

Stability and Change in a “Best Place to Work”: An Analysis of Human Capital Management at
the Securities and Exchange Commission

Ellen V. Rubin
Assistant Professor
Department of Public Administration and Policy
Rockefeller College of Public Affairs and Policy
State University of New York, University at Albany
135 Washington Ave
Albany, NY 12222
erubin@uamail.albany.edu

David P. McCaffrey
Distinguished Teaching Professor of Public Administration
Department of Public Administration and Policy
Rockefeller College of Public Affairs and Policy
State University of New York, University at Albany
135 Washington Ave
Albany, NY 12222
d.mccaffrey@albany.edu

Karen Bryce
PhD Student
Department of Public Administration and Policy
Rockefeller College of Public Affairs and Policy
State University of New York, University at Albany
135 Washington Ave
Albany, NY 12222
karen.bryce01@albany.edu

This is a working paper in the truest sense: the authors welcome your comments as we revise and improve this manuscript.

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Abstract

The Securities and Exchange Commission (SEC) has managed to maintain a stable operating environment despite significant changes in the financial markets. This stability is due largely to a consensus among its network partners on the norms of a shared regulatory framework. The response of the SEC and its network to the changes in the financial markets has, in part, been shaped by a strong, long-standing culture. One area in which the changing markets have altered the internal operating environment of the SEC is in personnel management. Significant turbulence in personnel management, however, does not appear to have substantially influenced the central elements of the SEC’s culture, operations, and relationships with other parts of the financial regulatory system. Although significant personnel changes have been implemented over the last decade, only now is there early evidence that the SEC is seeing its human capital professionals as a strategic partner in its efforts to implement operational changes. From the perspective of O’Toole and Meier, past performance is likely to be the biggest influence on performance in the future.

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Individuals working in or observing financial markets have noted a mismatch between the skills required to understand financial markets and the skills available in regulatory and supervisory organizations for at least the past 40 years. For example, in a quotation that could have applied anytime during this period, an attorney in an investment bank commented to one of us in 1996 that “This is an unbelievably complex industry. It's one that is changing the fastest; none is faster. And the SEC and regulators are way behind the curve. SEC reports come way after the fact. The technology changes constantly. How do you do a regulated business using rules not designed for today's technology” (McCaffrey & Hart, 1998, p. 136). The problem is not limited to public regulators. Internal control failures also occurred in financial firms; reports on failures after the onset of the financial crisis in mid-2007 emphasize that internal control personnel did not challenge business unit judgments effectively in the majority of firms examined. This was largely because internal control personnel did not understand complex transactions nearly as well as the business offices actually executing and defending them. They therefore did not have the credibility to overcome business unit viewpoints in debates before top management on whether the firm should trade off short-term profits for avoiding long-term risks (Deloitte, 2009; Senior Supervisors Group, 2008; Simcorp StrategyLab, 2009; Société Générale General Inspection Department, 2008; UBS, 2008).

External regulators acknowledge freely their problems in overseeing complex financial technology, problems aggravated by large pay and support differences between subject matter experts in financial services firms and regulatory organizations (Bookstaber, 2007; Faerman,

McCaffrey, & Van Slyke, 2001; McCaffrey, Smith, & Martinez-Moyano, 2007; United States Government Accountability Office, 2009). One of the main themes in the reports on the financial crisis is the need to increase the abilities of regulatory organizations to oversee such instruments and market systems (Counterparty Risk Management Policy Group, 2008; Group of Thirty, 2009). In July 2009, Securities and Exchange Commission (SEC) Chair Mary Schapiro told the House Financial Services Committee that “to better enable our staff to conduct oversight of complex trading strategies and products that exist in today’s markets, we are enhancing training for our staff and also recruiting additional professionals with expertise in securities trading, portfolio management, valuation, forensic accounting, information security, derivatives and synthetic products, and risk management” (Schapiro, 2009, p. 6). On September 24, 2009, SEC Commissioner Troy Paredes remarked:

It is not enough to offer regulatory guidance in concept. The Commission needs to be able to execute on it. To best position the agency to fulfill its mission, we need to have the right blend of skills. The SEC staff has extensive knowledge and expertise and is extremely hardworking and dedicated to serving the public interest. However, the SEC needs to be staffed with more economists and other non-lawyers with a deep understanding of financial markets. Our increasingly complex markets will be better served if the Commission has more economists, quantitative analysts, and others with strong backgrounds in trading and finance actively engaged in every aspect of what the SEC does. When it comes to market structure, the Commission also could benefit from deeper expertise in industrial organization, not just financial economics and trading. For an agency that regulates the world's largest securities markets to be so dominated by lawyers is ill-advised. (Paredes, 2009)

Despite such longstanding questions about regulatory capabilities, the SEC has been one of the most respected public regulatory agencies through most of its history since its establishment in 1934 (Seligman, 2003). For example, a special Congressional study in 1977 identified the SEC as the most effective independent regulatory agency. In the 1980s, the Roper Center for Public Opinion reported surveys indicating that 58% of those polled, and over 80% of

those with an opinion, viewed the SEC favorably or highly favorably (Coates, 2001, pp. 543-544). In testimony before the Senate Committee on Banking, Housing, and Urban Affairs in 2008, Arthur Levitt commented that “For the past 75 years, the SEC has been the crown jewel of the financial regulatory infrastructure and the administrative agencies” (Levitt, 2008, pp. 7-8).

Recent critical reports regarding the Bernard Madoff fraud and matters related to the financial crisis have damaged the SEC’s reputation, at least temporarily, and a survey in 2009 reported that the SEC had the least favorable reputation among six federal agencies listed (Carton, 2009; United States Securities and Exchange Commission Office of Investigations, 2009a, 2009b). However, the periodic crises in the SEC’s history, including at present, complicate but do not fundamentally change this longstanding pattern of credible operations and high levels of prestige in the United States regulatory system.

The goal of our ongoing research, of which this is a part, is to explore the intersections and disconnections between human capital management in the SEC and changes in the financial markets. Specifically, the paper discusses how the SEC’s organizational and political context shape these initiatives. While the paper focuses on the Securities and Exchange Commission, it suggests general questions about the need to understand more fully the political and social context of organizational performance, and the role of human resource management in transforming organizational cultures.

The paper proceeds first with a review of the literature on why management matters in the public sector. This literature identifies a series of variables which are critical to performance, including management efforts to define key organizational tasks and priorities, the manner in which management responds to changes in the external environment, the role of policy networks in implementation, and the consequences of personnel instability. Each of these issues can be

found in the case of the SEC, its response to turmoil in the financial markets, and its management of agency personnel.

Literature Review

Scholars of public management have debated and attempted to establish that management matters to public organizations (Brudney, O'Toole, & Rainey, 2000; Donahue, Jacobson, Robbins, Rubin, & Selden, 2004; Heinrich, Hill, & Lynn, 2004; Hicklin, 2004; Ingraham, Joyce, & Donahue, 2003; Ingraham & Lynn, 2004; McGuire, 2002; Meier & O'Toole, 2003, 2005, 2006; O'Toole Jr. & Meier, 2003a, 2003b; O'Toole & Meier, 1999). For instance, Ingraham, et al (2003) contend that

Good management has different effects on, and follows different paths to, performance in different organizations and levels of government. Without any question, however, the quality of management in government organizations is an important factor in the ability of those organizations to effectively pursue their mission and to use resources well. Good management matters in stable as well as turbulent times; it is a significant influence on the organization's ability to maintain an effective course. (p. 117)

If we assume that effective management relates positively to effective performance, as scholars and public managers have done (Donahue, et al., 2004), then looking deeper into the structure of public management, and therefore the ways that structure affects management, is warranted.

The Meier-O'Toole model of management performance in public organizations, originally presented in 1999, has been a source of study for not only themselves, but other scholars as well (Donahue, et al., 2004; Hicklin, 2004; Nicholson-Crotty & O'Toole, 2004). Their model seeks to understand the relationship between public program performance, hierarchy, environmental factors, and internal management that contributes to program stability and network management (Donahue, et al., 2004; Meier & O'Toole, 2005). Management

includes motivating, coordinating, stabilizing, leveraging, performance improvement and reshaping structural settings (O'Toole & Meier, 1999).

Within the O'Toole-Meier model the management component is represented by M, which can be divided three ways: M₁ represents internal organizational management, including efforts to set goals, priorities, and incentives; M₃ represents management's efforts to exploit the environment of the organization; and M₄ represents management's effort to buffer the unit from environmental shocks (Meier & O'Toole, 2005).

Internal organizational management (M₁) has been studied in several capacities, such as contracting, representative bureaucracy, law enforcement and education (Meier & O'Toole Jr., 2005; Meier, O'Toole, & Goerdel, 2006; Meier, O'Toole, & Nicholson-Crotty, 2004; Nicholson-Crotty & O'Toole, 2004; O'Toole & Meier, 2004). Findings suggest that M₁ is an important factor to understanding public program performance, but it is not easily defined or studied. It contains many factors that could be continually parsed, but are difficult to isolate (Meier & O'Toole, 2004, 2005).

Meier & O'Toole, and others, have placed more emphasis on researching M₃ and M₄—the network and environmental factors. These terms are often studied as a ratio that produces M₂. Networks, in the managerial context usually include central organizations that have relationships with multiple stakeholders. Network environments allow shared responsibility for implementation of public policies and tend to perform better than hierarchical organizations (Donahue, et al., 2004).

Network environments increase the variables that managers may manipulate in their organizations to achieve desired performance. At the same time, they also increase opportunities for instability and uncertainty (O'Toole, 2000). Additionally, managers will often have to choose

between facilitating network action and pleasing key network actors. This can be difficult, but is often the case in light of limited resources (McGuire, 2002).

A relationship exists between managerial networking environments and the autoregressive nature of administration (Meier & O'Toole, 2003). Autoregression implies that there is rigidity to some organizations that do not adapt well to change. Higher levels of network management mean lower levels of autoregressivity (Meier & O'Toole, 2003, 2005). Additionally, greater efforts at external management in the central agency result in greater support from clientele and political organizations (Meier & O'Toole, 2005).

Networks have unique cultures that are separate from the hierarchical organizations, which are members of the network. Culture plays an important role in public management and “understanding the often elusive cultures of public programs, and why key commitments evolve in any given culture, is an essential ingredient for understanding why government programs perform the way they do” (Khademian, 2002, p. 5). The O'Toole-Meier model fails to adequately account for culture as an important influence on how managers and networks respond to change in the external environment. Specifically, cultural norms and expectations with the network limit the range of potential responses to changes in the external environment and organizations can be slow to respond, if at all, to large external changes. The importance of good managers is clear in these cases as they improve internal stability and build trust (O'Toole Jr. & Meier, 2003a).

Personnel stability is identified as another contributor to organizational performance and is a critical component of management capacity (O'Toole and Meier, 2003; Selden and Jacobson, 2007). When considering personnel stability as a part of the performance puzzle, the literature to date has focused on turnover of key staff and found that an increase in turnover, i.e.,

a decrease in personnel stability, is associated with decreased student performance (O'Toole and Meier, 2003). However, personnel stability is more complex than just turnover rates. Significant changes to an agency's personnel rules, revisions to performance appraisal and incentive systems, and the agency's ability to attract, retain, and develop individuals with needed skills and competencies can also play an important role. In fact, arguments in favor of various civil service reforms frequently insist that the changes to the structure and incentives of the personnel system will change bureaucratic behavior and thus improve agency performance.

Following the approach of the Government Performance Project, the components of personnel stability can be classified as focused on the matters of structure, obtaining employee, maintaining employees, and motivating employees (Selden and Jacobson, 2007, Selden, Ingraham and Jacobson, 2001, Ingraham and Selden, 2001).¹ Focusing on the structure of the personnel system guides researchers to consider if changes have been made to the rules for classification, pay, and hiring. For example, at the federal level, does the agency operate within the confines of the General Schedule or does it have the authority to implement an alternative pay and classification system—a highly disruptive and time-consuming process? Questions concerning an agency's ability to obtain employees focus on recruitment and hiring efforts, while an emphasis on maintaining employees considers efforts to retain and develop skilled staff. Finally, the presence and effectiveness of performance incentives and performance appraisal systems influence the ability of the agency to motivate its employees.

¹ The Government Performance Project, initially conducted at the Maxwell School of Citizenship and Public Affairs at Syracuse University, was a criteria-based assessment of management systems in federal agencies and state and local governments. Funding for the project was provided by The Pew Charitable Trusts. The project's website presents details of the GPP, its data collection, analytic methods, results at: <http://sites.maxwell.syr.edu/gpp3/index-2.html>.

To summarize, there is increasing evidence in public administration scholarship that management matters. The frequently used O’Toole and Meier framework identifies a series of management actions that impact performance including management efforts to define key organizational tasks and priorities, the manner in which management responds to changes in the external environment, the role of policy networks in implementation, and the consequences of personnel instability. We add to this framework the importance of considering the cultural norms in the network as a limit on potential managerial responses to environmental change and more detail to the types of personnel instability that may be related to organizational performance. With this context, we now turn attention to studying these issues in the case of the SEC.

Managerial Efforts to Determine Tasks and Shape Perceptions

The first managerial component of the O’Toole and Meier model focuses attention on the activities of leaders to maintain the operations of an organization. This is accomplished through goal setting, framing policy messages, and creating incentives for certain behavior. Much before the current turmoil in the markets, the SEC—directed by the securities laws—formulated its key task as making investment information transparent. It positioned itself as an advocate for individual investors, although engaged in a wider range of tasks including overseeing firms’ operations and market structure.

The SEC Usually Has Avoided Polarizing Tasks

The securities laws, and the SEC when implementing them, mainly require firms to disclose information to investors. The SEC thus avoids the political and technical difficulties of independently assessing the merits of investments on either the part of issuers or investors (Seligman, 2003). The agency occasionally proposes controversial regulations, but usually has

done so cautiously and with the backing of substantial segments of the securities industry or affected corporations. Thus, for example, when scholars in law and economics have argued vigorously for several initiatives reducing the SEC's authority over corporate disclosures to investors—ostensibly benefiting corporations raising capital—the corporations largely have ignored the proposals. Coates (2001) argues that the SEC has responded to industry concerns about the disclosure system, modified rules to avoid charges of a “one size fits all” regulatory approach, and thus avoided persistent criticism from firms issuing securities .

The SEC as “The Investor’s Advocate”

The SEC's “What We Do” webpage leads with the designation “The Investor’s Advocate” (United States Securities and Exchange Commission, 2009b). The original federal securities laws in the 1930s focused on aiding investors who lacked the information and experience to act as well-informed consumers. The laws required corporations and other market participants to provide information to investors and to follow certain standards of behavior.

Individual investors continue to be a significant share of financial markets, but are much more likely to invest indirectly through mutual funds or other institutions, and the SEC's regulations now deal far more with technological and market structure questions involving professionals and institutions (see figure 1). Still, the agency highlights how its activities contribute to “investor confidence” or fairness in the markets even when they affect individual investors indirectly and remotely. The SEC's political legitimacy stems from its image as the government organization assuring that individual investors are not overwhelmed by professionals and institutions in securities markets (Cartwright, 2009; Evans, 2009; Goldberg, 2009; Langevoort, 2009; Levitt, 2002). This image also constrains the agency. As noted above, Congress usually defers to the agency on technical questions (Khademian, 1992; Krause, 1999).

However, key legislators and other elected officials also push the SEC actively and publicly on “investor protection” issues, even when the SEC probably would rather avoid acting in the area on policy and technical grounds, as in controversies over short selling (McCaffrey, 2009). Either way, the SEC’s mission of being the investor’s advocate, when performed credibly, enhances its prestige.

[insert figure 1 about here]

The SEC carries out its investor protection role mainly through rulemaking and periodic high-profile enforcement actions. In practice, other institutions, including other public and private regulators, carry out most ground-level interventions on behalf of investors. The SEC received “nearly 81,000” investor complaints and questions in FY 2008 (United States Securities and Exchange Commission, 2008, p. 18). The SEC’s webpage on “How the SEC Handles Your Complaint” encourages investors to approach firms directly with complaints. If the investor wishes to pursue the complaint further, the agency notes:

We [the Office of Investor Education and Advocacy] will analyze your complaint and decide if we need to refer it to our Division of Enforcement, another SEC office, or another regulator's office. Our Division of Enforcement conducts investigations, but our office does not. The SEC generally conducts investigations confidentially. As a result, the SEC will neither confirm nor deny the existence of any investigation. After analyzing your complaint, we will send a copy of the complaint to the brokerage firm or company. We'll ask the firm or company to send a written report to you and us that responds to your complaint.

Do you know what our limitations are?

Sometimes a complaint is successfully resolved when we ask a firm to report to you and us. But in many cases, the firm or company denies wrongdoing, and it remains unclear as to who is wrong or whether any wrongdoing occurred at all. If this happens, we cannot act as a judge or an arbitrator and force a broker, brokerage firm, or company to resolve your complaint. But the law allows you to take legal action on your own (United States Securities and Exchange Commission, 2009a).

Thus, the agency regularly refers complaints to other regulators, or advises investors to pursue private civil litigation, arbitration, or other private legal assistance. One rough way to compare the volume of direct investor assistance, outside of the important area of rulemaking, is to compare the number of enforcement actions by various regulators and the volume of private civil litigation and arbitration proceedings. Regulatory and legal actions obviously involve more than direct dealings with investors, but large differences among institutions nevertheless would suggest different roles in the system of investor protection. Figure 2 indicates the number of private securities arbitration cases and civil suits initiated under securities and commodities laws, the self-regulatory organization disciplinary proceedings filed with the SEC, and the SEC's total enforcement actions as well as those targeting broker-dealer firms. Figure 2 does not include data on state government enforcement actions, which are not publicly available. However, an aggregate summary from the North American Securities Administrators Association reports that 42 of 53 states and territories surveyed reported 8,365 enforcement actions in the 2004-2007 period (North American Securities Administrators Association (NASAA), 2009).

The SEC obviously plays a major role in setting out the rules governing this system and in pursuing enforcement actions. However, Figure 2, and the NASAA data alluded to above, illustrate the argument that the SEC plays only a small role in directly protecting individual investors. Instead, private litigation and arbitration, Self-Regulatory Organizations, and state governments handle the largest share of ground-level work in dealing with investor protection.

[insert figure 2 about here]

In addition to the roles of management in normalizing the organization's task environment, priorities, and public image, managers of public organizations implement their respective programs in networked environments. While the scope and size of the network may vary, working in networks creates additional challenges for managers to ensure successful program implementation. Like social services and homeland security, financial markets are regulated through a network of partners. In this case, the SEC shares regulatory responsibilities with a variety of institutions, most of them private, in a relatively stable network.

Specifically, the SEC and private organizations share market regulation under securities laws, with some important exceptions. The SEC oversees "self-regulatory organizations" (SROs)—the largest being the Financial Industry Regulatory Authority (FINRA), as well as NYSE Regulation and other securities exchanges—and has the authority to control the SROs directly if need. The SROs, in turn, oversee member firms and individuals who need the professional certifications the SRO's provide to operate in the industry. This system of shared responsibilities dates back to the original 1930s securities laws. At the time, a networked arrangement was a political necessity for successful passage and implementation. The SEC, courts and the Congress have reinforced this understanding in various ways (Pritchard & Thompson, 2009; Seligman, 2003).

Thus, the public and private sectors interact formally and extensively in securities regulation. Negotiations occur in a network of government agencies and private organizations that developed over decades. The SEC, SROs, and firms disagree strongly about particular issues, but issues generally get settled before they escalate to court or Congress. People move freely across the sectors—usually, but not exclusively, from the public to the private—so many individuals in key positions are familiar with each sector's perspective. For example, an article

by two attorneys with SEC experience commented that “many members of the securities bar once worked at the Commission and often attained senior positions within the agency. As a result of that experience, securities practitioners afford the staff an enormous amount of respect, appreciate the difficulties of the staff’s job, and treat the enforcement process seriously” (Flannery & Indek, 1995, pp. 23-24).

Such networks pose both benefits and risks. Regular dealings among regulators and firms outside of regular rulemaking or enforcement proceedings enhance cooperation, reduce information disparities, strengthen regulatory cultures, and arguably lower the threshold of external pressure required to effect changes within firms. They also restrict the flow of information, perspectives, and criticism from outsiders, potentially leading to erosion of performance standards and eventual serious problems (McCaffrey, et al., 2007). Relationships of “mutual respect” among regulators, regulated firms, and supporting organizations like law firms—reinforced by flows of individuals among organizations—stabilize the agency’s political environment as long as the agency is not regarded as “captured” by the industry. The SEC’s most visible role as “the investor’s advocate” helps insulate it from claims that the industry is engaging in regulatory capture.

Network Culture as a Buffer to Environmental Shocks

Managers, and the networks in which their programs operate, have a number of options to respond to shocks from the environment. The options range from defensive reactions aimed to insulate the organization from the event, to exploiting the opportunity as a chance to expand influence, resources, scope of authority, etc. However, this ratio of buffering responses to exploitative responses is limited in scope by the operating norms of the network. For example, a network with relatively stable operations in which the members are in general agreement about

key activities and roles may not see the need for a significant change, despite turmoil in their environment around them. This response may exist because power relations are clear, or because stability is seen as more desirable than the turbulence around the network.

The significant driver of cultural norms in the financial regulatory network is the attorney culture. For example, in the drafting of the securities laws in the 1930s, attorneys, law professors, and judges were the key figures. Today, those inside and outside the SEC see the agency's distinctive mission as one of legal development and enforcement of the securities laws, and attorneys thus constitute its most prominent profession. In a reinforcing process, the attorneys at the center of the SEC have articulated its core purposes, and those purposes in turn require the skills that they provide. While the agency also includes accountants, economists, financial analysts, and information technology specialists, these professions are present in such limited numbers that they have a much smaller influence on the operational culture of the SEC (Khademian, 1992; Seligman, 2003). Figure 3 indicates the number of positions by occupation in the SEC from 1998 through March 2009. The "Legal and kindred" category, about 90% of which is "General Attorney" in 2009 and prior years, is the largest occupational grouping. The Financial Analysis and Economist categories are a small part of the agency.

[insert figure 3 about here]

Legal experience at the SEC is a valuable asset in a career in financial market regulation. The flow of attorneys between the agency and institutions in financial markets both reflects and reinforces the shared system of public and private regulation discussed above. The Association of Securities and Exchange Commission Alumni (ASECA), for example, is one such network. It has "nearly 1,000" members, sponsors an annual dinner with awards, and gives scholarships and competitions directed to law schools and law students. "Initially formed to continue the

camaraderie that existed among ASECA members when they worked together for the SEC,” it now “provide[s] the opportunity for education and growth of industry professionals, to promote study and research in the field of securities law, and to educate members on securities law by means of lectures, seminars and publications. Gatherings also provide a forum for exchanging information and sharing ideas regarding the administration and reform of securities law” (Association of Securities and Exchange Commission Alumni, 2009). Our contacts with individuals in government and industry during the course of this research regularly referred to this association. Similarly, the SEC Historical Society is an active nonprofit organization providing a “virtual museum and archive of the history of financial regulation.” While not formally linked with the SEC, its donors, sponsors, and participants in its events include a large number of former SEC personnel, firms in financial services, and law firms. It focuses heavily on legal issues with additional attention to accounting, reflecting the distribution of activities at the SEC (Securities and Exchange Commission Historical Society, 2009).

In addition to cultural norms established by attorneys in the financial industry, cultural norms are reinforced by SEC employees who consistently rate their agency as both a prestigious institution and a highly satisfying place to work. One example of the prestige and satisfaction is the SEC’s consistent appearance among the top federal agencies in the Best Places to Work ranking of government agencies, produced by the Partnership for Public Service. The SEC was ranked as the fifth best large agency for employment in the federal government in 2005, the third best in 2007, and the eleventh best in 2009.

While prestige remains high in the eyes of the industry and employees, and while the SEC performs well relative to other federal agencies, the recent stress in the markets is beginning to show in the organization. The index scores calculated by the Partnership for Public Service

indicate a steady decline from the 2005 to the 2009 rankings. In 2005 the SEC's index score was 73.1, in 2007 the score equaled 71.9, and in 2009 the index dropped further to 66.2, for a total decrease of 9 percent.

A direct analysis of the Federal Human Capital Survey data provides additional detail beyond the secondary rankings provided by the Best Places to Work report.² In 2004, 2006, and 2008, all employees in the SEC were surveyed. Additive indices were created by the authors of this manuscript to capture employee perceptions regarding overall satisfaction, individual performance management, organizational performance management, and opportunities for training and professional development (see table 1). Survey questions were selected based on their fit with the concept and their appearance in all three waves of the survey; Cronbach's alpha was used to confirm the appropriateness of including the items in the various indices and is reported in table 1, in addition to descriptive statistics.

[insert table 1 about here]

Index means across the 2004, 2006, and 2008 survey provide details on the changes in employee perceptions during this time period (table 2). First, it is clear that 2008 was a hard year for SEC employees. All averages are down as compared to 2004 and 2006. The largest change between 2004 and 2008 occurred in the area of individual performance management. This is not surprising considering both the turmoil in the markets and significant changes made to the agency's performance appraisal and pay-for-performance system that is described below in greater detail.

[insert table 2 about here]

² The Federal Human Capital Survey is administered governmentwide bi-annually by the Office of Personnel Management. For more information about the survey, see <http://www.fhcs.opm.gov>.

These changes are further illustrated when comparing SEC index scores to those of the rest of the federal government. Satisfaction at the SEC in all three years is significantly different from all other agencies (table 3). However, the direction of the difference changes. Whereas in 2004 and 2006 SEC employees were generally more satisfied than other employees, in 2008 they were less satisfied. Additionally, the difference in organizational performance management is not significant in 2006, but the SEC's perceptions of organizational performance management are lower than at all other agencies in both 2004 and 2008.

Interestingly, no differences exist between SEC employees and the rest of the federal government in terms of training and professional development perceptions until 2008. At that point, SEC employees seem less satisfied with training and professional development than all other agency employees. This may be attributed to criticisms from outside the agency suggesting that employees are under-trained and that the agency is not preparing its employees to respond effectively in a changing market. Finally, in the area of organizational performance management, SEC employees report lower perceptions than the rest of the federal government in 2004 and 2008, but not in 2006. Agencies government-wide have been criticized for underutilizing performance information and strategic planning documents for guiding programmatic decisions (U.S. General Accounting Office 2004b); employee perceptions indicate this may be an even bigger challenge at the SEC.

[insert table 3 about here]

While the trend is downward in the face of a significant amount of environmental instability, it is remarkable that the agency continues to perform well, relative to other federal agencies, in terms of employee perceptions of the workplace. The SEC remains an organization of high prestige among employees and the financial markets community.

Personnel Instability

In addition to significant changes in the SEC's external environment, the agency has faced significant changes internally, especially in relation to personnel management. As noted previously, personnel stability is one of many contributors to organizational performance and is a critical component of management capacity (O'Toole and Meier, 2003, Selden and Jacobson, 2007). In all four areas of personnel stability—structure, obtaining employees, maintaining employees, and motivating employees—the SEC has faced a distinct lack of stability over the last decade. Specifically, the SEC implemented an alternative personnel system to be consistent with the other financial regulatory agencies outside of Title V and faces turnover rates higher than the government average. Linked in part to high turnover and in part to expanded agency resources, the agency engaged in a significant hiring spree and developed capacity to train the influx of new staff. At the same time, agency management implemented a pay for performance system, which is now being rolled out for a second time in response to a court directive. Coupling these changes with the loss of the SEC's northeast regional office in the collapse of the World Trade Center on 9/11, it is clear to see that the agency operates in a turbulent personnel environment.

Structural Instability

Over the last decade, Congress approved a number of structural changes to the pay, classification, and hiring systems at the SEC. In January 2002, the first statutory change to personnel management in the agency was enacted as part of the Investors and Capital Markets Fee Relief Act, otherwise known as the Pay Parity Act.³ This enabled the SEC to develop its own pay scale and classification system. As a result of the Pay Parity legislation, the SEC

³ Public Law 107-123, January 16, 2002.

implemented a system that “transitioned away from the General Schedule to a compensation system consisting of 17 pay grades” (Ruiz, 2008, p. 1).

Later in 2002, the SEC was granted a significant increase in staffing resources. This increase was included as part of the massive Sarbanes-Oxley legislation, passed as a response to the failures of Enron, Adelphia, and others.⁴ In a short period of time, the SEC increased its staff by one-third to respond to the new responsibilities given to the agency as a result of this legislation (Ruiz, 2008). However, the SEC experienced difficulty in hiring the newly authorized staff and thus sought additional statutory relief. The Accountant, Compliance, and Enforcement Staffing Act of 2003 provided expedited hiring authority for accountants, economists, and securities compliance examiners.⁵ Under excepted service authority, the agency was allowed to hire individuals for these positions in a manner consistent with the manner used to hire government attorneys—i.e. more quickly than under traditional merit system requirements.

Instability in Obtaining Employees

In addition to structural instability, the SEC faced significant challenges obtaining staff. Prior to the passage of the Pay Parity legislation, the General Accounting Office (GAO) reported that the SEC lost approximately one-third of its staff between fiscal years 1998 and 2000, half of whom were attorneys (United States General Accounting Office, 2001). Turnover, staffing levels, and levels of experience among staff fluctuated during this time. After a high of 13.7 percent in 2000, turnover rates appear to initially drop after the passage of the Pay Parity legislation, but then begin to fluctuate between 5.9 and 9.1 percent between 2003 and 2008 (see table 4). The SEC would prefer to have turnover rates at or below 7 percent (United States

⁴ Public Accounting Reform and Investors Protection Act of 2002. Public Law 107-204, July 30, 2002.

⁵ Public Law 108-63, July 3, 2003.

Securities and Exchange Commission, 2008). Due to turnover and significant amounts of hiring, no more than 50 percent of agency employees held 10 or more years of experience over the last decade. Employees with less than one year of experience dramatically increased with the authority to expand agency staffing levels in 2003 and 2004. Furthermore, after the staffing increases, the agency's budget was later cut, resulting in overall staffing reductions and less hiring in 2006 and 2007.

[insert table 4 about here]

The instability in hiring and retaining staff, according to a survey of current and former staff conducted by GAO in early 2001, was due mostly to compensation issues, but limited opportunities for advancement, high levels of uncompensated overtime, and the poor quality of administrative support services were also cited as reasons for leaving (United States General Accounting Office, 2001). These concerns led employees to vote in support of forming a union in July 2000 under the National Treasure Employee's Union (United States General Accounting Office, 2001). A later survey by GAO after implementation of the Pay Parity legislations indicated employees were more satisfied with their compensation, but less satisfied with the quality of supervisions and the performance appraisal system (United States Government Accountability Office, 2004).

The high turnover and constant hiring at the SEC impacted its ability to monitor the markets. In a study conducted before passage of Pay Parity legislation and Sarbanes-Oxley, the significant number of junior staff at the SEC resulted in delayed reporting, reporting of lower quality, and oversight that was both less frequent and less thorough, including an "increased focus on procedural violations rather than substantive ones" (United States General Accounting Office, 2002, p. 25).

Instability in Maintaining Employees

With the lack of stability in obtaining employees at the SEC, the agency has engaged in an expansion of its programs to maintain its employees through training and professional development. On one hand, the agency has expanded training opportunities offered internally, and these opportunities are linked to their new competency-based system. However, the agency lacks a formal knowledge management system and a completed strategic workforce plan (United States Government Accountability Office, 2006). Knowledge management systems are intended to identify the knowledge, skills, and competencies currently available in the agency. Strategic workforce plans are to identify the human capital needed for meeting the agency's strategic goals, identify the gaps between on-board talent and needed competencies, develop policies for closing the gaps, and specify performance measures for tracking progress (United States General Accounting Office, 2003). According to its annual performance and accountability reports, the SEC began and then shelved a knowledge management framework in 2006 and 2007 (United States Securities and Exchange Commission, 2007). In the same report, the agency indicated it developed but had not implemented a workforce planning system.

The SEC has expanded training opportunities available through the creation and expansion of the SEC University or SECU, despite the lack of formal information about competency needs. Since its creation in 2004, SECU has expanded each year to include courses that fill needs identified by agency executives (United States Securities and Exchange Commission, 2008). Although annual performance reports indicated evaluations of the training system have occurred, no details are provided as to the results of the evaluations and changes made as a result of the evaluations (United States Securities and Exchange Commission, 2006, 2008). Despite this expansion of agency investments in professional development opportunities,

the amount spent on training per employee per year in the agency remains well below best practices.

Instability in Methods for Motivating Employees

In addition to instability in obtaining and maintaining its employees, the SEC experienced turbulence in the manner in which it motivates its employees—turbulence that was sometime self-imposed, and at other times, imposed upon them. Specifically, the implementation of the Pay Parity changes was accompanied by changes to the performance appraisal system and the implementation of pay-for-performance. According to the annual performance reports, the pay for performance system was originally implemented in 2004 and revised in 2006 (United States Securities and Exchange Commission, 2006). The 2006 revision included the transition to a competency-based performance appraisal and the creation of the Performance and Accountability Branch within the Office of Human Resources to focus exclusively on the appraisal system and merit pay (Ruiz, 2008).

At the end of the first cycle of the new appraisal system, the union representing SEC employees filed a grievance claiming that the pay-for-performance system lacked transparency and consistency and resulted in discrimination (Ruiz, 2008). In September 2007 an arbitrator ruled that the ratings allocation in the 2003 appraisal cycle had a disparate impact on African Americans and employees over the age of 40, and called the system “subjective and discretionary” (Kelley, 2007). One year later, the SEC and its union reached a \$2.7 million settlement, used for back pay and increases to base pay for the affected employees (Gilman, 2008). A later Inspector’s General evaluation of the system found appraisals were neither performed consistently nor on time and that inadequate guidance was given to managers on how ratings should be allocated (Stachnik, 2007).

The SEC redesigned the performance appraisal system in 2006 in part due to the grievance with the union over the system and in part due to the move to a competency-based system.. The SEC has phased in the implementation of the competency-based performance appraisal system so that the system can be evaluated and revised before it is applied to all employees. During this phased implementation, pay was decoupled from performance; everyone receiving an acceptable rating was given the same pay increase.

Personnel Instability as an Opportunity for Driving Cultural Change

Despite all of the changes to the structure, rules, and make-up of personnel within the SEC, little evidence currently exists to suggest the agency has harnessed this opportunity to initiate cultural change from within, in lieu of its network demanding change. For example, performance appraisal systems, and pay-for-performance systems in particular have the potential to serve as significant drivers of cultural change. By articulating the competencies by which performance will be evaluated, the agency can use the appraisal systems to identify the long-standing behaviors worth continuing. Additionally, they can identify valuable new competencies necessary to successfully respond to changing financial markets. The placement of new competencies in the appraisal system and facilitate holding employees accountable for receiving training in these areas, and exhibiting them on a regular basis.

At this point in the research, the authors are seeking additional information from the SEC regarding the new competency-based appraisal system, so we are not yet able to forecast or hypothesize whether the new appraisal system will play a role in changing organizational culture. Additionally, because the system is being implemented agency-wide this fall, it is too soon to tell what impact it will have, if any, on reshaping the competencies and expectations of the workforce. However, agency human capital executives have expressed intentions consistent

with governmentwide guidance in this area and appear committed to evaluation and revisions of the new system during its initial implementation.

The significant amount of hiring in 2003 and 2004 represented another opportunity for bringing in additional individuals with investigative and analytical skill sets beyond those of lawyers. As noted above, the SEC engaged in that hiring spree without the benefit of a strategic or workforce plan to guide its hiring. As figure 3 illustrates, the SEC did not use the authority to change the occupational distribution of its staff. It is important to note, however, that current SEC leadership is signaling an interest in revising this occupational distribution. As noted previously, Mary Schapiro, the Chair of the SEC, made the hiring of individuals with skills in complex financial technology and financial investigations one of the key elements of her initiatives at the SEC (Schapiro, 2009). Depending on the number of people the agency can hire in these areas of need, this has the potential to contribute additionally to a cultural change in the agency.

More expansively, as the SEC and Congress consider structural changes to the agency and the manner in which it conducts its regulatory business, agency executives would benefit from the consideration of human capital issues in reform and transformation efforts. Recently there was evidence of management's acknowledgment of the importance of including human capital in such discussions. For example, Robert Khazumi, the new Director of the Division of Enforcement, announced the creation of new specialized units to focus on particularly complex areas of securities law (Khuzami, 2009). In making the announcement, he stressed the desire to capture and develop the abilities of staff with expertise in these areas, and the need to hire more individuals with relevant professional knowledge to contribute to the effort. This and other reforms in the division announced by Khazumi each include comments regarding how

employees will be used or impacted, how decision processes will be changed to enable employees to perform their work effectively, and how the opportunities will be used to develop and hire the talent needed for the division to be successful. All of this signals the beginning of a shift in the expectations of agency management that personnel issues are important to consider when embarking in change initiatives.

Discussion and Conclusion

The SEC is operating in an environment characterized by both stability and change. External to the organization and its network, the financial instruments and the organizations the SEC is tasked with regulating are becoming more complex and less transparent, to both industry insiders and the regulators themselves. At the same time, the long-standing network culture operates under a shared understanding of a stable distribution of power and jointly agreed-upon roles for different network members. While the network may be resisting or delaying change at the present time, personnel management within the SEC has been unstable in part because of the market turmoil. In multiple forums, the current SEC leadership indicates a need to fundamentally change the culture of the organization and how it does business. However, the ability of the leadership to effectively implement transformation change is dependent on both the response of its network to market pressures and the ability of the agency to include considerations of personnel management in those change efforts.

As we continue our research effort, a number of questions present themselves as worthwhile pursuits. First, we need a better understanding of the degree to which network culture influences management decisionmaking. Specifically, if a network is stable and resistant to change, what implications does that have for organizational leaders who are trying to effect change? At a more discrete level, additional analysis is necessary to determine how or if the new

performance appraisal system, and other changes to human capital management at the SEC, is used as a changing force in the organization. The publically available survey data do not allow us to make that determination currently. Furthermore, initial indications from agency executives signal a desire to engage in formal knowledge management and strategic workforce planning efforts. It is incumbent upon us to follow the agency's actions in this respect, especially as it relates to how the agency shapes the mix of skills and competencies available in the workforce to meet the needs of the changing financial markets. These systematic planning and analysis tools can help ensure the agency is investing its limited training resources wisely.

Table 1
Items used for the Indices

Index	Survey Items	Summary Statistics	2004	2006	2008
<i>Satisfaction</i>		Min	4	4	4
	My work gives me a feeling of personal accomplishment.	Max	20	20	20
	I like the kind of work I do.	Mean	15.257	15.173	15.303
	Considering everything, how satisfied are you with your job?	St. Dev.	3.442	3.418	3.42
	Considering everything, how satisfied are you with your organization?	Cronbach's alpha (C α)	0.863	0.858	0.861
<i>Individual Performance Management</i>					
	Awards in my work unit depend on how well employees perform their jobs.	Min	4	4	4
	In my work unit, differences in performance are recognized in a meaningful way.	Max	20	20	20
	My performance appraisal is a fair reflection of my performance.	Mean	13.549	13.235	13.278
	Supervisors/team leaders provide employees with constructive suggestions to improve their job performance	St. Dev.	3.505	3.564	3.677
		C α	0.833	0.836	0.85
<i>Organizational Performance Management</i>					
	Managers communicate the goals and priorities of the organization.	Min	2	2	2
	Managers review and evaluate the organization's progress toward meeting its goals and objectives.	Max	10	10	10
		Mean	7.100	7.002	7.060
		St. Dev.	1.923	1.939	1.964
		C α	0.874	0.878	0.891

Table 1 cont.

Training and Professional Development

The workforce has the job-relevant knowledge and skills necessary to accomplish organizational goals.	Min	6	6	6
The skill level in my work unit has improved in the past year.	Max	30	30	30
Supervisors/team leaders in my work unit support employee development.	Mean	21.541	21.451	21.717
Employees have electronic access to learning and training programs readily available at their desk.	St. Dev.	4.371	4.414	4.45
My training needs are assessed.	C α	0.819	0.824	0.832
How satisfied are you with the training you receive for your present job?				

Table 2
 Securities and Exchange Commission Perceptions in 2004, 2006, and 2008

	2004	2006	2008
Satisfaction	15.614 (3.373)	15.559 (3.458)	15.062 (3.589)
Individual Performance management	13.217 (3.650)	13.348 (3.687)	12.401 (3.836)
Organizational performance management	6.874 (2.000)	7.018 (3.011)	6.751 (2.078)
Training and skills development	21.409 (4.096)	21.609 (4.401)	21.230 (4.503)

Standard deviations are presented in parentheses.

Table 3

Difference of Means: Securities and Exchange Commission and All Other Agencies

	All Other Agencies	SEC	T-value
2004			
Satisfaction	15.252	15.614	-4.851
Individual Performance management	13.554	13.217	4.441
Organizational performance management	7.103	6.874	5.504
Training and skills development	21.543	21.409	1.417
2006			
Satisfaction	15.169	15.558	-4.947
Individual Performance management	13.234	13.348	-1.388
Organizational performance management	7.001	7.018	-0.380
Training and skills development	21.449	21.609	-1.568
2008			
Satisfaction	15.305	15.062	2.833
Individual Performance management	13.285	12.401	9.599
Organizational performance management	7.063	6.751	6.325
Training and skills development	21.721	21.230	4.406

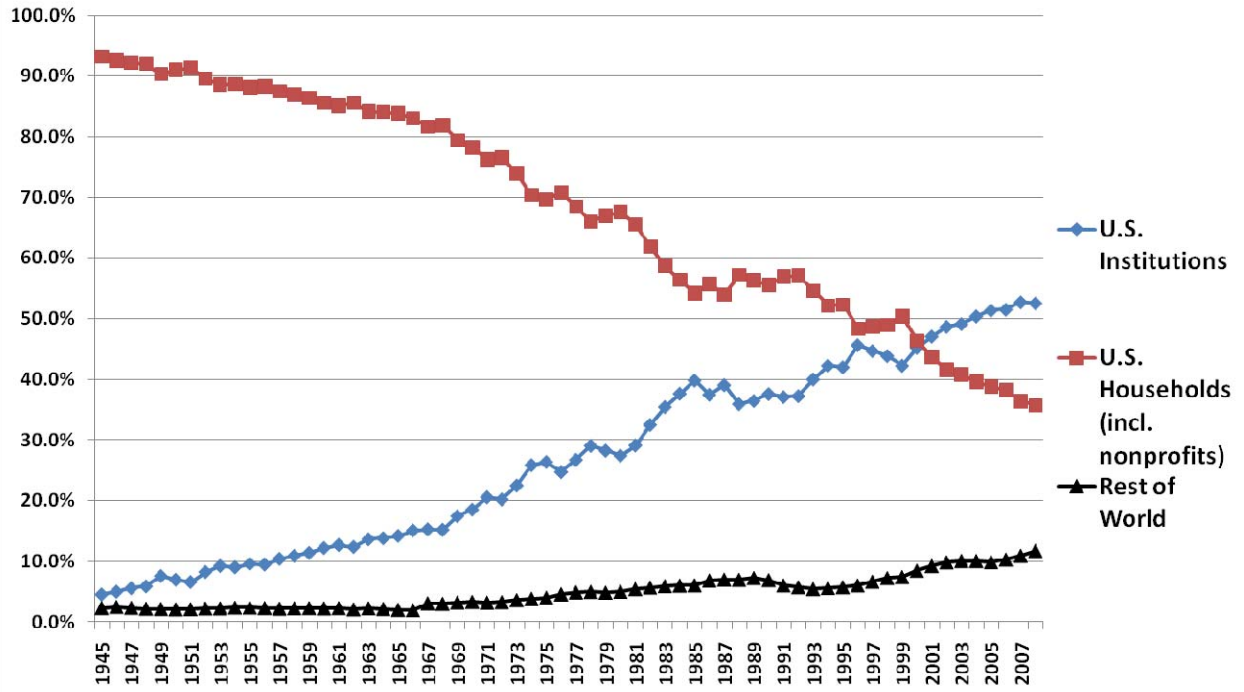
Table 4
 SEC Employees Years of Experience and Turnover Rates, 2000-2008

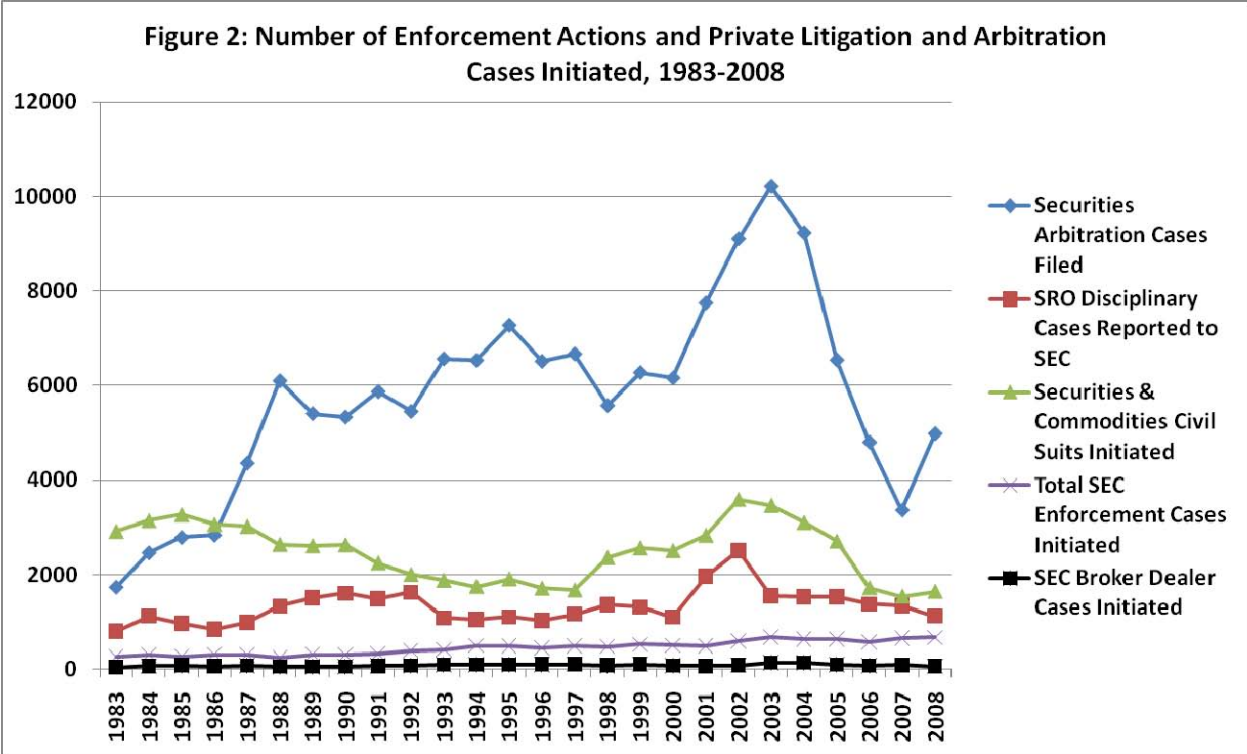
Year	Percent of employees with specific levels of experience					% Turnover (1)	Total Staff
	Less than 1 yr.	1-2 yrs	3-4 yrs	5-9 yrs	10 + yrs		
2000	11.7	14.1	9.2	19.2	45.8	13.7	2952
2001	8	17.3	9.9	18	46.9	9.1	3049
2002	3.1	16.7	12.4	17.9	49.9	5.8	3027
2003	9.4	9.1	14.6	19.3	47.6	5.9	3256
2004	14.5	10.7	12.3	19.6	42.8	6.3	3797
2005	7.7	20.3	7.4	20.7	43.8	7.5	3907
2006	1.2	18.5	9.8	23	47.5	9.1	3598
2007	4.7	6.6	18	21.2	49.5	8.6	3498
2008	7	5.4	16.7	22.6	48.4	6.2	3631

Experience reported at www.fedscope.opm.gov

1) Reported in the SEC Annual Performance Reports

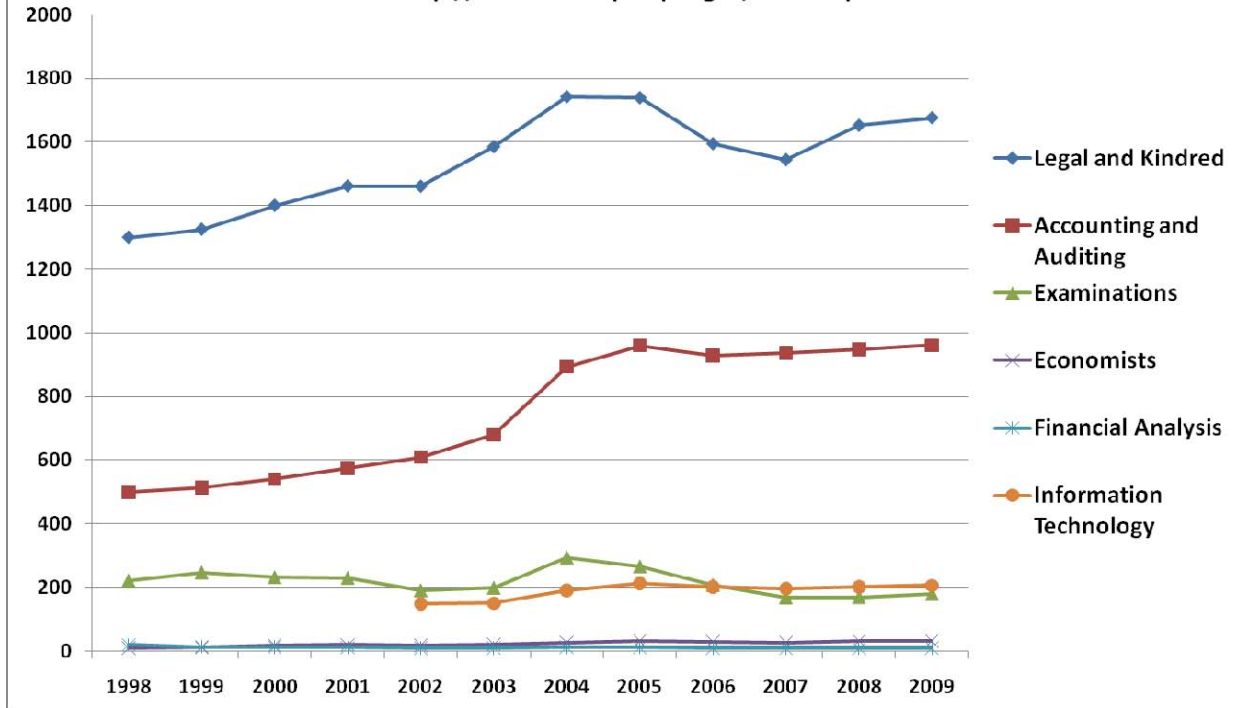
Figure 1: % Holdings of U.S. Corporate Equities 1945-2008 (Source: Source: Compiled from Table L100, June 11 2009 Release www.federalreserve.gov/datadownload/Choose.aspx?rel=Z.1)





Source: Securities arbitration data from Securities Industry Conference on Arbitration, FINRA, and NYSE. SRO disciplinary cases from SEC annual reports and FINRA and NYSE websites; data beyond 2003 include only FINRA/NASD and NYSE, excluding some smaller SROs, and so not strictly comparable to earlier data. Civil suit data are from Administrative Office of United States Courts, and SEC data from SEC annual reports. Civil suit and SEC enforcement data are fiscal year or otherwise not calendar year data. Detailed information on data sources is available from d.mccaffrey@albany.edu.

Figure 3: Number of Positions By Occupation, Securities and Exchange Commission, 1998-2009 (1998-2008 are September data, 2009 reference is March) Source: <http://www.fedscope.opm.gov/index.asp>



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