

December 20, 2023

Melinda Grant, Undersecretary  
California Business, Consumer Services and Housing Agency  
500 Capitol Mall, Suite 1850  
Sacramento, CA 95814

Dear Undersecretary Melinda Grant,

In accordance with the State Leadership Accountability Act (Leadership Accountability), the Department of Real Estate submits this report on the review of our internal control and monitoring systems for the biennial period ending December 31, 2023.

Should you have any questions please contact Marcus McCarther, Chief Deputy Commissioner, at (916) 576-8775, [marcus.mccarther@dre.ca.gov](mailto:marcus.mccarther@dre.ca.gov).

## **GOVERNANCE**

### **Mission and Strategic Plan**

#### **Mission:**

The mission of the California Department of Real Estate (DRE) is to safeguard and promote the public interests in real estate matters through licensure, regulation, education and enforcement.

#### **Vision:**

To be the champion for public protection in real estate.

#### **Strategic Goals:**

##### **Goal 1: Customer-centric Service**

Our primary focus is on real estate consumers and customers. Protecting their interests drives industry confidence economic vitality, and forms the foundation where all Californians live, work, and play. We build towards our reputation as the best consumer protection and customer empowerment department through our exemplary and consistent actions.

#### **Objectives:**

1. Consistently deliver timely, quality, and courteous experiences for external and internal customers.
2. Scan for and anticipate emerging opportunities and trends that will enhance consumer protection.
3. Improve the review and regulation of subdivisions and timeshares.

4. Build upon effective licensing programs to ensure industry competence that continuously improves consumer protection.
5. Increase regulatory compliance through proactive outreach and effective enforcement.

### **Goal 2: Healthy Organization**

We are a talented team of consumer protection champions. We achieve our mission and power our other strategic goals by deliberately investing in an inclusive, collaborative, and engaged workforce.

#### **Objectives:**

1. Be an engaged workforce through commitment, communication, learning, career advancement, retention, and recruitment.
2. Improve how leaders and employees manage dynamic workloads to align priorities and capacity.
3. Cultivate a respectful and inclusive culture that leverages diversity as a strategic strength.
4. Foster an adaptable hybrid workplace where we continuously evolve how we collaborate.

### **Goal 3: Innovative Operations**

We are re-imagining our processes and technology to embrace innovation. Our teams leverage lean methods and modern tools to continuously improve the delivery of results.

#### **Objectives:**

1. Expand adoption of digital solutions for high-volume and routine services to increase self-service, enhance functionality, and efficiency.
2. Streamline processes that require manual intervention by addressing key bottlenecks.
3. Strengthen program knowledge and continuity with updated and easily referenced standards and procedures.
4. Continually seek opportunities to update our operations to align with legislative and market changes.
5. Prepare for the future and reduce risks by enhancing the use of and modernizing our mobile and core technologies.

### **Goal 4: Resourceful Stewardship**

We leverage our resources to perform at the highest level possible. Our resources include our people, budgets, facilities, data, and technology assets. As stewards of these resources, we make wise investments and transparently track our impact according to our strategic priorities.

#### **Objectives:**

1. Expand the fiscal awareness of our individual and interconnected budgets.
2. Proactively monitor and reallocate vacant positions to the place of highest need.
3. Evaluate utilization of resources and propose solutions to ensure adequate

workforce and technology capacity.

4. Evaluate and align service level capacity with allocated budgets and forecasted fee revenue.
5. Adapt facilities and technologies to enable a new hybrid of onsite, field, and remote workforce.

### **Control Environment**

The Commissioner of the Department of Real Estate, Doug McCauley, is responsible for the overall establishment and maintenance of internal controls, along with the effective and objective ongoing monitoring of these controls.

### **Integrity and Ethical Values**

The executive management of DRE establishes the culture and attitude regarding the importance of maintaining internal controls and sets the expectation of standards of conduct within the organization, which is "the tone at the top."

The executive management is fully committed to the values of integrity, ethical practice and the safeguarding of assets and has developed systems of oversight and review to assure proper standards are maintained and followed. Examples of management's commitment to internal controls can be demonstrated through adherence to control environment principles, as follows:

Management is committed to integrity and ethical values, as required by adherence to the DRE's published Conflict of Interest statement. All employees who speak or attend events on behalf of DRE do not accept gifts or honoraria. This restriction is also noted on DRE's speaker request forms. The prohibition on the acceptance of gifts also applies to all employees in their performance of daily work duties. Management maintains segregation of duties over tasks such as travel expense claim handling and purchasing, while expenses such as rental cars and airline tickets require authorization by the employee's supervisor/manager and DRE's Chief Deputy Commissioner. Many of DRE's employees are required to file an annual Form 700 - Statement of Economic Interests and take a biennial Ethics Training Course. This is all part of setting "the tone at the top."

The Chief Deputy Commissioner, Assistant Commissioners (Executive Management), managers, and supervisors are primarily responsible for identifying the compliance risks and internal controls for their operational areas. In addition, individual employees have responsibility for evaluating, establishing, improving, and monitoring internal controls for their areas of responsibility and accountability.

### **Core Values**

- **Excellence:** Develop the flexibility and resilience to deal with change, challenges, and uncertainty so that our employees continue to provide timely,

- professional, effective, and efficient service to all customers.
- **Professionalism:** To continue to communicate effectively, ethically, and appropriately to always find a way to be productive.
  - **Knowledge:** To continue to find sources to improve our workflow to increase productivity, nurture teamwork and trust relationships between management and our employees.
  - **Communication:** We continue to strive for effective communication to boost teamwork and customer service, ensuring that management and the team are on the same page.
  - **Caring:** We work with our stakeholders as partners to support mutual understanding of ideas and open exploration of our differences. We continue to ensure our employees and customers feel appreciated and valued.

### **DRE Oversight Structure**

The Department of Real Estate has implemented and documented the ongoing monitoring processes as outlined in the monitoring requirements of California Government Code sections 13400-13407. These processes include reviews, evaluations, and improvements to the DRE's systems of control and monitoring.

In 2022, DRE established a dedicated Internal Audit Unit (IAU). The IAU upholds its autonomy by directly reporting to the Commissioner and Chief Deputy Commissioner. IAU provides management with insights into the quality and effectiveness of internal controls, along with assessing the quality of operational performance in comparison to established standards. The audit procedures are crafted to determine the presence and proper functioning of internal controls while also pinpointing any inefficiencies. DRE undergoes regular audits conducted by the Department of Technology and Military Department in relation to Information Technology operations and security. Audits from the Department of General Services, Department of Finance, CalHR, and State Personnel Board are also conducted to assess administrative functions.

### **Ability to Report Ethical Concerns**

Annually, employees are notified about the Whistleblower Protection Act through email and posted flyers in all offices. Reports of improper activities by DRE employees can be submitted directly to the IAU, through the California Whistleblower Hotline managed by the California State Auditors (CSA), as well as through their supervisor, Equal Employment Opportunity (EEO) officer or Human Resources (HR) channels. The IAU is equipped to receive complaints against DRE employees through direct contact or referrals from the Bureau of State Audits' Whistleblower Hotline.

The IAU is responsible for responding to complaints received from the CSA "Whistleblower Hotline." When a complaint is received from CSA, a determination is made as to whether the IAU or management in the affected program will conduct the investigation. The determination is based on past experience, materiality of the issues

and/or the position of the individual(s) involved in the complaint.

### **Organizational Structure to Ensure Appropriate Level of Responsibility**

DRE comprises nine divisions and each division is led by an Assistant Commissioner, with management and supervisory levels beneath. Additionally, DRE has an independent EEO officer that reports directly to the DRE Commissioner.

### **Establishing and Maintaining Competent Workforce**

As a result of DRE's recent Workforce Analysis and Succession Planning, an Action Plan has been submitted to CalHR to address identified gaps and risks. These initiatives include:

- **Knowledge Transfer Initiatives:** DRE is focusing on employee training and professional development, aligning leadership training with succession management. They are creating tools and resources to identify potential future leaders, developing individual career plans, and launching a new Learning Management System called SOLD. The department promotes a culture of knowledge-sharing through webinars and workshops and is actively documenting policies and procedures to close knowledge gaps. Additionally, a new onboarding and New Employee Orientation program has been implemented to assist supervisors and acclimate new employees.
- **Retention Initiatives:** DRE is addressing employee needs by reviving and updating its recognition program, allowing for electronic peer-to-peer and supervisory-to-staff recognition. Recognizing the importance of feeling valued, the program emphasizes both business recognition and personal gestures like day-to-day kudos and birthday well-wishes. Additionally, the Upward Mobility Program aims to support the development and advancement of employees in low-paying occupations, providing opportunities for career growth within DRE and enhancing their knowledge, skills, and abilities to meet organizational needs.
- **Succession Management Initiatives:** DRE is set to establish a formal Executive Mentorship Program (EMP) with clear goals to facilitate the transfer of tacit organizational knowledge not covered in training. They also plan to implement Executive Enrichment, offering Succession Management Participants opportunities to engage in work beyond their usual functions and enhance their understanding of DRE operations.

### **Information and Communication**

The outcomes of external audits from government entities are communicated to both management and the IAU for risk assessment and internal review or audit purposes. The results of the SLAA department-wide Risk Assessment were documented and shared with the Commissioner and Deputy Commissioner, serving as a foundation for the formulation of the new biennial audit plan.

DRE facilitates organization-wide information sharing via All-Staff Meetings conducted on Microsoft Teams, featuring participation from all executive management. Prior to these meetings, a survey is distributed to all employees, allowing them to submit topics or questions for management. Employees also have the opportunity to pose questions during the event. Additionally, routine information sharing occurs and is archived on the Intranet news page, known as eConnect.

Communication with external stakeholders primarily takes place through DRE's public website and its social media platforms. The DRE's website provides resources for filing complaints, accessing consumer alerts, guides, publications, forms, and license information.

DRE employees can report inefficiencies and inappropriate actions to management through the IAU, their supervisors/managers, EEO officer, and/or HR.

## **MONITORING**

The information included here discusses the entity-wide, continuous process to ensure internal control systems are working as intended. The role of the executive monitoring sponsor includes facilitating and verifying that the Department of Real Estate monitoring practices are implemented and functioning. The responsibilities as the executive monitoring sponsor(s) have been given to: Marcus McCarther, Chief Deputy Commissioner.

Management oversees the internal control system through ongoing monitoring and periodic internal and external evaluations. Executive Staff convene biannually to discuss internal controls, risk assessment, and monitoring processes. Program Managers conduct annual meetings to educate staff on the State Leadership Accountability Act, highlighting the importance of each employee in the internal control structure. Any deviations are to be reported through the employees' chain of command.

In addition to the establishment of the IAU, DRE undergoes audits from various entities, including the Department of General Services, CalHR, Department of Technology, the Military Department, State Personnel Board, and California State Auditors in case of a whistleblower complaint.

The IAU will perform routine reviews of all identified risks to address and mitigate potential gaps. When a risk is identified, the Assistant Commissioner of the division takes responsibility for developing a plan to manage or eliminate the risk, including an estimated completion date. The IAU conducts follow-ups to ensure the plan is completed and objectives are met.

## **RISK ASSESSMENT PROCESS**

The following personnel were involved in the Department of Real Estate risk assessment process: executive management, middle management, front line management, and staff.

The following methods were used to identify risks: brainstorming meetings, employee engagement surveys, ongoing monitoring activities, audit/review results, other/prior risk assessments, external stakeholders, questionnaires, consideration of potential fraud, and performance metrics.

The following criteria were used to rank risks: likelihood of occurrence, potential impact to mission/goals/objectives, timing of potential event, potential impact of remediation efforts, and tolerance level for the type of risk.

## **RISKS AND CONTROLS**

### **Risk: Risk 1: Financial Sustainability**

The DRE is currently facing a declining fund balance, leading to a growing gap between revenue and operational costs. With an annual deficit of approximately \$8.4 million and a cost recovery level of 86%, DRE's revenue is insufficient to cover operational expenses, including facility costs, salaries, benefits, and increased costs of goods and services.

#### **Control: DRE 's Strategic Cuts and Conservative Spending for FY 2023-24**

The Department of Real Estate (DRE) expects to fully expend its appropriated spending authority for FY 2023-24. In an effort to balance the budget, DRE intends to make significant cuts to discretionary spending and resources including restrictions on supplies, travel, training, new contracts and hiring. DRE prepared a very conservative spending plan which includes several notable expenses: roughly \$800,000 in one-time costs associated with DRE's move to the Richards Boulevard Office Complex (RBOC) and \$700,000 to accommodate pending retirements.

#### **Control: DRE's Fee Study**

The long-term fiscal projections for DRE identify a declining fund balance. DRE's revenue is not keeping pace with the cost of operations. These increasing costs include facilities, salaries and benefits, and the general overall increased costs of goods and services.

Given this outlook, DRE conducted a "fee study." In March of 2022, DRE contracted with a vendor to initiate this process. At the conclusion of the evaluation, the findings revealed an annual deficit of approximately \$8.4 million or a cost recovery level of 86%. DRE's current fees are set at their statutory maximum, therefore the only way to increase them is to prepare and request legislative changes. DRE's request will be to adjust fees for adequate cost recovery. If approved, DRE would begin collecting the new fees in fiscal year 24/25. If DRE does not address the cost recovery issues, DRE is projected to be insolvent by FY 2025-26.

### **Risk: Risk 2: Staffing and Knowledge Drain**

As a result of DRE's current financial challenges, the department implemented case-by-case evaluations for hirings, using whether the position is mission critical as a key factor. The hiring restriction, combined with multiple vacant positions in Licensing, Audits, Enforcement, and Legal and the inability to hire and offer promotions to internal staff, has resulted in staff leaving the department, taking critical knowledge and skills with them. This poses a significant risk to meeting DRE's goals and impairs the ability to provide timely and efficient services to stakeholders and consumers.

### **Control: Managing Resources, Prioritizing workloads, and Updating Manuals**

- **Licensing:** To address the processing delays, licensing has taken several measures:
  1. Licensing currently is asking for other divisions to loan staff (1 to 2 days per week) to assist with processing of which they will need the appropriate training.
  2. Licensing staff have expressed valid concerns regarding their growing workloads. In response, management has proactively engaged in discussions with various licensing sections to convey our unwavering support.
- **Audit:** Audits is prioritizing audit types, with a continued emphasis on investigative audits generated from the public. However, proactive audits based on risk assessments may decline due to staff focusing on investigative audits. While Audits does have a select group of experienced auditors, many of the most seasoned professionals are nearing retirement. This poses concerns about their availability to train new staff when hiring becomes possible again.
- **Enforcement:** Enforcement employs existing manuals and guides for staff reference. There is also a working group actively drafting a manual for Enforcement management (anticipated completion date is October 2023). Management engages with staff regularly to ensure they are connected, providing any needed resources and guidance on work.
- **Legal:** Legal has temporarily redistributed workloads among existing employees, which serves as a short-term. However, if not addressed in the long term, it may pose limitations. In addition to employee retirements and departures, Legal routinely maintain and update the attorneys' and secretaries' manuals. Nevertheless, Legal has yet to review and update them specifically to address knowledge gaps arising from employee departures.

### **Risk: Risk 3: Lack of Diversity, Equity, and Inclusion (DEI) in the Strategic Plan**

The current DRE Strategic Plan does not align with Executive Order N-16-22, which emphasizes DEI practices and community engagement. This is attributed to the Strategic Plan developed prior to the announcement of the governor's Executive Order. The Executive Order specifically requests the inclusion of inclusive practices, as well as active engagement and input gathering from marginalized communities affected by our department's policies and programs.

### **Control: DRE and BSCH Collaborate on Executive Order Implementation**

DRE, in collaboration with the BSCH agency, is actively engaged in the implementation of the Executive order. To effectively steer this process, an action plan encompassing five key priorities has been established. Regular meetings between DRE and the BSCH agency are being held to ensure coordinated progress. The requirement of the Executive Order will be incorporated into the next DRE Strategic Plan.



**Risk: Risk 4: Outdated Program Manuals**

Certain programs still require updates to their manuals, posing an ongoing risk exacerbated by the hiring restriction and the importance of knowledge transfer.

**Control: Manual Updates**

Programs are actively working on updating their manuals. The IAU will continue to follow up with programs to ensure timely completion.

**CONCLUSION**

The Department of Real Estate strives to reduce the risks inherent in our work and accepts the responsibility to continuously improve by addressing newly recognized risks and revising risk mitigation strategies as appropriate. I certify our internal control and monitoring systems are adequate to identify and address current and potential risks facing the organization.

Douglas R. McCauley

**Chika Sunquist, Real Estate Commissioner**

CC: California Legislature [Senate, Assembly]  
California State Auditor  
California State Library  
California State Controller  
Director of California Department of Finance  
Secretary of California Government Operations Agency