

December 03, 2019

Alexis Podesta, Secretary  
California Business, Consumer Services and Housing Agency  
915 Capitol Mall, Suite 350-A  
Sacramento, CA 95814

Dear Ms. Alexis Podesta,

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, 2019.

Should you have any questions please contact Sandra Knau , Acting Real Estate Commissioner, at (916) 576-8776, Sandra.Knau@dre.ca.gov.

## **GOVERNANCE**

### **Mission and Strategic Plan**

The mission of the Department of Real Estate (DRE) is to safeguard and promote the public interests in REAL ESTATE MATTERS through licensure, regulation, education and enforcement. The strategic goal areas for the DRE include:

- Licensing
- Enforcement
- Legal
- Audits
- Subdivisions
- Information Technology Services
- Communication & Publications
- Legislation
- Organizational Effectiveness

### **Control Environment**

The philosophy, attitude and actions of Department of Real Estate (DRE) management regarding the importance and existence of control system within the organization defines its control environment. 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 control environment provides the discipline and structure for the achievement of the primary objectives of the system of internal controls. The DRE's control environment includes the following principles:

- Demonstrating a commitment to integrity and ethical values

- Maintaining management oversight of the internal control system
- Establishing organization structure, authority, and responsibility to pursue business objectives
- Demonstrating a commitment to attract, develop, and maintain competent people
- Maintaining accountability for the internal control responsibilities

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 a "the tone at the top."

Management's oversight over the internal control system is achieved through the establishment of policies and procedures and review of activities by managers and supervisors to assure adherence to these standards. Policies and procedures are put in place to minimize risks identified by management. Risks in specific programs are identified through polling of management staff. These policies and procedures are communicated to staff in writing and then managers and supervisors are assigned responsibility to monitor adherence to these policies and procedures.

Management has established structures, reporting lines, and appropriate authority and responsibility in the pursuit of its objectives. It is critical that management delegate authority and define responsibilities at the various levels of the organization. To assure the standards of conduct are being adhered to across all levels of DRE, management evaluates the directives, attitudes, and behaviors of individuals and groups. Evaluations may consist of ongoing monitoring. Individuals can also report issues through regular staff meetings or through their supervisor.

DRE has demonstrated a commitment to attract, develop, and retain competent individuals in alignment with its objectives. Monitoring staff competence is very important in maintaining a system of internal control, and evaluation should not be limited to the hiring process. Instead, competence is something that should be nurtured and reinforced through an ongoing plan to develop and train employees.

An example of this commitment can be shown through DRE's strategic plan goals on providing and increasing training on various programs such as Legal, Enforcement, and Audits.

The Chief Deputy Commissioner, Program Managers (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.

## Information and Communication

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The DRE is the State agency that (1.) licenses, regulates, and disciplines real estate agents, and those residential mortgage loan originators who have obtained an endorsement to their real estate license, (2.) investigates and commences action against unlicensed persons acting as or in the capacity of real estate licensees, (3.) enforces the statutory laws known as the Subdivided Lands Act relative to the qualification of offerings for the initial public sale, lease or financing of new residential subdivision properties through the issuance of public reports, (4.) oversees the Vacation Ownership and Time-Share Act, (5.) administers a consumer recovery account program for victims of licensees, and (6.) otherwise safeguards and promotes the public interests and consumer protection in real estate matters.

The mission of the DRE is to safeguard and promote the public interest in real estate matters through Licensure, Regulation, Education, and Enforcement.

#### Transition to Department Status

Senate Bill 173, signed by Governor Brown on October 15, 2017, removed the Bureau of Real Estate from bureau status under the Department of Consumer Affairs (DCA) and returned it to department status under the Business, Consumer Services and Housing Agency, effective July 1, 2018. The newly created Department of Real Estate had to commence the hiring process to fill 18 positions needed to rebuild its Fiscal/Budget, Human Resources, Legislation, Publications and Communications, and Information Security functions. The filling of these positions was critical to performing the functions required of a department in State government, including:

- Establishment of a separate budgeting and accounting capability in the new statewide Fi\$Cal system;
- Ability to engage in hiring, disciplinary, labor relations and other personnel-related proceedings;
- Capability of evaluating the effect of proposed legislation on consumers and the real estate industry, and provide technical input on proposed legislation;
- Preparing consumer and industry advisories, alerts, forms and articles, and publishing of the Real Estate Law Book, quarterly Real Estate Bulletins, as well as updating of policy and recovery plan manuals;
- Protecting private information and ensuring that our information security practices and reporting are in full compliance.

#### Accounting Reports

The Bureau of Real Estate was transitioned onto the new Fi\$Cal system as a part of the DCA, effective July 1, 2017. Effective July 1, 2018, the DRE was separated from the DCA in Fi\$Cal, becoming a separate departmental unit. The challenges facing DRE were related to Fi\$Cal being able to hire employees with experience in the new system as part of the rebuilding of our Budget/Fiscal section, and to create timely budget and accounting reports that can be utilized in making sound financial decisions. Accessibility to budget and accounting reports lagged several months after completion of month-end (or fiscal year-end), inhibiting decision-making on fiscal matters. The DRE, as a one fund department, has strived to build timely accounting reporting through the hiring of key experienced staff.

Management obtains relevant data from numerous sources depending upon the program area. For example, in the DRE's Licensing Program to ensure real estate exams accurately describe current industry practice, DRE's Examination Administration and Development Unit in agreement with the Office of Professional Examination Services completed two phases of an examination validation study.

The completed occupational analysis phase identified the knowledge, skills, and abilities that are a necessary part of the practice of real estate so they may be reflected in the real estate licensing examinations. This task required the assistance of industry practitioners to help define the scope of the practice of real estate in California through a survey which is then used to develop a current occupational analysis. The second phase of the examination validation study consisted of written examination development. This task also involved the participation of industry subject matter experts who revised and created examination items that reflect the results of the new occupational analysis. Additional phases of the examination validation study will continue throughout 2019–20 and beyond.

DRE has increased reliance upon technology to communicate information necessary to achieve its objectives. DRE has made a significant investment in information technology solutions that promote efficiency and productivity in its operational functions. DRE's information technology infrastructure is composed of five core systems: Enterprise Information System (EIS), the Licensing (Masterfiles) Imaging System, the Electronic Exams System, the Application Center System, and the Web Systems. Externally, the DRE Website is the point of entry for the online Licensing system (eLicensing) which enables DRE's clientele to complete license renewals, various license and examination change transactions, and schedule examination dates via the Internet. DRE's ITS staff also developed an online application for subdividers and their authorized agents to submit an application and supporting documentation for a public report through the internet. To protect data, DRE servers have recorded images on CD, firewalls are used to protect the infrastructure, all servers, personal computers, and laptops have updated antivirus software installed and backup devices containing the server backups are stored at a secure, off-site facility.

Internally, DRE's core business processes depend on a complex infrastructure that is crucial to its ongoing operations. The five business processes are:

Licensing (includes Licensing Services and Exams, Education and Research)

Subdivisions

Enforcement (includes Enforcement, Audits, Legal, Recovery, and Mortgage Lending)

Administration (includes support programs) and,

Legislation and Public Information (including Records Management).

Employees can report inefficiencies and inappropriate actions to their supervisor, Human Resources or EEO officer. In addition, DRE has a Send Us Your Suggestions email that is forwarded to Executive Management for review.

## **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:  
Tom Cameron, Assistant Commissioner, Audits.

Management monitors the internal control system through ongoing monitoring and separate outside

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evaluations. Biannually, the Executive Staff meets and discusses internal controls, risk assessment and monitoring processes. For example, there are processes in place in DRE's Enterprise Information System where an email is sent to a log file or recipient to notify them of an error condition.

Program Managers have annual meetings to inform staff of the State Leadership Accountability Act and to emphasize each employee's importance in the internal control structure. Any deviations should be reported through the employee's chain of command.

DRE is audited by several entities including the Department of General Services, CalHR, and the Military Department. DRE has Tier 2 purchasing authority through Department of General Services for competitive and non-competitive bids and leveraged procurement agreements. In addition, DRE has separation of duties forms with Fi\$Cal. Any items needing correction during these audits are monitored by the Acting Real Estate Commissioner or the Assistant Commissioner, Audits.

## **RISK ASSESSMENT PROCESS**

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

The following methods were used to identify risks: brainstorming meetings, ongoing monitoring activities, audit/review results, other/prior risk assessments, and consideration of potential fraud.

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

## **RISKS AND CONTROLS**

### **Risk: Call Center - High Phone Call Volumes**

The Department of Real Estate will continue to experience high phone call volumes and long phone wait times, adversely affecting customer service.

#### **Control: A**

Licensing personnel are redirected to answer calls when call volume or call wait times are high.

#### **Control: B**

The DRE's Virtual Control Center (VCC) system directs callers to the appropriate section. The new system provides better reporting and can accommodate more daily calls.

#### **Control: C**

DRE has requested a Budget Change Proposal (BCP) for more staff in the Licensing Information Section to reduce call wait times.

#### **Control: D**

DRE to enhance eLicensing system to handle more electronic transactions.

### **Risk: IT Vulnerabilities**

There are IT vulnerabilities due to external attacks and security failures that expose information assets, including personal information/privacy.

#### **Control: A**

Each DRE staff member will be responsible for meeting published IT standards of behavior.

#### **Control: B**

Program area managers are responsible for assuring staff compliance with IT policies.

#### **Control: C**

IT security of each system will be the responsibility of IT custodian. The direction of the custodians is the responsibility of the IT Systems Administrator.

#### **Control: D**

DRE continually monitors IT controls through ISO reviews.

### **Risk: Staff Training**

Lack of training in changes to the Real Estate Law, Regulations and investigative techniques threaten our ability to properly determine or judge violations of law. There is a lack of training because specific classes are not available and staff do not have always have sufficient time. The complexity of the Real Estate Law and insufficient job shadowing has created different policies at our 5 District Offices.

#### **Control: A**

This risk can be mitigated through the use of updated enforcement manuals and program procedures. Additionally, assessments can be conducted with staff, manager meetings and training by legal.

#### **Control: B**

The use of updated audit manuals and program procedures can mitigate this risk. Additionally, assessments can be conducted with supervisor, staff meetings and training by legal.

#### **Control: C**

This risk can be mitigated through the use of updated legal manuals and program procedures. Additionally, assessments can be conducted with manager and staff meetings.

### **Risk: Succession Planning**

In the coming few years, the DRE will experience the loss of subject matter experts, so there is a need to succession planning.

**Control: A**

Continue to develop desk manuals for crucial positions.

**Control: B**

Continue to ensure key persons mentor other in processes.

**Risk: Case Management**

DRE has staff and management located in offices statewide and faces challenges in maintaining and applying consistent interpretations of the numerous California Real Estate Laws and Regulations. This has caused inconsistent processes regarding case management between offices and regions in DRE's Statewide Programs resulting in ineffective decisions.

**Control: A**

The DRE currently has Enforcement, Audit, Subdivision, and Legal manuals and program procedures. Best processes will be documented. Process mapping will occur where necessary.

**Risk: Physical Security**

Physical security shortcomings expose information assets on computers, including personal information/privacy, which could result in identity theft.

**Control: A**

The department maintains and will continue to update policies on security practices related to case files, HR files, fiscal files, laptops, as well as exam security practices. Additionally, the department will ensure there are security procedures for case file handling, and develop procedures for staff receiving new laptops.

**Control: B**

The department will lock up any mail received that contains checks. Credit/debit card information received electronically will come through secured channels. We will also ensure safe storage of information upon receipt and after processing.

**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.

**Sandra Knau , Acting Real Estate Commissioner**

CC: California Legislature [Senate (2), Assembly (1)]  
California State Auditor  
California State Library  
California State Controller  
Director of California Department of Finance  
Secretary of California Government Operations Agency