Testimony on "Federal Leased Property: Are Federal Agencies Getting a Bad Deal?"
by
Jeffrey Heslop
Chief Operating Officer, U.S. Securities and Exchange Commission

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Subcommittee of Federal Financial Management, Government Information, Federal Services and International Security
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Chairman Carper, Ranking Member Brown, Members of the Subcommittee:

Thank you for the opportunity to testify on behalf of the Chairman of the Securities and Exchange Commission[1] regarding the Commission's lease of office space at the Constitution Center building in Washington, D.C.

The report by the Commission's Office of Inspector General (OIG) concerning Constitution Center identified a number of significant flaws in the SEC's leasing processes. The fact that the SEC has not paid any rent to date for this property and that the bulk of the space has been leased to other tenants does not adequately address a situation that never should have occurred. The only appropriate response by the SEC is to take all necessary steps to resolve the remaining space issues, to correct the obvious deficiencies in our leasing processes, to ensure accountability for the events surrounding this lease, and to work with the General Services Administration (GSA) with regard to future space needs.

The Chairman of the SEC has pledged to address the issues identified by the OIG aggressively and transparently. My testimony today will outline for the Subcommittee how we intend to make certain that resources are used prudently, that the agency implements the recommendations of the OIG, and that future leasing activity is managed properly.

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1 The views expressed in this testimony do not necessarily represent the views of the full Commission.

I. Factual Background Leading To The OIG Report

The SEC currently employs approximately 3,900 permanent staff and more than 700 contractors. Approximately 60 percent of the permanent staff work out of the agency's headquarters, principally the Station Place buildings adjacent to Union Station in Washington, DC. The agency's remaining 1,500 employees (mainly enforcement and examination staff) work in our 11 regional offices. The SEC does not own any of its facilities, all of which are leased. In addition to office space, these leases include space for public meeting rooms, hearing and testimony rooms, files and records storage, and information technology (including the agency's data center and alternate data center). The SEC currently maintains about 2.5 million square feet of leased space. In the current fiscal year, the lease payments total approximately $100 million, which is about 8 percent of the agency's annual budget. The Commission's Office of Administrative Services (OAS), through its Real Property and Leasing Branch, has been responsible for managing the leasing program for the agency.

My understanding of what transpired in the Spring of 2010 is as follows:[2]

- In the Spring of 2010, the SEC anticipated the need not only to expand its longstanding core responsibilities but also to implement the substantial new obligations it was likely to be assigned under the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act). Because these efforts would require the hiring of additional staff and space for expansion was limited under existing leases, OAS started to consider options for additional office space.

- In June 2010, at a meeting regarding leasing issues with the then-Executive Director of the SEC as well as staff from OAS, Chairman Schapiro indicated her preference for hiring new staff in the regional offices rather than at headquarters, as well as a preference that new space in Washington be within walking distance of our headquarters at the Station Place buildings to eliminate the need for expensive shuttle services.

- Approximately one month later, just after the Dodd Frank Act had passed and assigned the SEC significant new responsibilities, on July 23, 2010, the then-Executive Director informed Chairman Schapiro's staff that he urgently needed to discuss obtaining space at

[2] My understanding is based both on my review of the OIG report and recent testimony of Chairman Schapiro.

Constitution Center, a building located at 400 Seventh Street in southwest Washington, DC. She was told that our other leasing options in Washington, DC no longer existed, that the space at Constitution Center was our only option given our space needs, that the pricing was advantageous, and that they had to move quickly as there was competition for the space. Given her previous discussions, Chairman Schapiro assumed the proposal was consistent both with the then existing budget projections for future employee growth and her preference for staff to be housed where possible in the regions, and concurred with the proposal.

- According to the OIG report, the budget projections for future employee growth were improperly increased by OAS staff, and staff also assumed – contrary to the Chairman's communicated position – that all new positions would be in the SEC headquarters. These facts, according to the OIG report, were used to justify an increase in the amount of space needed at SEC headquarters for the SEC's projected expansion, an increase that the OIG report concluded was improper.

- Shortly thereafter, on July 28, 2010, the SEC, through its leasing group, entered into an agreement for 900,000 square feet at Constitution Center, with an ability to assign or sublet the entirety of the space. The agreement was for a 10-year term, with the space to be delivered to the SEC in phases and the first space available at the start of fiscal year 2012 with rent payments to commence in January 2012.

- Within weeks, Chairman Schapiro became concerned that the previously anticipated increase in funding for the SEC (both for existing programs and the new Dodd-Frank Act responsibilities) would not come to pass, despite the Dodd Frank Act's authorization to double the SEC budget over five years. The Continuing Resolution, which would ultimately remain in place for the first six months of fiscal year 2011, would limit the Commission's ability to hire new staff and thus limit our need for additional space. In light of these budgetary concerns, Chairman Schapiro met during the Fall of 2010 on multiple occasions with members of the SEC's leasing group to discuss options for Constitution Center that would limit the SEC's exposure for space it likely would not fill. The SEC worked with two non-appropriated financial regulatory agencies (the Office of the Comptroller of the Currency and the Federal Housing Finance Agency) that wanted to occupy the majority of the space allotted to the SEC (558,000 square feet). The SEC then released that space, permitting the landlord at Constitution Center to lease the space to these other federal tenants. The releases were conditioned on the SEC being released from all obligations for the 558,000 square feet. The other agencies entered into leases for the Constitution Center space in January 2011. As described in more detail below, the SEC has since been working with the GSA regarding the remaining space.

The SEC's OIG recently reviewed the agency's leasing process for Constitution Center, issuing a report on May 16, 2011. The report provides a thorough review of the OIG's findings and recommendations, and reveals significant flaws in our leasing processes. We are promptly implementing the OIG's recommendations, and, as described in more detail below, recently submitted to the OIG a written corrective action plan. Specifically, the Chairman has directed me to implement the OIG's recommendations and to address the deficiencies in our leasing processes. In addition, the employees recommended for possible disciplinary action by the OIG have been reassigned to other duties pending resolution of the disciplinary process, which we are moving forward on quickly.

II. The SEC's Obligations Regarding The Remaining Space At Constitution Center

As noted above, growing budget uncertainties led the SEC to seek ways to undo or limit the obligations imposed by the Constitution Center agreement. After successfully identifying two new lessees for the majority of the space, the SEC retains approximately 300,000 square feet at Constitution Center.

Chairman Schapiro, I and others at the SEC recently met with the head of GSA to discuss, among other things, the remaining Constitution Center space. Both this and multiple subsequent conversations between our staffs have been very productive. GSA has informed us that it has prospective tenants with leasing needs that may align with the available Constitution Center space. More recently, Commission staff, working with GSA, has been seeking to finalize the terms concerning the remaining space to move this process forward so that the space may be used by another federal tenant. We are urgently addressing any remaining issues regarding this lease, and will continue to work closely with GSA. Because of the timing of the lease, the SEC has not been required to make any lease payments to date.

III. <u>The Inspector General's Recommendations</u>

The OIG report provides a thorough discussion of the OIG's findings and recommendations, and clearly reveals significant flaws in the process by which SEC leasing decisions were made. On June 30, the SEC provided the OIG with a written corrective action plan. While work is underway to implement the corrective actions described below, they may be revised or expanded as a result of the ongoing discussions with GSA. Currently the corrective action plan includes the following:

- As an interim action, the Chairman revoked designations of authority that previously permitted the SEC to enter into real estate leases without her approval. As described in more detail below, an arrangement with GSA recently was finalized, and as such, the agency will update any other delegations and designations of authority to ensure proper controls are in place.

- In response to the recommendation that the SEC conduct a comprehensive assessment of OAS operations, the SEC retained the services of outside consultants to assess OAS's organizational structure, including decision-making processes, reporting relationships, and quality controls.

- All leasing operations now report to me as Chief Operating Officer.

- A senior executive-level facilities management oversight committee is being created to provide oversight and guidance to the SEC leasing process and serve as a forum for executive-level discussion of the agency's leasing decisions.

- The directors of our national enforcement and examination programs are leading a review of the SEC's regional office presence, which will include an assessment of the agency's location strategy and associated office space needs.

- A new leasing project approval process is being developed that will address, among other things: coordination with GSA; estimation accuracy; the approval process for non-competitive leasing acquisitions; cost/benefit and business case analysis; funding availability; clear identification of hiring needs with the requisite geographic match; and external government agency requirements.

Although the SEC is engaged in the implementation of the corrective action plan, additional requirements and details are likely to be established consistent with the relationship established with GSA.

IV. <u>The Commission's Leasing Efforts Going Forward</u>

In light of the problems identified the SEC recognizes the benefits of having GSA manage the Commission's future lease acquisitions. Leasing is not part of the Commission's core mission and we cannot allow it to impede that mission. GSA, by contrast, has long experience and expertise in leasing.

In her recent meeting at GSA, in addition to discussing the Constitution Center space, Chairman Schapiro discussed with the GSA Administrator ways in which GSA could assist the Commission on our leasing efforts going forward. GSA indicated it was open to playing a significant role in those efforts. Following that meeting, Commission staff has had multiple further discussions with GSA staff. On August 1, 2011, the SEC and GSA entered into a Memorandum of Understanding (MOU) with each other that contemplates an immediate role for GSA in managing upcoming SEC leasing activities, as well as all other future leasing needs as they arise. Ultimately, we anticipate that GSA will be responsible for, among other things, assessing the space needs of the Commission including requirements development; planning for the acquisitions, including preparing preliminary cost estimates; drafting information lease prospectuses, conducting market surveys, and establishing negotiation goals and objectives; soliciting, receiving, assessing and negotiating the offers, which will cover the competition process; executing all required lease documents; and administering the lease, including responsibility for tenant improvements, construction, and any necessary moves. The arrangement with GSA also should permit the SEC to pare down its leasing program solely to function as liaison to GSA. In addition to the leasing activities at the core of the MOU, we will be exploring other avenues of administrative services that GSA may be able to assist us with that will permit us to scale back further our administrative functions in the relevant areas.

V. <u>Status Of The Disciplinary Proceedings Recommended By The OIG</u>

The OIG report recommended that the SEC initiate disciplinary proceedings for three individuals involved in the Constitution Center leasing process. Accountability is critical because, without it, there is neither fairness nor reform. This process has begun, and Chairman Schapiro has expressed a desire for this process to move as quickly as the laws and regulations permit, consistent with fundamental fairness, to assess and implement remedial measures and discipline as appropriate. In the meantime, the individuals for whom the OIG report recommended a disciplinary review have been reassigned. Their current duties do not involve leasing or any other authority that could bind the Commission, nor do they involve activities that relate to the expenditure of appropriated funds.

VI. Conclusion

There is no doubt that the OIG report identified substantial failures in the SEC's leasing process, and we are making every effort to address those failures and ensure no reoccurrence in the future. These efforts include items specific to Constitution Center, including actions to eliminate the remaining space obligations and to conduct the disciplinary process for the relevant individuals. In addition, we are moving quickly to make more programmatic reforms that are incorporating GSA into our future SEC leasing needs.

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