741	—	2,297,741
Contingent Liabilities	9,500	—	—	—	9,500
Other Accrued Liabilities	20,922	—	—	—	20,922
Other	157	—	—	—	157
Total Liabilities (Note 7)	$ 156,402	$ —	$2,297,741	$40,903	$2,495,046
NET POSITION					
Unexpended Appropriations	$ —	$ 9,860	$ —	$ —	$ 9,860
Cumulative Results of Operations	6,058,225	—	—	—	6,058,225
Total Net Position	6,058,225	9,860	—	—	6,068,085
Total Liabilities and Net Position	$6,214,627	$ 9,860	$2,297,741	$40,903	$8,563,131

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(DOLLARS IN THOUSANDS)	Earmarked	Other Entity Funds	Disgorgement and Penalties	Non-Entity Funds	Total
Statement of Net Cost					
For the Year Ended September 30, 2009					
Gross Program Costs	$ 980,825	$ 140	$ —	$ —	$ 980,965
Less Earned Revenues Not					
Attributable to Program Costs	1,109,806	—	—	85	1,109,891
Net (Income) Cost from Operations	$ (128,981)	$ 140	$ —	$ (85)	$ (128,926)
Statement of Changes in Net Position					
For the Year Ended September 30, 2009					
Net Position Beginning of Period	$5,903,289	$ —	$ —	$ —	$5,903,289
Appropriations Used	—	140	—	—	140
Imputed Financing	25,955	—	—	—	25,955
Other	—	—	—	(85)	(85)
Net Income (Cost) from Operations	128,981	(140)	—	85	128,926
Net Change	154,936	—	—	—	154,936
Cumulative Results of Operations	6,058,225	—	—	—	6,058,225
Unexpended Appropriations					
Appropriations Received	—	10,000	—	—	10,000
Appropriations Used	—	(140)	—	—	(140)
Total Unexpended Appropriations	—	9,860	—	—	9,860
Net Position End of Period	$6,058,225	$ 9,860	$ —	$ —	$6,068,085

For FY 2008, the assets, liabilities, net position, and net income from operations relating to earmarked, other, disgorgement and penalties, and non-entity funds consisted of the following:

(DOLLARS IN THOUSANDS)	Earmarked	Other Entity Funds	Disgorgement and Penalties	Non-Entity Funds	Total
Balance Sheet as of September 30, 2008					
ASSETS					
Fund Balance with Treasury	$5,921,810	$ —	$ 37,707	$51,793	$6,011,310
Investments, Net	—	—	2,982,542	—	2,982,542
Accounts Receivable, Net	47,395	—	88,118	2	135,515
Advances and Prepayments	4,968	—	—	—	4,968
Property and Equipment, Net	84,007	—	—	—	84,007
Total Assets (Note 2)	$6,058,180	$ —	$3,108,367	$51,795	$9,218,342
LIABILITIES					
Accounts Payable	$ 54,710	$ —	$ —	$ —	$ 54,710
Accrued Payroll and Benefits	27,403	—	—	—	27,403
FECA and Unemployment Liability	6,944	—	—	—	6,944
Accrued Leave	38,829	—	—	—	38,829
Custodial Liability	—	—	—	2	2
Liability for Non-Entity Assets	—	—	—	—	—
Registrant Deposits	—	—	—	51,793	51,793
Liability for Disgorgement and Penalties	—	—	3,108,367	—	3,108,367
Contingent Liabilities	—	—	—	—	—
Other Accrued Liabilities	27,005	—	—	—	27,005
Other	—	—	—	—	—
Total Liabilities (Note 7)	$ 154,891	$ —	$3,108,367	$51,795	$3,315,053
NET POSITION					
Unexpended Appropriations	$ —	$ —	$ —	$ —	$ —
Cumulative Results of Operations	5,903,289	—	—	—	5,903,289
Total Net Position	5,903,289	—	—	—	5,903,289
Total Liabilities and Net Position	$6,058,180	$ —	$3,108,367	$51,795	$9,218,342
Statement of Net Cost					
For the Year Ended September 30, 2008					
Gross Program Costs	$ 930,903	$ —	$ —	$ —	$ 930,903
Less Earned Revenues Not Attributable to Program Costs	956,317	—	—	—	956,317
Net (Income) Cost from Operations	$ (25,414)	$ —	$ —	$ —	$ (25,414)

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(DOLLARS IN THOUSANDS)	Earmarked	Other Entity Funds	Disgorgement and Penalties	Non-Entity Funds	Total
Statement of Changes in Net Position					
For the Year Ended September 30, 2008					
Net Position Beginning of Period	$5,853,768	$ —	$ —	$ —	$5,853,768
Appropriations Used	—	—	—	—	—
Imputed Financing	24,107	—	—	—	24,107
Other	—	—	—	—	—
Net Income (Cost) from Operations	25,414	—	—	—	25,414
Net Change	49,521	—	—	—	49,521
Cumulative Results of Operations	5,903,289	—	—	—	5,903,289
Unexpended Appropriations					
Appropriations Received	—	—	—	—	—
Appropriations Used	—	—	—	—	—
Total Unexpended Appropriations	—	—	—	—	—
Net Position End of Period	$5,903,289	$ —	$ —	$ —	$5,903,289

NOTE 13. Intragovernmental Costs and Exchange Revenue

At the beginning of the fiscal year, each SEC reporting unit provides a percentage allocation analysis associating their activities to the SEC's strategic outcomes. The SEC strives to achieve outcomes which are identified in the Strategic Plan and tied to the SEC's four strategic goals. An Activity Based Costing (ABC) model is programmed to allocate costs based on these reported percentages. The ABC model is updated during the year as a reporting unit's activity allocations are reevaluated due to changes in mission activities. The ABC model identifies costs to each outcome and then accumulates these costs by the appropriate strategic goal in the SNC.

The SEC assigned all costs incurred for FY 2009 and FY 2008 to specific goals described in the agency's Strategic Plan, but exchange revenue is not directly assignable to a specific goal and is presented in total. Total intragovernmental and public costs for the fiscal years ended September 30, 2009 and 2008, are summarized below.

Program Goals *(DOLLARS IN THOUSANDS)*	**FY 2009**	**FY 2008**
Enforce Compliance with Federal Securities Laws		
Intragovernmental Costs	$ 103,899	$116,189
Public Costs	511,515	479,138
Subtotal—Enforce Compliance with Federal Securities Laws	615,414	595,327
Promote Healthy Capital Markets through an Effective and Flexible Regulatory Environment		
Intragovernmental Costs	15,822	20,068
Public Costs	77,894	82,754
Subtotal—Promote Healthy Capital Markets through an Effective and Flexible Regulatory Environment	93,716	102,822
Foster Informed Investment Decision Making		
Intragovernmental Costs	28,437	26,052
Public Costs	139,999	107,435
Subtotal—Foster Informed Investment Decision Making	168,436	133,487
Maximize the Use of SEC Resources		
Intragovernmental Costs	17,457	19,374
Public Costs	85,942	79,893
Subtotal—Maximize the Use of SEC Resources	103,399	99,267
Total Entity		
Intragovernmental Costs	165,615	181,683
Public Costs	815,350	749,220
Total Costs	980,965	930,903
Less: Exchange Revenues	1,109,891	956,317
Net (Income) from Operations	$ (128,926)	$ (25,414)

Intragovernmental costs arise from exchange transactions made between two reporting entities within the federal government in contrast with public costs which arise from exchange transactions made with a non-federal entity.

NOTE 14. Exchange Revenues

For the fiscal years ended September 30, 2009 and 2008, exchange revenues consisted of the following:

(DOLLARS IN THOUSANDS)	FY 2009	FY 2008
Securities Transactions Fees	$ 927,112	$794,672
Securities Registration, Tender Offer, and Merger Fees	181,671	161,377
Other	1,108	268
Total Exchange Revenues	$1,109,891	$956,317

NOTE 15. Status of Budgetary Resources

A. Apportionment Categories of Obligations Incurred

The distinction between Category A and B funds is the time of apportionment. Category A funds are subject to quarterly apportionment by OMB. 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 activity. For the fiscal years ended September 30, 2009 and 2008, obligations incurred as reported on the SBR consisted of the following:

Obligations Incurred *(DOLLARS IN THOUSANDS)*	FY 2009	FY 2008
Direct Obligations		
Category A	$964,640	$915,422
Reimbursable Obligations		
Category B	1,236	403
Total Obligations Incurred	$965,876	$915,825

In addition, the amounts of budgetary resources obligated for undelivered orders include $152.8 million and $157.5 million as of September 30, 2009 and 2008, respectively.

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

A comparison between the FY 2009 SBR and the actual FY 2009 data in the President's budget cannot be presented, as the FY 2011 President's budget which will contain the FY 2009 data is not yet available; the comparison will be presented in next year's financial statements.

A comparison between the FY 2008 SBR and the FY 2008 data in the FY 2010 President's budget is as follows:

(DOLLARS IN MILLIONS)	Budgetary Resources	Obligations Incurred	Distributed Offsetting Receipts	Net Outlays
Combined Statement of Budgetary Resources	$974	$916	$ 4	$(105)
Expired Accounts	(1)	—	—	—
Internal Fund Transfer	—	—	(62)	—
Other	—	(1)	—	—
Budget of the U.S. Government	$973	$915	$(58)	$(105)

The SBR reports on both expired and unexpired amounts while the budget excludes expired accounts that are no longer available for new obligations. The $62 million difference is due to a large, one-time transfer from an SEC suspense fund to an SEC deposit fund which was not reported on the distributed offsetting receipts line of the SBR. The internal one-time transfer was not presented in the SBR in order to maintain comparability between years. Other differences are due to rounding.

NOTE 16. Custodial Revenues

For the fiscal years ended September 30, 2009 and 2008, the source of custodial revenues is shown below. Collections are transferred to Treasury.

(DOLLARS IN THOUSANDS)	**FY 2009**	**FY 2008**
Cash Collections		
Disgorgement and Penalties (Note 18)	$815,802	$192,958
Other	10	111
Increase/(Decrease) in Amounts to Be Collected	4	(2)
Total Non-Exchange Revenues	$815,816	$193,067

NOTE 17. Reconciliation of Net Cost of Operations (Proprietary) to Budget (formerly the Statement of Financing)

For the fiscal years ended September 30, 2009 and 2008:

(DOLLARS IN THOUSANDS)	FY 2009	FY 2008
RESOURCES USED TO FINANCE ACTIVITIES		
Budgetary Resources Obligated:		
Obligations Incurred (Note 15)	$ 965,876	$ 915,825
Less: Spending Authority from Offsetting Collections and Recoveries	(1,047,046)	(1,024,548)
Net Obligations	(81,170)	(108,723)
Other Resources:		
Imputed Financing from Cost Absorbed by Others (Note 10)	25,955	24,107
Total Resources Used to Finance Activities	(55,215)	(84,616)
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	6,185	13,721
Resources That Finance the Acquisition of Assets Capitalized on the Balance Sheet	(24,844)	(16,520)
Net Decrease in Revenue Receivables Not Generating Resources until Collected	—	27,678
Total Resources Used to Finance Items Not Part of the Net Cost of Operations	(18,659)	24,879
Total Resources Used to Finance the Net Cost of Operations	(73,874)	(59,737)
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:		
Costs That Will Be Funded by Resources in Future Periods	3,867	3,533
Net Increase in Revenue Receivables Not Generating Resources until Collected	(92,169)	—
Change in Lease Liability	(3,255)	(1,097)
Change in Unfunded Liability	10,176	754
Total Components of Net Cost of Operations That Will Require or Generate Resources in Future Periods	(81,381)	3,190
Components Not Requiring or Generating Resources:		
Depreciation and Amortization	26,414	29,626
Revaluation of Assets or Liabilities	—	1,457
Other Costs That Will Not Require Resources	(85)	50
Total Components of Net Cost of Operations That Will Not Require or Generate Resources in Future Periods	26,329	31,133
Total Components of Net Cost of Operations That Will Not Require or Generate Resources in the Current Period	(55,052)	34,323
Net (Income) from Operations	$ (128,926)	$ (25,414)

NOTE 18. Disgorgement and Penalties

The SEC's non-entity assets consist of disgorgement, penalties, and interest assessed against securities law violators where the Commission, administrative law judge, or in some cases, a court, has determined that the SEC should return such funds to harmed investors where practicable. The SEC also recognizes an equal and offsetting liability for these non-entity assets as discussed in *Note 1.M. Liabilities.*

When the Commission or court issues an order, the SEC establishes an account receivable due to the SEC. When collected, the SEC holds receipts in FBWT or invests in Treasury securities pending distribution to harmed investors. Disbursements related to disgorgements and penalties include distributions to harmed investors, payments to tax authorities, and fees paid to plan administrators and the Bureau of the Public Debt. When it is not practical to return funds to investors or when court orders expressly state that funds are to be remitted to the U.S. Treasury, the SEC transfers funds to Treasury. The SEC does not record on its financial statements any amounts ordered to another government entity such as a court, or a non-governmental entity such as a receiver. Additional details regarding disgorgement and penalties are presented in *Note 1.S. Disgorgement and Penalties, Note 2. Non-Entity Assets* and *Note 12. Earmarked, Other, Disgorgement and Penalties, and Non-Entity Funds.*

At September 30, 2009 and 2008, the net inflows and outflows for FBWT, Investments, and Accounts Receivable related to disgorgement and penalties consisted of the following:

(DOLLARS IN THOUSANDS)	FY 2009	FY 2008
Fund Balance with Treasury		
Beginning Balance	$ 37,707	$ 13,094
Collections	885,318	279,905
Purchases and Redemptions of Treasury Securities	1,032,328	709,902
Disbursements	(1,095,929)	(772,236)
Transfers to Treasury (Note 16)	(815,802)	(192,958)
Total Fund Balance with Treasury	43,622	37,707
Investments, Net (Note 4)		
Beginning Balance	2,982,542	3,602,666
Net Activity	(1,022,931)	(620,124)
Total Investments, Net	1,959,611	2,982,542
Accounts Receivable, Net (Note 5)		
Beginning Balance	88,118	63,610
Net Activity	206,390	24,508
Total Accounts Receivable, Net	294,508	88,118
Total Disgorgement and Penalties (Notes 2 and 12)	$ 2,297,741	$3,108,367

Appendix I: Material Weakness

During our audit of the Securities and Exchange Commission's (SEC's) fiscal year 2009 financial statements, we identified six significant deficiencies[1] that collectively represent a material weakness[2] in internal control over financial reporting. This material weakness gives rise to significant management challenges that have (1) increased the risk that data processed by SEC's information systems are not reliable or appropriately protected, (2) impaired management's ability to prepare its financial statements without extensive manual procedures, and (3) resulted in unsupported entries and errors in the general ledger. The significant deficiencies that we identified, and discuss in more detail in the following sections, relate to SEC's internal control over (1) information security, (2) financial reporting process, (3) fund balance with Treasury, (4) registrant deposits, (5) budgetary resources, and (6) risk assessment and monitoring processes. We reported on some of these issues last year[3] and in prior audits.

Information Security

Since our 2004 audit of SEC's financial statements, we have consistently reported significant deficiencies in SEC's information security controls. SEC has made progress in mitigating certain control weaknesses that we have previously reported, such as (1) designating a senior agency information security officer who will be responsible for managing SEC's information security program, (2) assigning a configuration manager to manage configuration for the general ledger system, (3) completing and approving physical security standards and procedures, and (4) completing the annual testing of security controls for the general ledger application and general support system. However, during fiscal year 2009, key information security control weaknesses remain that continued to jeopardize the confidentiality, availability, and integrity of information processed by SEC's key systems, increasing the risk of material misstatement for financial reporting. For example, in some instances SEC did not adequately (1) segregate computer-related duties and functions;

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

[2] A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

[3] GAO, *FINANCIAL AUDIT: Securities and Exchange Commission's Financial Statements for Fiscal Years 2008 and 2007*, GAO-09-173 (Washington, D.C.: Nov. 14, 2008).

(2) restrict user privileges; (3) implement patches and current software versions; (4) use approved, secure means to transmit data; (5) implement configuration management; and (6) complete a certification and accreditation of its general ledger supporting processes during fiscal year 2009.

We continued to identify ineffective information system controls for the Electronic Data Gathering, Analysis, and Retrieval (EDGAR) and Fee Momentum systems. EDGAR performs automated collection, validation, indexing, acceptance, and forwarding of submissions by companies and others who are required by law to file forms with SEC, and is the source of revenue data for material filing fee transactions. Fee Momentum is EDGAR's subsystem that maintains the accounting information related to filing fees and is integrated through an interface with SEC's general ledger system. For both EDGAR and Fee Momentum, SEC did not adequately (1) restrict user access privileges; (2) restrict remote access; (3) implement appropriate password settings; (4) implement policies and procedures for granting access; (5) verify that access requests were reviewed and approved; (6) consistently apply patches and current versions; (7) implement an audit trail showing system user activities; and (8) ensure the approved, secure transmission of data. We believe the risk of misstatements in SEC's financial reporting is heightened as a result of these weaknesses.

We also continued to find ineffective automated controls for SEC's general ledger system and supporting applications, and ineffective controls over the databases and supporting processes used to generate and maintain SEC's financial reports. For example, SEC did not adequately implement key configuration management controls over the information system components associated with the general ledger system. Specifically, SEC did not consistently implement test plans; adequately document or approve changes to system requirements, design, and commands; and establish or maintain configuration baselines of the system's hardware and software. Furthermore, the financial reporting and analysis database SEC used to prepare its financial statements did not have electronic database logging or an audit trail, and did not have the capability to track login/logout activity and/or other security-related events specified by the system's audit policy such as when records are updated, values are changed, or accounting data are inappropriately altered. Therefore, an individual could gain access and make system changes that would not be detected. During this year's audit, we discovered a discrepancy between certain general ledger account balances obtained directly from the general ledger system and the balances in SEC's financial reporting analysis database. It took SEC several months to identify and fix the cause of this discrepancy.

We also found that SEC did not adequately develop implementation guidelines for separating incompatible functions among personnel, and reasonably assure that staff duties for the general ledger system were properly segregated and monitored. In addition, as of the end of fiscal year 2009, SEC did not complete a certification and accreditation of its processes that support the preparation of the financial statements including the processing of (1) accounts receivable data, (2) accounts payable data for payments to harmed investors, and (3) investment-related data. System certification and accreditation is important, because without it, security weaknesses may go undetected and management may not be alerted to potential vulnerabilities. Systems that are not certified and accredited have increased risk of unauthorized modification or destruction of data.

Subsequent to fiscal year end, in October 2009, SEC completed the certification and accreditation procedures for the general ledger system and supporting processes, and identified similar risks associated with its financial reporting processes. For example, SEC identified the following vulnerabilities associated with the general ledger system and the supporting processes SEC uses to prepare its financial statements:

- Unauthorized personnel can view, manipulate, or destroy data.
- The general ledger system does not protect the integrity of transmitted information.
- The general ledger system does not enforce a sufficiently restrictive set of rights/privileges or accesses needed by users for the performance of specified tasks.
- Serious unauthorized activity may remain undetected and the general ledger system security log may not be sufficient to support the investigation of a compromised system.

SEC concluded in its security accreditation decision letter dated October 8, 2009, that the risk to agency operations, agency assets, or individuals associated with these vulnerabilities was at an acceptable level, and declared that adequate security controls have been implemented and are present in the general ledger system and supporting processes. However, our work concluded that until these vulnerabilities are addressed, SEC cannot rely on the internal controls contained in its automated financial management systems to provide reasonable assurance that, in the absence of effective compensating procedures, (1) its financial statements, taken as a whole, are fairly stated; (2) the information SEC relies on to make decisions on a daily basis is accurate, complete, and timely; and (3) sensitive data and financial information are appropriately safeguarded. This risk of SEC's ineffective information security controls is mitigated to some degree through its manual compensating controls, such as reconciliations between the general ledger system and the database used to prepare the trial balance and financial statements. However, SEC's reconciliation of filing fee revenue did not compensate for deficiencies in EDGAR and Fee Momentum because the reconciliation did not reconcile to third party or external source data. Collectively, these weaknesses represent a significant deficiency in internal control over information systems that increase the potential for undetected material misstatements in SEC's financial statements and inadvertent or deliberate misuse, fraudulent use, improper disclosure, or destruction of its financial information and assets.

Financial Reporting Process

Many of SEC's key accounting applications occur manually outside the general ledger system because SEC's general ledger system and certain software applications and configurations are not designed to provide the accurate, complete, and timely transaction-level financial information needed to accumulate and readily report reliable financial information. In addition, because of weak information system security controls discussed previously, SEC is unable to rely on its general ledger system to protect the integrity of the financial data. SEC's controls to compensate for its general ledger limitations are cumbersome and largely detective in nature, increasing the risk that errors or fraud that could result in a misstatement to the financial statements would not be prevented. During fiscal year 2009, we found that SEC's controls were not always effective in detecting misstatements that could occur as a result of SEC's extensive use of databases, spreadsheets, and manual workarounds and data handling in its financial reporting process. Following are examples of concerns and limitations we identified this year in SEC's financial reporting process.

- In fiscal year 2008, SEC implemented improvements to its general ledger system in response to previously reported issues concerning its accounting for disgorgement and penalties accounts receivable.[4] Specifically, SEC enhanced its general ledger to enable it to record disgorgement and penalty receivable transactions through a manual interface. This represents an improvement over its previous method of recording monthly summary-level general ledger adjustments. However, SEC has not developed an automated interface with the general ledger system for its receivables and currently has no definitive plans to do so. As a result, integration of disgorgement and penalty receivable amounts from Phoenix (the database that is the source of the disgorgement and penalty data) is still accomplished through manual processes, and significant analysis, reconciliation, and review are performed outside the system to calculate amounts for the general ledger postings of transactions, such as the allowance for loss on disgorgement and penalty accounts receivable. These manual processes are resource-intensive and prone to error, and coupled with the significant amount of data involved with disgorgement and penalty activity, increase the risk of material misstatement to the disgorgement and penalty accounts receivable. As of September 30, 2009, disgorgement and penalty receivables were comprised of 283 receivables totaling $714 million. Errors we identified this year in SEC's quarterly reconciliation of disgorgement and penalty accounts receivable data demonstrated that this important compensating control was ineffective in ensuring the accuracy of the disgorgement and penalty accounts receivable balance. Specifically, we found that SEC reconciled data to and from the same source system and its spreadsheet used for the reconciliation did not include control totals to ensure completeness of the data.

- SEC's general ledger system does not capture detailed investment activity and disgorgement and penalty activity at the enforcement case level. SEC tracks transactions related to this activity on a large spreadsheet which is not integrated with the general ledger system. SEC uses the spreadsheet to deconstruct the summary level data in the general ledger to the case level. The ability to have the detailed data at the case level is important in order for SEC to effectively manage its investments, which at September 30, 2009, totaled $2 billion, and the cash amounts attributable to the individual enforcement cases.

[4] A disgorgement is the repayment of illegally gained profits (or avoided losses) for distribution to harmed investors whenever feasible. A penalty is a monetary payment from a violator of securities law that SEC obtains pursuant to statutory authority. A penalty is fundamentally a punitive measure, although penalties occasionally can be used to compensate harmed investors.

However, our work identified several instances of incorrect or incomplete data in the worksheet which could affect SEC's ability to properly manage its investments and cash balances. In response to our findings, SEC has stated that it is in the planning stages of implementing an automated interface with the general ledger for its investment transaction activity. However, implementation of this interface, planned for fiscal year 2010, is contingent upon the availability of resources.

- SEC's general ledger system lacks the capacity to timely and accurately generate and report information needed to both prepare financial statements and manage operations on an ongoing basis. For example, the general ledger is unable to generate an accurate consolidated trial balance. Instead, SEC employs the use of a financial reporting and analysis tool, housed in a database that does not have electronic logging or audit trails, to produce its monthly trial balances and financial statements. Use of this tool requires effective manual compensating procedures to ensure the integrity of the data reported using this tool. In addition, SEC's general ledger has several unconventional posting models and other system limitations for certain activities that require extensive recording of journal entries and subsequent adjustments, creating significant risk of error or misstatement in SEC's financial reporting. Further, the accounts receivable module of the general ledger was not designed to provide information to support activity in the related general ledger accounts. For example, the general ledger cannot produce an aging of its accounts receivable due to an incorrect system configuration. As a result, SEC manually prepares a spreadsheet to support the accounts receivable balance reported in its financial statements. The initial spreadsheet SEC prepared at September 30, 2009, contained inaccurate data requiring multiple iterative corrections. In another example, the general ledger system's property module is not configured to enable the general ledger to readily report property balances. Instead, SEC has to import property data from the general ledger into an unsecured excel spreadsheet to create a property register, perform manual calculations in the spreadsheet, and use this spreadsheet to reconcile cost in the property module to the general ledger balance. The general ledger system also cannot produce a reliable accounts payable aging report. SEC concurred with our overall assessment relative to the limitations of its general ledger system and its reporting capabilities and is in the early planning phase for evaluating long-term options relative to adopting a sustainable, streamlined financial management solution.

Fund Balance with Treasury

During this year's audit, we found that SEC did not perform the required monthly reconciliation of its Fund Balance with Treasury (FBWT) for the first 8 months of fiscal year 2009. In addition, SEC did not timely research and resolve differences reported on the monthly *Statement of Difference*s Treasury provides to SEC. As of June 30, 2009, these differences amounted to $3.2 million. SEC was not able to perform its formal reconciliation or resolve Treasury differences due to an issue with the general ledger system that was not fixed until July and also to incomplete data necessary to properly record all travel-related expenses. As of September 30, 2009, SEC was still not able to determine the cause for all of the differences and recorded an unsupported journal entry of about $840,000 to force its FBWT account to match Treasury's balance.

The Treasury Financial Manual, *Part 2 Chapter 5100 Supplement*, provides that all agencies must complete and fully document a reconciliation of FBWT monthly. The reconciliation should be approved by an authorized agency official as evidence that the reconciliation was properly completed and reviewed. Federal agencies are also required to research and resolve differences reported on the monthly *Statement of Differences* (Treasury's Financial Management Service (FMS) 6652). FMS notifies agencies of their deposit and disbursement differences on FMS 6652. The supplement states: "An agency may not arbitrarily adjust its FBWT account. Only after clearly establishing the causes of errors and properly documenting those errors, should an agency adjust its FBWT account balance. If an agency makes material adjustments, the agency must maintain supporting documentation. This will allow correct interpretation of the error and its corresponding adjustment."

SEC's failure to perform the monthly Treasury reconciliation and its recording of an unsupported journal entry to adjust its FBWT represents a significant deficiency in internal control and increases the risk that the accuracy and timeliness of deposit and disbursement data reflected in SEC's FBWT and the related accounts are misstated. Failure to implement effective processes and procedures concerning reconciliations of FBWT also could increase SEC's risk of fraud, violations of appropriations laws, and mismanagement of funds. SEC agreed with the need to timely resolve differences between SEC and Treasury reporting and has stated it plans to develop a monitoring system to ensure all reconciliations are performed and reviewed timely.

Registrant Deposits

SEC is partially funded through the collection of securities registration, tender offer, merger, and other fees (filing fees) from registrants. SEC records the filing fees it collects as revenue. However, if registrants submit amounts to SEC in excess of the actual fee payment due for the filing, SEC records the excess payments collected in a registrant deposit liability account until earned by SEC from a future filing. SEC returns the amount in the deposit liability account to the registrant if the account has not had any activity against it for 6 months. As of September 30, 2009, SEC's liability for registrant deposits totaled $41 million.

As in prior years, during our testing of filing fee transactions this year, we identified amounts recorded in the registrant deposit account liability that were not properly returned to registrants and amounts that were not properly recognized as revenue in the correct fiscal year. Specifically, of the $41 million in registrant deposit accounts at September 30, 2009, $27 million in deposit accounts had been dormant for 6 months or more. Our audit also identified amounts in the registrant deposit account liability that SEC earned in prior years and therefore should have been recognized as revenue in those years. SEC was aware that some of the liability amounts were earned. For example, as of September 30, 2009, SEC identified $3.7 million in the liability account that should have been recognized as revenue in prior years; however, these amounts were not properly recognized as revenue due to a system configuration error. SEC acknowledged that its process for researching the deposit account activity to determine if amounts should be refunded or recognized as revenue is labor-intensive. SEC also acknowledged it does not have dedicated resources assigned to address this issue. SEC stated it has postponed materially redesigning the processes pertaining to its registrant deposit accounts in anticipation of an upcoming effort to replace EDGAR and Fee Momentum. Untimely review and recognition of revenue in the incorrect period represent a significant deficiency in SEC's internal control over the registrant deposit account balances, resulting in misstating filing fee revenue and the related registrant deposit account liability amounts in the current period.

Budgetary Resources

For fiscal year 2009, SEC incurred approximately $966 million in obligations, which represents legal liabilities against funds available to SEC to pay for goods and services ordered. At September 30, 2009, SEC reported that the amount of budgetary resources obligated for undelivered orders was approximately $152.8 million. Also during the year, SEC deobligated approximately $29 million for prior year undelivered order transactions that were either cancelled or the dollar amount of the obligation was decreased.

Since our 2007 audit of SEC, we have reported significant deficiencies in SEC's accounting for budgetary resources. During fiscal year 2009, we continued to identify weaknesses in SEC's accounting for obligations, including undelivered orders. Specifically, we continued to find numerous instances in which SEC recorded invalid obligation-related transactions as a result of incorrect posting configurations in SEC's general ledger. SEC updated some of its posting models to correctly post certain budget transactions; however, SEC was not able to correct all posting models by September 30, 2009. During fiscal year 2009, SEC made at least over $51 million in adjusting entries to correct for transaction posting configuration limitations. We also found errors this year in several obligation-related transaction postings in the general ledger, including errors in recorded amounts and budget object classifications. Further, we found obligations that were not always recorded timely and were not always supported by documentation evidencing the obligation as having been approved by an authorized individual.

Budgetary accounting system deficiencies resulting in significant manual workarounds and the posting of a large number of general ledger adjustments increase the risk of processing errors and misstatements related to budgetary activities in SEC's Statement of Budgetary Resources. SEC relied on labor-intensive, ad hoc queries and analyses to correct system-generated erroneous entries. In addition, we continued to find that SEC did not maintain sufficient documentation demonstrating proper authorization for downward adjustments to obligations for prior year undelivered orders. As a result, documentation was not sufficient to determine (1) whether transactions were approved for deobligation, (2) the names of the officials authorizing amounts for deobligation, or (3) the date the transaction was approved. The ineffective processes and related documentation deficiencies that caused these errors constitute a significant deficiency in SEC's internal control over recording and financial reporting of its budgetary activities. Further, these deficiencies put SEC at risk of future misstatements recorded in its general ledger and reported on its Statement of Budgetary Resources if the necessary compensating adjustments are not identified and made.

Risk Assessment and Monitoring Processes

During fiscal year 2009, SEC performed a risk assessment related to its internal controls over financial reporting and tested the operating effectiveness of controls based on the results of its assessment. The process of identifying and analyzing risk is a critical component of an effective internal control system and includes how management identifies risks relevant to the preparation of financial statements and information, assesses the likelihood of the manifestation of those risks, and decides upon actions to manage and mitigate the risks. During our audit, we identified significant risks to SEC's financial reporting that SEC did not initially identify during its own risk assessment. For example, SEC did not initially consider the risks associated with its information systems even though we have reported control deficiencies with SEC's information security controls since 2004. Based on our finding, subsequent to year end, in October 2009, SEC did identify and consider the risks associated with its information security controls. However, SEC's conclusion that the risks to its general ledger system and supporting processes were acceptable was not consistent with our conclusion. These risks were discussed previously in the information security section of this appendix.

SEC's risk assessment also did not initially consider risks related to its payroll service provider's (Department of the Interior's) Statement on Auditing Standards (SAS) 70 report,[5] which identifies key user controls that agencies using Department of the Interior's services should have in place to ensure effective control over payroll processing. Risks relevant to payroll transactions are important at SEC since its payroll expense is the most significant expense reported in its financial statements. Further, SEC's risk assessment did not document its evaluation, consideration, and mitigation of certain significant risks or control breakdowns identified from internal sources during the course of the year, and did not document SEC's evaluation of the design effectiveness of the key controls.

We also identified weaknesses in SEC's monitoring process which indicate a lack of effective oversight of controls. Management's monitoring of controls should include whether the controls are operating as intended

[5]SAS No. 70, *Service Organizations*, is the authoritative guidance that allows service organizations to disclose their control activities and processes to their customers and their customers' auditors in a uniform reporting format. The issuance of a service auditor's report prepared in accordance with SAS No. 70 signifies that a service organization has had its control objectives and control activities examined by an independent accounting and auditing firm. The service auditor's report includes valuable information regarding the service organization's controls and the effectiveness of those controls.

and include assessing the design and operation of controls on a timely basis and taking necessary corrective actions. As discussed previously, we found that SEC's monitoring procedures did not address all identified risks. Further, SEC management's oversight was not sufficient given the frequency and sensitivity of the control activity, and monitoring procedures were not always completed in accordance with SEC's stated testing plan. We also found that the results of SEC's monitoring procedures were not consistently documented. For example, SEC could not provide evidence that it monitored controls over its payroll exception reports to ensure payroll transactions were recorded accurately and timely. Also, SEC does not have a process that comprehensively captured the cumulative effect of correcting entries to evaluate their impact on current and prior year financial statements as a whole, nor did SEC monitor its compliance with the Prompt Payment Act.[6] Further, SEC's monitoring procedures were not robust enough in identifying certain control weaknesses that we found during the year and discussed previously in this report, such as issues with its registrant deposits and budgetary resources, which serves to underscore SEC's deficiency in this area.

Performing comprehensive risk assessments and monitoring procedures are key components of management's responsibility to establish and maintain internal controls on an ongoing basis. Collectively, the weaknesses we identified in these processes represent a significant deficiency in internal control, and because of their importance for ensuring reliable financial reporting, point to the need for SEC to make improvements to these processes a high priority.

[6]Under the Prompt Payment Act and implementing regulations, federal agencies are required to timely pay proper invoices submitted by vendors when applicable, pay interest penalties for late payments, and only take discounts when payments are made by the discount date. See 31 U.S.C. ch. 39; 5 C.F.R. pt. 1315.

Appendix II: Comments from the Securities and Exchange Commission

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

THE CHAIRMAN

November 16, 2009

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 respond to the Government Accountability Office's draft report on the Securities and Exchange Commission's fiscal year 2009 and 2008 Financial Statements (GAO-10-250). I would like to personally recognize and commend your and your staff's efforts and dedication in working with the SEC again this year to complete the required audit of the agency's financial statements.

I am pleased that the audit found that the statements and notes are presented fairly, in all material respects, and in conformity with U.S. generally accepted accounting principles. I am also pleased that there were no instances of reportable non-compliance with laws and regulations.

As you know, the SEC determined that six significant deficiencies, discussed more fully in the opinion on internal control, in the aggregate represent a material weakness over information systems and related financial controls. We are committed to making the resolution of these deficiencies a priority of the very highest order, and are developing a plan to remediate this material weakness by devoting the resources necessary to address these issues head-on. Over the coming months, we will tackle the systems and operational issues identified to enhance the SEC's controls in all areas, thereby strengthening the reliability of our financial reporting. As you and your staff noted, the issues that underlie these deficiencies have been building and accumulating for years. While some of them can – and will – be addressed quickly, others will take more time to solve. But our resolve to diligently correct all of these problems is strong.

I very much appreciate our cooperative relationship and look forward to continuing our productive dialogue on the issues addressed in this year's audit. If you have any questions or concerns, please feel free to contact me.

Sincerely,

Mary L. Schapiro

Mary L. Schapiro
Chairman

(196201)

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