

December 18, 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 Business Oversight 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 Chris Shultz, Chief Deputy Commissioner, at (916) 616-7408, [Chris.Shultz@dbo.ca.gov](mailto:Chris.Shultz@dbo.ca.gov).

## **GOVERNANCE**

### **Mission and Strategic Plan**

The DBO serves as the state's primary regulator of financial services, products and professionals, and provides protection to consumers and services to businesses engaged in financial service transactions. At the end of 2019, the DBO maintained oversight of 23 financial service industries. Its regulatory purview extends over domestic and foreign banks, industrial banks, credit unions, payday lenders, mortgage lenders, originators and servicers, finance lenders, escrow companies, broker-dealers and investment advisers, money transmitters (Western Union, PayPal and others), as well as premium finance companies, student loan servicers, business and industrial development corporations, check sellers and trust companies. The DBO has two primary regulatory responsibilities: protect consumers and protect the health of financial-service markets.

The DBO's regulatory authority and its licensees are governed by the California Financial Code and Corporations Code. The DBO's FY 2018-19 budget totaled \$101.1 million and authorized 660 positions. The DBO is funded entirely with special funds derived mainly from fees paid by licensees. The DBO was formed July 1, 2013 pursuant to the Governor's Reorganization Plan No. 2 (GRP 2) with the consolidation of the Department of Corporations (DOC) and the Department of Financial Institutions (DFI).

#### **Mission:**

Serve Californians by effectively overseeing financial service providers, enforcing laws and regulations, promoting fair and honest business practices, enhancing consumer awareness, and protecting consumers by preventing potential marketplace risks, fraud and abuse.

#### **Strategic Plan Goals & Objectives:**

**Goal 1.** Be a leading financial services regulator protecting consumers and supporting financial security.

- **Objective 1**, Licensing: Help ensure a competitive, safe financial services market through timely, well-grounded and consistently applied licensing decisions.
- **Objective 2**, Examinations: Ensure licensees' safety and soundness, and compliance with consumer protection laws, through thorough examinations, effective monitoring of new licensees, and consistent coordination with the Enforcement and Legal Divisions.
- **Objective 3**, Enforcement: Maintain an effective deterrent presence that provides strong protection for consumers and keeps licensees safe and financially sound.
- **Objective 4**, Customer Services: Secure the confidence of consumers, licensees and the public, and help consumers make more informed decisions in the financial services market.
- **Objective 5**, Public Relations: Make DBO the No. 1 name in financial services regulation for consumers, the public and media.

**Goal 2.** Maximize resources effectively and efficiently in support of the Department's mission.

- **Objective 1:** Ensure all programs are at least 90% staffed to meet workload needs.
- **Objective 2:** Increase productivity by 10% (as measured by workload) through process analysis.
- **Objective 3:** Increase employee retention by 10% within 3 years based on retention information from HR.

**Goal 3.** Build an exceptional organization with outstanding leadership and a highly engaged, collaborative workforce.

- **Objective 1:** 90% of staff will complete an approved leadership development or team building classes.
- **Objective 2:** Develop and implement a Leadership Mentoring Program to be completed by 90% of participating staff.
- **Objective 3:** Achieve 80% positive ratings on the employee satisfaction survey.
- **Objective 4:** 100% of all DBO employees will attend at least one DBO Roadshow presentation on an annual basis.

**Goal 4.** Increase efficiency and effectiveness through innovative use of technology and education.

- **Objective 1:** 100% of requested examination documents will be encrypted and uploaded to a secure portal.
- **Objective 2:** 100% of all Department files will be scanned, stored, and accessible from a central divisional repository.
- **Objective 3:** 100% of DBO employees' current training records will be uploaded to (available in) the CornerStone Learning Management System.

## Control Environment

### Integrity and Ethical Values

Management establishes and demonstrates integrity and ethical values by holding all DBO employees to the highest ethics and integrity standards, and management leads by example through their actions. Internal Audit (IA) evaluates accountability of all levels of employees through testing internal and compensating controls to ensure that they work as intended. In addition, all employees are mandated to attend periodic ethics trainings.

**Core Values:**

1. Collaboration – We work as a team to foster a culture of learning, respect, and open communication to effectively solve problems and accomplish goals.
2. Integrity – We are fair, honest, and accountable.
3. Service – We are dedicated to providing exceptional support to the public and licensees.
4. Vigilance – We are diligent in executing our responsibilities.

**Ability to Report Ethical Concerns:**

Improper activities of DBO employees may report directly with the Internal Audits Unit or through the California Whistleblower Hotline, maintained by the Bureau of State Audits. The Internal Audits Unit can receive complaints against DBO employees from three primary sources: direct telephone calls, direct written complaints, or referral from the Bureau of State Audits' Whistleblower Hotline.

The Bureau of State Audits (BSA) maintains the State's Whistleblower Hotline which enables State employees and the public to report improper governmental activities. The hotline was established in response to the Reporting of Improper Governmental Activities Act, which is contained in Section 8547 et seq. of the California Government Code.

The Internal Audits Unit is responsible for responding to complaints received from the BSA "Whistleblower Hotline." When a complaint is received from BSA, a determination is made as to whether the Internal Audits Unit or management in the affected program will conduct the investigation. The determination is based on past experience, materiality of the issues and the position of the individual(s) involved in the complaint.

**DBO's Oversight Structure**

The Department of Business Oversight (DBO) 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 Department of Business Oversight systems of controls and monitoring.

As the Commissioner of DBO, Manuel Alvarez is responsible for the overall establishment and maintenance of the internal control and monitoring systems. This is achieved through periodic meetings with Chief Deputy Commissioner and Deputy Commissioners, as well as the establishment an Internal Audit (IA) unit. The IA maintains its independence by directly reporting to the Commissioner and Chief Deputy Commissioner. IA provides management information about the adequacy and effectiveness of internal controls and the quality of its operating performance when compared to established standards. Audit procedures are designed to evaluate whether internal controls are present and operating as intended as well as identifying inefficiencies

**Organizational structure to ensure appropriate levels of responsibility and authority:**

DBO has seven Divisions, each led by a Deputy Commissioner (DC), management, and supervisory levels below that. DBO's Delegation of Authority was revised in August 2019, empowering staff to make position-appropriate decisions.

## Executive Monitoring Sponsors

The executive monitoring sponsor responsibilities include facilitating and verifying that the Department of Business Oversight internal control monitoring practices are implemented and functioning as intended. The responsibilities as the executive monitoring sponsors have been given to: the Commissioner, Chief Deputy Commissioner, General Counsel, Senior Deputy Commissioner - Division of Financial Institutions, and Senior Deputy Commissioner - Division of Corporations. Information is communicated to staff through meetings, emails and DBO's internal monthly newsletter available on Department's intranet page.

## Establishing and maintaining a competent workforce:

As part of DBO's Workforce Action Plan:

- DBO increased its applicant pool by reaching out to five California University career fairs, handing out 258 applicant packets;
- DBO consolidated two similar examiner/auditor classifications, which opened up cross-divisional growth opportunities and made it easier to fill entry level examiner roles;
- DBO implemented an ongoing enterprise-wide Competency Training Initiative, all employees are encouraged to participate in the various training modules;
- From Q1-2017 through Q3-2019, 120 DBO managers/supervisors attended leadership training.

In addition to these enterprise-wide formal trainings, management also provided informal trainings when new process or procedure is implemented. As the process matures, the process documentation is revised accordingly and stored in SharePoint where employees can easily access them for guidance.

Annual performance evaluation is performed by management and reviewed by Human Resources for completeness and fairness to make sure reviews are reasonable. To ensure healthy working environment, DBO has an Equal Employment Officer who assists both employees and management. In addition, management periodically review staff workloads to review whether rebalancing of assignments is necessary.

## Information and Communication

DBO collects, retains, and process large amount of data. To ensure our data integrity and security, Department of Business Oversight (DBO) is audited biennially by Department of Technology and Military Department respectively. In addition, DBO's Internal Audit (IA) also performs validation of various data and effectiveness of its internal controls. The integrity and validity of DBO's data is crucial as it assists DBO to identify trends and better allocate its resources to better serve and advise the California citizens to make sound financial decision.

The results of monitoring activities for DBO-wide risks, including any changes made to strengthen internal controls, are documented in writing and retained by the assigned deputy commissioner(s) involved. Additionally, results of monitoring activities are documented on the DBO Risk Assessment Matrix.

DBO actively shares information between divisions. In addition, DBO management has an open communication style where they immediately share any information to the employees. The monthly executive meetings' minutes are also shared with the employees through email from the Commissioner

to all employees, as well as posting on DBO's intranet.

Results are communicated in weekly senior executive staff meetings, monthly executive committee meetings as a standing agenda item, and up or down through the established DBO chain of command. DBO also shares newsworthy progress to address risks through an internal monthly newsletter, called "The Ledger," and monthly interoffice communications to all employees from the Commissioner.

Communication with external stakeholders are mainly through DBO's consumer-facing website, which include monthly bulletins. This website is constantly monitored, maintained, and updated by a team from the Consumer Service Office that includes Outreach and Education unit which is responsible to analyze data and consumer complaints to identify trends and communicate DBO's directions to the various stakeholders. In addition, DBO posts information on its Facebook and Twitter pages for external stakeholders.

## **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 Business Oversight monitoring practices are implemented and functioning. The responsibilities as the executive monitoring sponsor(s) have been given to:

Betsy Barnhart, Chief Financial Services;

Edgar Gill, Senior Deputy Commissioner, Division of Corporations; Manuel Alvarez, Commissioner;

Chris Shultz, Chief Deputy Commissioner; and Harun Lomanto, Senior Auditor.

### **Monitoring Activities**

All levels of DBO management and personnel are responsible for ensuring that adequate internal controls are in place within their respective program areas. DBO continually evaluates internal control systems to ensure that risks are adequately addressed. Experts in each program area discuss concerns in daily, weekly, monthly, quarterly and annual meetings and raise potential issues with supervisors for consideration. Any critical items identified are evaluated by first-line managers, middle managers, senior managers and executive leadership for mitigation. DBO's senior executives consult on the highest-level priorities to properly address issues, assign resources and monitor progress.

A risk must be documented when it meets both of the following criteria:

1. The ability of the DBO (program specific or enterprise-wide) to carry out mission-critical or mandated functions is threatened.
2. There is no known internal control (existing business process) in place to mitigate the risk.

Staff members in DBO's Internal Audits unit also conduct routine, robust assessments of all departmental areas on both a scheduled and an ad hoc basis to mitigate gaps. DBO's Information Technology (IT) unit employs an Information Security Officer (ISO) who continually evaluates and addresses risks to the department's IT assets and information, as well as mitigations and contingencies.

### **Addressing Vulnerabilities**

Once potential risks are identified, and depending on their severity and/or likelihood, each scenario is

considered and elevated for resolution. Any critical or serious issues are mitigated immediately, where possible. Others are prioritized based on significance and addressed through project or contract management, process improvements, policy amendments, audit findings, budget change proposals, the system development lifecycle process, or the SLAA paradigm. Assigning responsibility to take action and address these risks is based on area of expertise, experience, sphere of influence and accountability. Staff is assigned to research risks as identified and to develop a plan for managing or eliminating risk. The appropriate deputy commissioner of each area with an identified risk is responsible for ensuring that progress is made toward reducing the identified vulnerability. Risks that are considered enterprise-wide may involve additional oversight by internal auditors, IT management and/or the Information Security Officer, branch chiefs, program deputy commissioners, or senior executive management, up to and including the DBO Commissioner.

## **RISK ASSESSMENT PROCESS**

The following personnel were involved in the Department of Business Oversight 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: DBO Portal is at its end of its life**

The software platform of the internal DBO website Self Service Portal, which allows licensees and consumers to submit and view documents is at its end of life and is no longer supported by the developer, Microsoft. Microsoft no longer provides security updates and patches for the website's software platform. The inability to provide ongoing security website maintenance leads to potential security vulnerabilities on the electronic information provided by the DBO and from its customers.

### **Control: Replacing the Portal with a new software platform**

DBO's IT division will be replacing the Portal with a new software platform and for the first step, IT has internally routed the Stage 1 Business Analysis (S1BA) package as a requirement of the California Department of Technology's (CDT) Project Approval Lifecycle (PAL) process for new IT system development requests. The S1BA is one of four Stage processes within CDT's PAL.

By engaging in the state's PAL process, the DBO will be following the standardized processes and procedures of the System Development Life Cycle in the development of the department's portal. Replacing the portal with a supportable platform will greatly reduce the risks associated with security breaches through the portal as well as not implementing a viable product.

### **Risk: Lack of Multi-Factor Authentication (MFA)**

The lack of experienced IT resources is a major contributor of not being able to implement an Multi-Factor Authentication (MFA) solution. An IT security assessment performed by the California Military Department in 2016 identified that DBO lacked MFA security processes for departmental users accessing IT services and systems. The risk of not implementing a MFA security process could lead to potential security breaches or threats to DBO's IT network infrastructure.

#### **Control: Seeking additional IT security resources**

DBO's IT division is seeking additional IT security resources to enhance the department's security program. The additional IT security personnel will provide the necessary resources to implement an MFA solution.

The risk of not being able to successfully implement a Multi-Factor Authentication solution will be reduced by acquiring skilled and experienced security personnel.

### **Risk: Documents on website not ADA compliant**

Some PDF documents are not ADA compliant and out of compliance with AB 434, which requires all content available to the public on the state website to be ADA compliant.

Non-compliance poses a risk of failure to make information accessible to some DBO stakeholders.

#### **Control: Hiring a limited-term position**

Hire a Limited Term position to help further remediate document-accessibility in compliance with ADA. This will initially reduce the risk of inadequate resources in providing support for this endeavor.

#### **Control: Providing training and implementing processes on assessing, converting, posting, and issuing ADA compliant documents**

Implement on-going training and processes for DBO programs on assessing, converting, posting, and issuing ADA compliant documents. This process will help the department reduce the risk of not having internal personnel trained on ADA compliance processes and procedures, and will ensure that documents posted or issued to the public meet the ADA compliance standards.

## **CONCLUSION**

The Department of Business Oversight 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.

**Manuel Alvarez, 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