

December 31, 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 California Housing Finance 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 Shelby Banks, Fiscal Services Manager, at (916) 326-8439, sbanks@calhfa.ca.gov.

GOVERNANCE

Mission and Strategic Plan

CalHFA's mission is to create and finance progressive housing solutions so more Californians have a place to call home. CalHFA was established in 1975 by Governor Edmund G. Brown Jr.'s signature of the Zenovich-Moscone-Chacon Housing and Home Finance Act with the purpose of working with the private sector to provide more affordable housing for California. CalHFA is charged with providing mortgages to the middle to low income home buyers and with lending to developers of affordable rental units. The agency sets loan interest rates slightly above its cost of funds and charges fees for specific services to cover its lending costs and risks.

The Agency's Chief Deputy Director (along with the Leadership Team) is responsible for preparing and presenting the Strategic Business Plan to the CalHFA Board of Directors annually. The Strategic Business Plan for fiscal year 2019-20 includes three goals and six key strategies to achieve those goals.

The first goal is to promote state-wide affordable housing production and opportunities for homeownership while maintaining financial sustainability and independence. Strategies to achieve that goal include 1) promoting sustainable homeownership opportunities by expanding eligibility requirements and product offerings while serving a broad range of income and housing needs, 2) expanding multifamily lending opportunities and unit production while addressing preservation needs and providing incentives for mixed-income housing, and 3) strengthening the Agency's financial position by monetizing assets for liquidity while maximizing return on equity and investment.

The second goal is continuing to improve operational efficiencies through technology, workforce planning, and the implementation of best practices. Key strategies to achieve this goal include 1) increasing operational efficiencies and 2) continuously monitoring and employing long-term strategies to mitigate enterprise risk and improve agency management reporting.

The final goal is collaborating with other housing entities, lenders (both public and private), and

stakeholders who complement CalHFA's lending objectives and policy priorities in order to deliver effective and innovative housing solutions. The strategy to achieve this goal is to establish partnerships to increase opportunities for affordable housing production.

Control Environment

As the head of California Housing Finance Agency, Tia Boatman Patterson, Executive Director, has the ultimate responsibility for establishment and ensuring adherence to the Agency's core values, codes of conduct and demonstration of integrity and ethical values. The Agency strives to build a trusting, respectful and positive workplace culture by promoting transparent communication and reporting ethical concerns. The Executive Director is also responsible for creating, maintaining and monitoring organizational controls. Organizational controls include developing rules, procedures and other protocols to direct the work of employees, improve communication, document various Agency systems, ensure financial stability, increase productivity and efficiency, help in meeting annual goals, improve morale, legal compliance, improve quality control, fraud and error prevention, information security and risk management. Additionally, the Executive Director is responsible for CalHFA operations including the mission, functions, image and reputation, protection and appropriate use of assets held by CalHFA, and management support to effectively carry out their designated role and responsibility. The Executive Director develops and monitors the framework for the Business Continuity Management Plan in the event of a disaster. The Business Continuity Plan establishes policies, authority and provides a prescriptive guide for disaster readiness training and awareness for CalHFA staff and creates an effective process of managing a disaster while ensuring safety of staff and CalHFA assets. It also identifies, through the Business Impact Analysis, what products and services are most critical to the Agency and what must be recovered in a disaster.

Each division head is responsible for establishing and monitoring the internal controls in the area of their responsibility in order to protect assets, ensure that records are accurate, promote operational efficiency to achieve the organizational mission and goals and ensure compliance with policies, rules, regulation, and laws. Division managers along with their supervisory staff develop detailed policies, procedures and practices pertaining to their individual department's operations and mission as well as a structure of segregating key duties and responsibilities among staff in order to reduce error, misuse, or fraud, establishing and communicating the management philosophy and operating style, assignment of authority and the process of ongoing monitoring activities and reporting deficiencies. Agency's written policies and procedures are published on the internal Agency's website for easy access to allow all employees to clearly understand their roles and responsibilities within predefined limits.

As a component unit of the State of California, CalHFA is administered by a Board of Directors consisting of 13 voting members and three non-voting members, including a chairperson selected by the Governor from among his or her appointees. Of the 13 voting members, seven are appointed by the Governor, four are ex-officio and two are appointed by the Legislature. The term of the appointed members of the board is six years. The CalHFA's Board of Directors oversees an Executive Director, who is an appointee of the Governor, and directs the staff of the Agency. The CalHFA Board of Directors meet every other month and provide oversight on all compliance control activities, risk assessments, information security compliance, as well as monitoring activities. Additionally, the board members are responsible for approving financing of multifamily projects, Agency financial information, bond finance authority, operational budget, business and other aspects of CalHFA.

Additionally, the Agency has established an ongoing Audit Committee to assist the Board of Directors in fulfilling its oversight responsibilities in the area of financial reporting and accounting integrity. The Committee meets at least twice per year to conduct meetings with an independent auditor, management and staff that serve as a resource for their understanding of the Agency's financial reporting responsibilities and any significant issues related to financial reporting and accounting policies.

Furthermore, the Agency contracts with an independent audit firm, currently CliftonLarsonAllen (CLA), to assist in preparing the annual audit report. The annual audit process ensures that the Agency's internal controls, processes, guidelines, and policies are adequate, effective and in compliance with governmental requirements, industry standards and federal regulations. This type of audit also ensures that reporting mechanisms can help prevent errors in financial statements. The Firm also provides the periodic board training sessions on risks and activities that may significantly impact the risk profile of the Agency.

CalHFA is not subject to an appropriated budget by the State. However, for sound financial management and oversight purposes, an annual budget is presented to and approved by the Board of Directors. Mid-year budget and mid-year business plan updates are provided to the Board of Directors in March of each year.

The CalHFA's preliminary budget is initially reviewed by the Executive Director on or before December 1 of each year for the ensuing fiscal year to be transmitted to the Secretary of the Business, Consumer Services and Housing Agency, the Director of Finance, and the Joint Legislative Budget Committee. This preliminary budget is included in the Governor's January Budget Proposal for informational purposes. However, the Agency's final budget is not reviewed and approved by the CalHFA Board until May of each year.

According to HSC 51005, the agency shall, by December 31 of each year, submit an annual report of its activities under this division for the preceding year to the Governor, the Secretary of the Business, Consumer Services and Housing Agency, the Director of Housing and Community Development, the Treasurer, the Joint Legislative Budget Committee, the Legislative Analyst, and the Legislature. The report shall include specific information evaluating the extent to which the programs administered by the agency have attained the statutory objectives of the agency.

Organizational structure of the Agency clearly defines key areas of authority and responsibility and establishes appropriate lines of reporting. The Agency's administration Division produces the monthly organizational charts to provide a clear picture of the functional sub-units of each department and the relationships among them. Pursuant to Title 25, California Code of regulation sections 10002 and 13302 (c), the Executive Director of the Agency established Delegation of Authority to sign contracts, debt obligations or other documents and instruments on her behalf when the Director is unavailable. The Office of General Counsel maintains an updated list of signature delegations.

The Agency's Workforce Plan was developed to align with CalHFA's Strategic Business Plan and is intended as a tool to help ensure that there are systems in place to recruit, develop and retain staff to support CalHFA business goals and operational needs. To create this Workforce Plan, CalHFA Senior Managers identified workforce challenges (gaps) and then prioritized workforce planning initiatives (goals) to address those gaps over the next three to five years. This was done as part of a pilot workforce planning program through the California Department of Human Resources (CalHR). The

Workforce Plan outlines the current state of CalHFA's workforce, identifies workforce challenges and environmental factors affecting business needs, and discusses the plan for mitigating these concerns.

The Administration Division recently developed an onboarding process for all incoming CalHFA new hires which is a structured guide to assist managers/supervisors in welcoming, integrating, and assimilating new employees to CalHFA. The process encompasses orienting and engaging new employees with the Agency environment and helps map out the key onboarding phases and information needed to help get a new employee started. It was also designed not only to help managers/supervisors, but to ensure that each new employee receives a consistent and comprehensive onboarding experience.

Performance appraisals, goals and objectives become a routine annual process throughout the Agency. The supervisory and management staff are responsible for meeting with their respective employees and conducting an evaluation of their work performances. In addition, the meetings are used to communicate an expectation of competence in the relevant knowledge, skills, and abilities required for each position. Management has a responsibility to hold personnel accountable through performance appraisals and disciplinary actions. Moreover, when hiring a new staff member, the Administration Division has a strong commitment to verifying the qualifications of job candidates before hiring and promoting only those with required knowledge and skills. In addition, CalHFA demonstrates its commitment to competence by ensuring that staff receives training and supervision in order to perform job duties. All employees are required to complete regularly scheduled trainings on ethics and anti-fraud policies of the organization. Each division manager is responsible for planning and preparing for succession by developing contingency plans and cross training for the re-assignment of duties when employees change positions or leave the Agency.

Information and Communication

The Leadership Team consisting of Agency's division directors and upper level managers was created to carry out the vision of the Executive Director to encourage a culture of effective communication as well as developing a management team that thinks in terms of the Agency's well-being rather than just in terms of their own parts of the organization. The main goal of the Leadership Team is to facilitate and enforce that the same standards and values are evident throughout the Agency. The team is responsible for communicating the core values and codes of conducts to the front-line management which then communicates the same information to the Agency's staff during staff meetings. The agenda includes updates related to the status of current programs, implementation of new initiatives, legislative changes and updates as well as policy discussions. The new Agency initiatives and special announcements are also communicated to the Agency's staff by the Executive Director through her "Director's Corner" page on the CalHFA internal website.

Additionally, the process of identifying top risks of the Agency is included in the strategic planning and annual business planning process. Every January and February the Agency's Leadership team attends a series of off-site business planning sessions with the Executive Director and Chief Deputy Director designed to review the organization's performance against the current year business plan and use that discussion to assist in the development of the proposed business plan for the upcoming fiscal year. Directly following the business planning sessions, each department head is tasked with the development of a budget that supports the achievement of the goals and strategic initiatives outlined in the Agency's proposed business plan. In March, staff provide a detailed Board Report and conduct a

mid-year business plan update and policy workshop with the Board in which staff presents actual business plan results through mid-year (December 31) and projections for the remainder of the current fiscal year. Staff also provide the CalHFA Board of Directors with information regarding possible initiatives. Each May, the Chief Deputy Director of the Agency presents the proposed Strategic Business Plan and Operating Budget for the upcoming fiscal year to CalHFA's Board of Directors.

The Agency has several external constituencies with which it must communicate, including first-time homebuyers, lending partners, developers, local governments, the California Legislature and many others. While each of those constituencies have different needs for information, CalHFA strives to ensure that our message is reliable and relevant, and consistent with our annual Business Plan's stated goals.

CalHFA communicates externally via multiple platforms, and majority of the communications are reviewed prior to release. Our public website at www.calhfa.ca.gov, our audience-specific email announcements, and various social media services give us the broadest reach for getting our messages out. We also issue periodic press releases over BizWire and place op-ed pieces to reach traditional news media. Additionally, face-to-face and in-person communications are very important; including a dedicated Single Family Lending outreach team for in-person training seminars. Staff attend and speak at dozens of housing fairs, conferences, expositions and other events throughout the year, for both our Single Family and Multifamily lending divisions.

CalHFA supports the California State Auditor's Office efforts to report the improper activities by state agencies and employees under the California Whistleblower Protection Act. Annually, the Director of Administration communicates to all staff of their responsibility, as a government employee, to report any type of fraud, waste, or abuse, which ultimately protects scarce state resources, and to be free from retaliation for doing so. Reports are logged and assessed against the Agency's goals and strategies. If the risk could negatively affect goals, the Enterprise Risk Management (ERM) group along with the Leadership Team will meet to develop a plan mitigating controls.

In order to record pertinent operational, programmatic and financial information, the Agency staff uses the accounting/financial and programmatic data from its system for decision-making purposes and performance evaluation. Management looks to the information management function for critical operating data and supports efforts to make improvements in the systems as technology advances. The information systems used by the Agency are a combination of in-house built programs and third-party software.

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 California Housing Finance monitoring practices are implemented and functioning. The responsibilities as the executive monitoring sponsor(s) have been given to:
Don Cavier, Chief Deputy Director.

As the head of CalHFA, Tia Boatman Patterson, Executive Director, is responsible for the overall establishment and maintenance of the internal control and monitoring systems.

Monitoring Activities

Management plays a key role in assuring that high standard of business and ethical practices permeate throughout the activities surrounding the custody and use of the Agency's resources. Established internal control policy and procedures provide guidance to employees in their stewardship role in achieving Agency's goals and objectives. The head of each division is responsible for ensuring that internal controls are established, properly documented, maintained and adhered to in each unit within their division as well as monitoring employee compliance with internal controls. Control activities include approvals, authorizations, verifications, reconciliations, reviews of performance, security of assets, segregation of duties and controls over information systems. All employees and managers are empowered to identify risk and develop mitigation efforts to control the various risks. The Enterprise Risk Management (ERM) group is tasked with independent evaluations of program controls to identify and mitigate risk enterprise-wide. On an annual basis, the ERM group meets with all divisions and program areas to conduct the risk assessment. ERM routinely reviews and monitors the Agency's activities to ensure compliance with policies and to identify any possible risks. These discussions assist in establishing the priorities for the year to focus on the highest and most critical risks to the Agency.

The Agency undertakes activities focused on raising organizational awareness and fostering a culture that enhances communication through its divisions. The Leadership Team meets biweekly to discuss previously identified potential risks and develop a plan to mitigate them. Reconciliation of agency key bank and general ledger accounts are conducted on a daily, monthly and quarterly basis. Operating payments are regularly verified for accuracy and compliance with contract terms or agreements. The Loan Administration Division reviews monthly reports from outside servicers and compares them to internal reports for purposes of accuracy. Additionally, the Single Family Lending Division established a Quality Control group which monitors the compliance and accuracy of Agency's loan documentation.

CalHFA's information technology division continuously monitors security measures in the areas of technical support, application support, and information security. In 2018, the Information Technology Division completely revised the Information Security Policy Manual which promotes effective management and oversight of information security program by formulating and documenting the security level of an information system. The manual is used as a foundation for appropriate security measures and controls to provide for the confidentiality, integrity, and availability of information, regardless of its form (electronic, optical, oral, print, or other media) which are critical for ensuring business continuity, protection of informational assets against unauthorized access, use, disclosure, disruption, modification, or destruction. In addition to routine risk management activities, the Agency established a disaster response system including a business continuity and disaster recovery plan to respond swiftly and appropriately in the event of a disaster and conducts training and drills on a regular basis.

The independently contracted accounting firm, CLA, assists Fiscal Services Division with fiscal risk management and oversight, and provides the certification that the Agency's financial statements are accurate and prepared in accordance with the Generally Accepted Accounting Principles. For further establishing of the effectiveness of the internal controls and monitoring of Agency's potential vulnerabilities, the Board of Directors plays active role in the Agency's risk management process. It determines the risk strategy and oversees management implementation of various loan programs and products, new initiatives, investments, hedging activities, counterparty relationships and servicers. During the Board meetings, the Agency's staff prepares and presents the quarterly reports on production, delinquency and progress towards attaining strategic milestones.

If any inadequacies are discovered, the Agency takes the appropriate measures to remedy the issues.

RISK ASSESSMENT PROCESS

The following personnel were involved in the California Housing Finance risk assessment process: executive management, middle management, and front line management.

The following methods were used to identify risks: ongoing monitoring activities, audit/review results, other/prior risk assessments, 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.

Since its establishment in 2017, the ERM continues to play a vital role in managing Agency's risks and identifying the potential vulnerabilities. ERM instills the risk awareness into the Agency, enhances its transparency and assists with collecting, mitigating, monitoring and reporting the various enterprise risks. The ERM's goal is to focus management's attention on the organization's most significant risks and improve its ability to meet its mission, goals, and objectives. The Agency strives to align the amount of risks it is willing to accept with strategic objectives and use a consistent approach to assess risks. Division Directors set internal expectations and requirements through the established standards of conduct, oversight structure, organizational structure, and expectation memos as part of the control environment. On an annual basis, the ERM group meets with division heads to identify new risks, reassess the top risks identified in the prior year and assists with developing an action plan on how to mitigate these risks. Bi-annually, each division director is tasked with responding to the assurance risk assessment questionnaire that assists the ERM group in evaluating the level of risks for each division, including the likelihood that the risk will occur and the impact of the risk if it occurs. The identified risks are ranked based on various factors. These factors include operational risk, systematic risk, financial risk, environmental risk, risk to the sustainability of the Agency, and conformity to regulatory compliance requirements.

RISKS AND CONTROLS

Risk: Key Person Dependence, Workforce Planning

CalHFA is a smaller organization with less than 200 employees. Like many departments across the State, CalHFA identified succession planning as a significant risk to the organization. As staff reach retirement age or find other career opportunities, it is critical that the Agency has a strategy for knowledge transfer. Some of the Agency's positions are held by key employees with extensive knowledge and tenured expertise where they have become a significant resource. Over time, the Agency has become dependent upon them. When the key employees leave, it creates the risk of the lack of historical knowledge and the existing staff not having the expertise and skills to smoothly continue the operational sustainability of the organization. CalHFA must retain and cultivate the knowledge and expertise needed to continue to meet and fulfill our mission.

Since its implementation in 2018, CalHFA has been actively implementing the Workforce Plan to address short-term and long-term staffing needs. The Agency was able to reduce the number of key person dependencies; however, in certain divisions this issue still poses a concern. The CalHFA

Workforce Plan and Business Plan supports business continuity and a process to identify and supply a qualified and motivated workforce prepared to take over when senior staff and other key employees leave.

Strategies for mitigating this risk include job shadowing, mentoring and making sure procedure manuals are in place and updated regularly.

Control: Control A

Leadership Team and supervisors are aware of the key employee dependency risk and continue to put adequate measures in place to mitigate the risk. Managers are setting up plans and schedules with key employees to share knowledge (knowledge transfer) with their peers and provide training and shadowing with staff to assure more than one person knows how to do that specific duty or work assignment. Additionally, each division has been tasked with developing and maintaining the individual desk procedures to ensure compliance with laws and regulations and establishing consistent standards and practices throughout the Agency.

Since 2017, CalHFA has increased its efforts in recruitments by adding 35 new employees; of which five were key leadership positions. Additionally, the Agency has given 16 exams, offered 48 job opportunities, and provided 35 promotions. This enlarge has stabilized our workforce, resulting in our ability to address issues, strategies, and other business objectives timelier and more efficiently. The hiring of the key leadership positions has led to more teamwork, productivity, strategy and building the foundation for organizational success today and into the future.

Risk: Funding - Sources, Levels

The Single Family and Multifamily housing programs offered by CalHFA are revenue-generating and provide the Agency's primary source of income. Not being able to secure a permanent source of funding to finance Agency's initiatives is identified as a significant risk to Agency's operations.

Various economic and regulatory factors such as prevailing economic conditions, legislative changes, mortgage interest rates, investment rates, the demand for housing, the cost of housing and of operating housing programs, the volume of mortgage lending activity in the State and other factors affecting the supply of housing in California create significant challenges for the Agency in Single Family and Multifamily housing programs as well as its overall operations.

Control: A

The Agency produces program reports to track production activity so that we may monitor and mitigate risks associated with funding. These reports are also sent to governance agencies.

In 2019, the Agency established Strategic Project Advisory Group (SPAG). SPAG ensures that strategic projects align with the Agency's Business Plan, facilitate communication and collaboration between divisions, and acknowledge the interdependence necessary for successful project oversight while enhancing the exchange of information and ideas to foster consensus and buy-in. In addition, SPAG facilitates continuous efforts to pursue permanent funding sources for the Agency's programs in order create and finance progressive housing solutions. The Agency is in the process of developing a framework for partnerships with entities who support CalHFA's

affordable lending objectives including building relationships with the private sector and Legislators; and to offer CalHFA technical assistance as it relates to State and Federal affordable housing priorities.

Risk: Technology - Data Security

Technology plays a vital role in CalHFA's business operations. It provides necessary tools and functions, helps increase productivity, allows for better decision-making process, and enables customers to interact with the Agency through various communication technology systems.

With the increasing threat of information security breaches, managing data security risk has become an increasingly important business concern of protecting the confidentiality and availability of the organization's data. The information security breach could cause a significant impact on agency reputation as well as regulatory reporting and sanctions that may be imposed by federal and state laws. CalHFA Executive Director and Leadership Team has been working closely with the Agency's Chief Information Security Officer (CISO) and developed the enterprise architecture for CalHFA to assist in rationalizing, standardizing and consolidating information technology application assets, infrastructure data and procedures for all division within CalHFA. The updated Information Security Policy Manual is used as a guide for all division managers and staff to comply with information technology policies in order to fulfill the Information Security Officer (ISO) roles and responsibilities. The Agency also established the Information Security Governance Council which is comprised of the Chief Deputy Director, General Counsel, Chief Information Officer, Director of Administration, Risk Manager, and Information Security Officer. This Council provides guidance to the information technology management team.

Control: A

CalHFA information technology team created a multi layered framework to mitigate risks associated with data security and data loss. The data security and loss prevention encompass the following framework consisting of IT infrastructure, Personal Computing, Outsourced IT, and IT Governance. IT infrastructure (e.g. servers, networks, internet, Wi-Fi, operating system and application software) is managed against successful attacks by separating and controlling access to various systems and networks with different threat levels and sets clearly defined security roles for users who may operate and interface with CalHFA technology environment. Personal computing ("endpoint" equipment - e.g. desktops, laptops, tablets, mobile devices) regulated through CalHFA's network by safeguarding information systems and assets at its entry and exit points.

Control: B

CalHFA IT team recently implemented new security measures for email, logins, and mobile devices which includes a 2-factor authentication, re-enabling of conditional access and mobile device management. Outsourced IT includes use of the cloud, backup and data storage. CalHFA's IT team has been contracting with reliable cloud hosting providers to minimize the Agency's risk of a security data breach. In terms of data loss risk, CalHFA's cloud host provides CalHFA multiple storage solutions by running real-time mirrors of data to ensure neither the security nor data loss risks are serious. The hosting cloud provider also maintains multiple server farm locations and

often have multiple storage solutions in each location to allow redundant data storage.

CONCLUSION

The California Housing Finance 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.

Tia Boatman Patterson, Executive Director

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