STATE OF CALIFORNIA

Report to the California State Legislature

PROPERTY TAX APPORTIONMENTS

Calendar Year 2014

BETTY T. YEE
California State Controller

October 2015

BETTY T. YEE
California State Controller

October 15, 2015

To: Members of the California State Legislature and the People of California

SUBJECT: Property Tax Apportionments Report to the Legislature for Calendar Year 2014

I am pleased to present the Property Tax Apportionments Report for calendar year 2014. This report, prepared pursuant to Government Code section 12468, is intended to help mitigate problems associated with the counties' apportionment and allocation of property tax revenues.

The State Controller's team completed audits of 16 of the 58 counties in the State of California, and found the audited counties to be in compliance generally with the legal requirements for allocating property tax revenues. However, this report notes specific problem areas related to individual counties.

I hope you find the report informative and useful for future policy decisions. If you have any questions regarding this report, please contact Jeffrey Brownfield, Chief of our, Division of Audits, at (916) 324-1696.

Sincerely,

Original signed by

BETTY T. YEE

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Executive Summary

This report summarizes the results of the State Controller's Office (SCO) audit of county property tax apportionments and allocations during the 2014 calendar year. After the passage of Proposition 13 in 1978, the California legislature enacted new methods for allocating and apportioning property tax revenues to local government agencies and public schools. The main objective was to provide local agencies with a property tax base that would grow as assessed property values increase.

Property tax revenues that local governments receive each year are based on the amount received in the prior year plus a share of the property tax growth within their boundaries. Property tax revenues are then apportioned and allocated to local agencies and schools using prescribed formulas and methods defined in the California Revenue and Taxation Code. This methodology is commonly referred to as the AB 8 process or the AB 8 system. The method has been further refined in subsequent laws passed by the legislature.

The SCO's property tax audit program began on July 1, 1986, pursuant to Revenue and Taxation Code section 95.6 (now Government Code section 12468). The statute mandates that SCO perform audits of the allocation and apportionment of property tax revenues by counties and make specific recommendations to counties concerning their property tax administration. The statute also specifies that SCO is to prepare an annual report summarizing the results of its findings under this audit program.

SCO developed and implemented a comprehensive audit program that includes, but is not limited to, a detailed analysis of past and current requirements of property tax laws and an examination of property tax systems, processes, and records at the county level. Each audit encompasses an evaluation of a county's property tax apportionment methodology, allocation procedures, and compliance with applicable laws and regulations. SCO applied procedures considered necessary and appropriate to provide a basis for reporting on the areas examined.

Government Code section 12468 requires that audits be conducted periodically for each county according to a prescribed schedule based on county population. During 2014, SCO completed audits of 16 counties' property tax apportionment and allocation systems, processes, and records. The 16 counties are Alameda, Butte, Del Norte, Kern, Lake, Lassen, Los Angeles, Marin, Modoc, Riverside, San Francisco, Santa Clara, Santa Cruz, San Mateo, Stanislaus, and Trinity.

Current statutes do not allow counties to charge school and community college districts, the county superintendents of schools, and/or the Educational Revenue Augmentation Fund (ERAF) for property tax administrative costs. The legislature may wish to consider legislation to address an apparent conflict between Revenue and Taxation Code section 95.3 and Health and Safety Code sections 34183 and 34188, which may indirectly charge those costs to school and community college districts, the county superintendents of schools, and/or the ERAF.

As a part of the audits, SCO performed follow-up reviews to ensure that the counties properly addressed the findings identified in previous SCO audit reports.

Except for the findings and recommendations noted in this report, the processes used by the 16 counties audited during 2014 appear to comply with the requirements for the apportionment and allocation of property tax revenues.

The audit report findings broadly are classified as follows:

Prior Audits

The counties of Alameda, Kern, Modoc, San Mateo, and Stanislaus did not fully resolve all findings noted in prior audits.

Current Audits

- Modoc County excluded local utility assessed value from computations of annual tax increment factors, which is part of the AB 8 process.
- San Francisco, Stanislaus, and Trinity counties had factor or revenue carry-forward errors in the computation of annual tax increment factors, which is part of the AB 8 process.
- Kern, Marin, and Modoc counties had procedural issues regarding jurisdictional changes.
- Kern and Modoc counties had errors in the supplemental property tax apportionments for K-12 schools.
- Kern, Lassen, Marin, Modoc, Riverside, San Mateo, Stanislaus, and Trinity counties included the ERAF in the unitary and operating nonunitary apportionment process.
- Lassen and Modoc counties included the railroad assessed value in the unitary and nonunitary apportionment process.
- Lake County did not properly compute unitary excess growth.
- Modoc County used AB 8 factors to apportion unitary taxes in two fiscal years.
- Trinity County had errors in the unitary debt rate computation and failed to carry forward prior year revenue for excess rate computations.

- Lassen and Modoc counties failed to establish the unitary railroad assessed value apportionment process.
- San Francisco and San Mateo counties excluded the ERAF and included redevelopment agencies in the unitary railroad apportionment calculations.
- Kern County included incorrect school entities in the qualified electric property apportionment.
- San Francisco City and County excluded the ERAF and included redevelopment agencies in the electric property computation process.
- Kern, Lassen, Los Angeles, Marin, and Santa Cruz counties have unresolved administrative cost issues with cities.
- Kern, Lake, and Trinity counties had ERAF computation errors.
- Los Angeles County is reviewing its tax equity allocation process to ensure compliance.
- Lake, Lassen, Modoc, and Trinity counties had growth computation errors in their VLF computations.
- Kern County improperly computed negative ERAF amounts for some school entities in the vehicle license fee (VLF) computation process.
- Lassen and Trinity counties had errors in their negative bailout computations.

Overview

Introduction

This report presents the results of 16 audits of county property tax apportionments and allocations completed by the State Controller's Office (SCO) in calendar year 2014. The following counties were audited: Alameda, Butte, Del Norte, Kern, Lake, Lassen, Los Angeles, Marin, Modoc, Riverside, San Francisco, Santa Clara, Santa Cruz, San Mateo, Stanislaus, and Trinity. Government Code section 1268 requires that such audits be conducted periodically for each county according to a prescribed schedule based on county population. The purpose of the audits is to help mitigate problems associated with property tax apportionment and allocation process.

Except for the findings and recommendations noted in this report, the 16 counties audited generally complied with the requirements for the apportionment and allocation of property tax revenues.

Background

After the passage of Proposition 13 in 1978, the California legislature enacted new methods for allocating and apportioning property tax revenues to local government agencies and public schools. The main objective was to provide local agencies with a property tax base that would grow as assessed property values increase. These methods have been further refined in subsequent laws passed by the legislature.

One key law was Assembly Bill 8 (AB 8), which established the method of allocating property taxes for fiscal year (FY) 1979-80 (base year) and subsequent fiscal years. The methodology is commonly referred to as the AB 8 process or the AB 8 system.

Property tax revenues that local governments receive each fiscal year are based on the amount received the prior year plus a share of the property tax growth within their boundaries. Property tax revenues are then apportioned and allocated to local agencies and schools using prescribed formulas and methods defined in the Revenue and Taxation Code.

The AB 8 process involves several steps, including the transfer of revenues from schools to local agencies and the development of the tax rate area annual tax increment growth (ATI) factors, which determine the amount of property tax revenues allocated to each entity (local agencies and schools). The total amount allocated to each entity is then divided by the total amount to be allocated to all entities to determine the AB 8 factor (percentage share) for each entity for the year. The AB 8 factors are computed each year for all entities using the revenue amounts established in the prior year. These amounts are adjusted for growth annually using ATI factors.

Subsequent legislation removed revenue generated by unitary and operating nonunitary property and pipelines from the AB 8 system. This revenue is now allocated and apportioned under a separate system.

Other legislation established an Educational Revenue Augmentation Fund (ERAF) in each county. Most local government agencies are required to transfer a portion of their property tax revenues to the ERAF. The fund subsequently is allocated and apportioned by the county auditor according to instructions received from the local superintendent of schools or chancellor of the California community colleges.

Revenues generated by the different types of property tax are allocated and apportioned to local agencies and schools using prescribed formulas and methods, as defined in the Revenue and Taxation Code. Taxable property includes land, improvements, and other properties that are accounted for on the property tax rolls, which are primarily maintained by the county assessor. Tax rolls contain an entry for each parcel of land, including parcel number, owner's name, and value. The types of property tax rolls are:

- *Secured Roll*—Property that, in the opinion of the assessor, has sufficient value to guarantee payment of the tax levies and that if the taxes are unpaid, the obligation can be satisfied by the sale of the property by the tax collector.
- *Unsecured Roll*—Property that, in the opinion of the assessor, does not have sufficient "permanence" or have other intrinsic qualities to guarantee payment of taxes levied against it.
- *State-Assessed Roll*—Utility properties, composed of unitary and nonunitary value, assessed by the State Board of Equalization.
- *Supplemental Roll*—Property that has been reassessed due to a change in ownership or the completion of new construction, where the resulting change in assessed value is not reflected in other tax rolls.

Audit Program

The property tax audit program began on July 1, 1986, under Revenue and Taxation Code section 95.6 (now Government Code section 12468). The statute mandates that the State Controller periodically perform audits of the allocation and apportionment of property tax revenues by counties and make specific recommendations to counties concerning their property tax administration. However, the State Controller's authority to compel resolution of its audit findings is limited to those findings involving an overpayment of State funds.

Overpayment of State General Fund money is recoverable by the State under several provisions of law. In addition, the State Controller has broad authority to recover overpayments made from the State Treasury. If an audit finds overpayment of State funds, and the State agency that made or authorized the payment does not seek repayment, the SCO is authorized to pursue recovery through a variety of means (Government Code sections 12418–12419.5). The specific remedy employed by SCO depends on the facts and circumstances of each situation.

SCO developed and implemented a comprehensive audit program to carry out the mandated duties. The comprehensive audit program includes, but is not limited to, a detailed analysis of past and current requirements of property tax laws and an examination of property tax records, processes, and systems at the county level.

These property tax apportionment audits have identified and aided in the correction of property tax underpayments to public schools. The underallocation of property taxes by individual counties to their public schools results in a corresponding overpayment of State funds to those schools by the same amount. This, in turn, causes public schools in other counties to receive less State funding because the total funds available are limited. Subsequent legislation forgave some counties for underpayments to schools without requiring repayment, or assessment of penalties. However, the legislation required that the cause of the underallocations, as identified by the audits, be corrected.

Audit Scope

Each audit encompasses an evaluation of a county's property tax apportionment methodology, allocation procedures, and compliance with applicable laws and regulations. SCO auditors used procedures considered necessary to provide a basis for reporting on the areas examined. In conducting the audits, the auditors focused on the following areas to determine whether:

- The apportionment and allocation of the ATI was in accordance with Revenue and Taxation Code sections 96 through 96.5;
- The methodology for redevelopment agencies' base-year calculations and apportionment and allocation of the ATI was in accordance with Revenue and Taxation Code sections 96.4 and 96.6, and Health and Safety Code sections 33670 through 33679;
- The effect of jurisdictional changes on base-year tax revenues and the ATI was in accordance with Revenue and Taxation Code section 99;
- The apportionment and allocation of property tax revenues from supplemental assessments was in accordance with Revenue and Taxation Code sections 75.60 through 75.71;
- The apportionment and allocation of State-assessed unitary and operating nonunitary property taxes was in accordance with Revenue and Taxation Code section 100;
- The computation and apportionment of property tax revenues to low- and no-tax cities was in accordance with Revenue and Taxation Code section 98;
- The computation and collection of local jurisdictions' property tax administrative costs was in accordance with Revenue and Taxation Code sections 95.2 and 95.3;

- The computation and apportionment of property tax revenues to the ERAF was in accordance with Revenue and Taxation Code sections 97 through 97.3; and

- The payment from the ERAF was made in compliance with Revenue and Taxation Code section 97.68, commonly known as the "Triple Flip," and section 97.70, commonly known as the "VLF Swap."

Conclusion

The property tax allocation and apportionment system generally is operating as intended. In the interest of efficiency and cost control for both the counties and the State, we submit the Summary of Findings and Recommendations in this report to assist in initiating changes that will help improve the system.

Summary of Findings and Recommendations

Introduction

Except for the findings and recommendations cited in this report, the audit reports issued in 2014 indicated that the 16 audited counties generally complied with the legal requirements for the apportionment and allocation of property tax revenues. However, problem areas were identified and are described below. Recommendations to resolve the problems are included within the individual county findings.

Unresolved Prior Audit Findings

The counties of Alameda, Kern, Modoc, San Mateo, and Stanislaus did not fully resolve all findings noted in prior audits.

Computation of Annual Tax Increment Factors (ATI)

The Revenue and Taxation Code requires that each jurisdiction in a tax rate area (TRA) must be allocated property tax revenues in an amount equal to the property tax revenues allocated to it in the prior fiscal year. The difference between this amount and the total amount of property tax assessed in the current year is known as the annual tax increment (ATI). The computation of the annual tax increment results in a percentage that is used to allocate growth in assessed valuation to a county's local government jurisdictions and schools from the base year forward. Revenue and Taxation Code sections 96 through 96.5 prescribe this methodology. (Some exceptions to this allocation are contained in the Revenue and Taxation Code for specified TRAs.)

Modoc County excluded local utility assessed value (AV) from the computation of annual tax increment, which is part of the AB 8 process.

San Francisco City and County only computed ATI factors to four decimal places.

Stanislaus County did not carry forward prior year gross tax amounts in all fiscal years.

Trinity County did not carry forward prior year revenue used to compute tax increment in FY 2012-13.

Jurisdictional Changes

Revenue and Taxation Code section 99 prescribes the procedures a county must perform in order to make adjustments for the apportionment and allocation of property taxes resulting from changes in jurisdictional controls or changes in responsibilities of local government agencies and schools. The statute requires a county to prepare specific documentation that takes into consideration services and responsibilities.

In Kern County, there is a lawsuit pending with a city regarding interpretation of a memorandum of understanding and the computation of annual tax increment (ATI) factors based on that memorandum.

Marin County had ATI factor errors in the jurisdictional change process.

Modoc County had some procedural errors in their jurisdictional change process.

Supplemental Property Tax Apportionments

When a revaluation of property occurs during the fiscal year due to changes in ownership or completion of new construction, supplemental taxes usually are levied on the property. Revenue and Taxation Code sections 75.70, 75.71, and 100.2 provide for the apportionment and allocation of these supplemental taxes.

In Kern County, the county included multi-county schools in the supplemental property tax apportionment process.

Modoc County did not adjust the schools' apportioned amounts by average daily attendance (ADA).

Supplemental Property Tax Administrative Fees

In addition to the fee allowed by Revenue and Taxation Code section 95.3 for the administration of the secured tax roll, Revenue and Taxation Code section 75.60 allows the charging of a fee for the administration of the supplemental tax roll. Once a county adopts a method of identifying the actual administrative costs associated with the supplemental roll, it is allowed to charge an administrative fee for supplemental property tax collections. This fee is not to exceed 5% of the supplemental taxes collected.

No errors were noted in this area.

Unitary and Operating Nonunitary Property Taxes

The process for apportioning and allocating property taxes from certain utility companies functions through the unitary and operating nonunitary tax system employed by the State Board of Equalization. Unitary properties are those properties on which the State Board of Equalization "may apply the principle of unit valuation in valuing properties of an assessee that are operated as a unit in the primary function of the assessee" (i.e., public utilities). The Revenue and Taxation Code further states, "Operating nonunitary properties are those that the assessee and its regulatory agency consider to be operating as a unit, but the board considers not part of the unit in the primary function of the assessee." Revenue and Taxation Code section 100 prescribes the procedures counties must perform to allocate unitary and operating nonunitary property taxes beginning in FY 1988-89.

Kern, Lassen, Marin, Modoc, Riverside, San Mateo, Stanislaus, and Trinity counties included the educational revenue augmentation fund (ERAF) in the unitary and operating nonunitary apportionment process.

Lassen and Modoc counties included the regulated railroad unitary values in the unitary and nonunitary apportionment process, for all fiscal years.

Lake County used incorrect AB 8 apportionment factors to compute excess 102% growth apportionment factors.

Modoc County used AB 8 factors to apportion unitary and operating nonunitary taxes in FY 2010-11 and FY 2011-12.

Trinity County made errors in the unitary debt service rate computation and did not properly carry forward prior year revenue used to compute excess 102% growth apportionment factors in FY 2006-07, FY 2011-12, and FY 2012-13.

Unitary Railroad Property Taxes

The process for apportioning and allocating property taxes from certain regulated railway companies functions through the unitary railroad tax system employed by the State Board of Equalization. Unitary railroad properties are defined in Revenue and Taxation Code section 723. Revenue and Taxation Code section 100.11 prescribes the procedures counties must perform to allocate unitary railroad property taxes beginning in FY 2007-08.

Lassen and Modoc counties included railroad property value with their unitary apportionment process in the qualified electric property apportionments.

San Francisco and San Mateo counties excluded the ERAF and included redevelopment agencies in the railroad apportionment process.

Unitary Qualified Electric Property Taxes

The process for apportioning and allocating property taxes from certain qualified electric properties, owned by a public utility, functions through the property tax system employed by the State Board of Equalization. Revenue and Taxation Code section 100.95 prescribes the procedures counties must perform to allocate qualified electric property taxes beginning in FY 2007-08.

Kern County included all schools in the electric property computations, not just the affected schools.

San Francisco City and County excluded the ERAF and included redevelopment agencies in the qualified electric property apportionments.

Property Tax Administrative Fees

Counties are allowed to collect from each appropriate jurisdiction, that jurisdiction's share of the cost of assessing, collecting, and apportioning property taxes. Revenue and Taxation Code section 95.3 prescribes the requirements for computing and allocating property tax administrative fees (PTAF). The offices of the county assessor, tax collector, assessment appeals board, and auditor generally incur county property tax administrative costs. The county generally is allowed to be reimbursed for these costs.

Prior to FY 2006-07, counties could not impose a fee, charge, or other levy on a city, nor reduce a city's allocation of ad valorem property tax revenue, in reimbursement for services performed by the county under Revenue and Taxation Code sections 97.68 and 97.70. Pursuant to Revenue and Taxation Code section 97.75, beginning with FY 2006-07, a county may impose a fee, charge, or other levy on a city for these services, but the fee, charge, or other levy shall not exceed the actual cost of providing the services.

In Kern, Lassen, Los Angeles, Marin, and Santa Cruz counties, there were unresolved issues concerning the property tax administrative fee collection process for some of the cities within the county.

Educational Revenue Augmentation Fund (ERAF)

The legal requirements for the local agency shift of property tax revenues to the Educational Revenue Augmentation Fund (ERAF) are contained in Revenue and Taxation Code sections 97 through 97.3. Beginning in FY 1992-93, each local agency is required to shift an amount of property tax revenues to the ERAF using formulas prescribed by the Revenue and Taxation Code. The property tax revenues in the ERAF subsequently are allocated to schools and community colleges using factors supplied by the county superintendent of schools or chancellor of the California community colleges.

Since the passage of the ERAF shift requirements, the Legislature has enacted numerous bills that affect the shift requirements for various local government agencies. One bill was Assembly Bill (AB) 1589 (Chapter 290, Statutes of 1997). This bill primarily addressed three areas related to the ERAF shift:

- ERAF shift requirements for certain county fire funds for FY 1992-93 (Revenue and Taxation Code section 97.2(c)(4)(B));
- A special provision for counties of the second class (population of at least 1,400,000 and under 4,000,000) when computing the ERAF shift amount for county fire funds in FY 1993-94 (Revenue and Taxation Code section 97.3(c)(4)(A)(I)); and
- ERAF shift requirements for county libraries for FY 1994-95 and subsequent years. After the passage of AB 1589, the State Controller requested advice from the California Attorney General regarding the application of Chapter 290, Statutes of 1997. The Attorney General responded in May 1998.

After the passage of AB 1589, the State Controller requested advice from the California Attorney General regarding the application of Chapter 290, Statutes of 1997. The Attorney General responded in May 1998.

The Attorney General advised that the amendment to Revenue and Taxation Code section 97.2(c)(4)(B) significantly narrowed the scope of the exemption granted by the code section and was to be given retroactive application. The result is that many counties and special fire protection districts that were able to claim an exemption under the section as it formerly read, lost the exemption retroactive to FY 1992-93. Consequently, those counties and special districts were required to shift additional funds to the county ERAF.

In response to the advice by the Attorney General, and noting the severe fiscal impact the loss of the exemption would have on local government agencies, the SCO recommended that the legislature consider restoring the exemption previously granted to fire protection districts and eliminated as a result of AB 1589 (Chapter 290, Statutes of 1997). Subsequently, the legislature enacted AB 417 (Chapter 464, Statutes of 1999), restoring the exemption to fire districts.

Kern County miscalculated a disaster relief credit adjustment from the ERAF.

Lake County computed an incorrect ERAF contribution, which overstated the county's ERAF share.

Trinity County had an error in the ERAF computation, which overstated the ERAF share for the county and a special district.

Redevelopment Agencies

The legal requirements for the apportionment and allocation of property tax to redevelopment agencies (RDAs) are found in Revenue and Taxation Code sections 96.4 and 96.6, and Health and Safety Code sections 33670 through 33679. California community redevelopment law entitles a community redevelopment agency to all of the property tax revenue realized from growth in values since the redevelopment agency's project area inception, with specified exceptions.

No errors were noted in this area.

Current Requirements

Recent legislation, ABX1 26 (Chapter 5, Statutes of 2011) and AB 1484 (Chapter 26, Statutes of 2012), added and amended sections of the Health and Safety Code and mandated the dissolution of redevelopment agencies. Under ABX1 26, the county auditor-controller is required to "create within the county treasury a Redevelopment Property Tax Trust Fund for the property tax revenues related to each former redevelopment agency, for administration by the county auditor-controller." Distributions from the Redevelopment Property Tax Trust Fund (RPTTF) are made in accordance with specified priorities in Health and Safety Code section 34183.

Excess revenues in the RPTTF are distributed according to the requirements of Health and Safety Code section 34188. Proceeds from asset sales are to be transferred to the county auditor-controller for distribution as property tax proceeds. Unencumbered balances of redevelopment agency funds, including housing funds, are to be remitted to the county auditor-controller for distribution by the auditor-controller using the same methodology for allocation and distribution of property tax revenues as provided in section 34188.

Tax Equity Allocation (TEA)

Revenue and Taxation Code section 98 and the Guidelines for County Property Tax Administration Charges and "No-/Low-Property-Tax Cities" Adjustment, provided by the County Accounting Standards and Procedures Committee, provide a formula for increasing the amount of property tax allocated to a city that had either no- or low-property-tax revenues.

Los Angeles County is reviewing its tax equity allocation computations to ensure compliance, which will be reviewed in the next audit.

Sales and Use Tax/Vehicle License Fee Adjustments

Sections 97.68 and 97.70 of the Revenue and Taxation Code require allocation of ad valorem property tax revenue by ERAF to Sales and Use Tax and Vehicle License Fee adjustment amounts. If there is not enough ad valorem property tax revenue in the ERAF, the difference shall be reduced from all school districts and community college districts that are not excess tax school entities.

Lake, Lassen, Modoc, and Trinity counties had growth computation errors resulting in overpayment and underpayment to cities and counties.
Kern County included multi-county and pre-average daily attendance (ADA) school revenues in the computation to remove from ERAF.

Negative Bailout (SB 85)

After the passage of Proposition 13, the Legislature passed SB 154 (Chapter 292, Statutes of 1978), which provided for the distribution of State assistance, or bailout, to make up, in part, for local property tax losses. The relief for counties was $436 million in cash grants plus the State's assumption of $1 billion associated with mandated health and welfare programs.

In the second year following the passage of Proposition 13, the Legislature passed AB 8 (Chapter 282, Statutes of 1979), which provided for a long-term solution consisting of a one-time adjustment (shift) that created a new property tax base for each local agency.

Counties received 100% of their SB 154 block grants and a small adjustment for the Aid to Families with Dependent Children, minus the amount of the indigent health block grant. For some counties, the value of the indigent health block grant was so great that it exceeded the value of the SB 154 block grant. In those cases, the AB 8 shift resulted in a reduction of the property tax base instead of an increase. These counties are referred to as "negative bailout counties." For all but the negative bailout counties, the increased property tax was deducted from the schools' property tax. For the negative bailout counties, school property taxes should have been increased by the negative bailout amount.

Subsequently, it was discovered that the negative bailout counties were not transferring the required property taxes to the schools. Consequently, the legislature passed AB 2162 (Chapter 899, Statutes of 1983), forgiving prior allocation errors but requiring future payments to be made in accordance with statute.

The negative bailout amount has grown each year as the assessed value of property in the counties has grown. In 2010, the legislature passed SB 85 (Chapter 5, Statutes of 2010), which did not eliminate the negative bailout amount, but capped it according to a specified formula.

Both Lassen and Trinity counties had errors resulting in overcharges to the ERAF.

Item for Legislative Consideration

Revenue and Taxation Code section 95.3 allows a county to charge for the cost of administering the property tax program in the county. While the county computes the schools', community college districts', county schools superintendent's, and ERAF's shares of these costs, statute does not allow the county to collect these shares. School entities and the ERAF thus are held harmless from administrative cost charges. The legislature has stated intent to reimburse the costs attributable to school entities and the ERAF "by a future act of the legislature that makes an appropriation for purposes of that reimbursement."

Health and Safety Code section 34183 allows the county auditor-controller to deduct from the Redevelopment Property Tax Trust Fund, administrative costs allowed under Health and Safety Code section 34182, and Revenue and Taxation Code section 95.3, prior to making the prioritized distributions that follow. As a result, any balance to be distributed pursuant to Health and Safety Code section 34188 is reduced, thus reducing all taxing agencies' (including schools') and the ERAF's shares of residual revenues. Consequently, schools and the ERAF are paying a portion of the administrative costs.

Recommendation

As the Health and Safety Code sections referred to above are not appropriations, the legislature may wish to consider legislation regarding the charging of administrative costs allowed under Health and Safety Code section 34182 and Revenue and Taxation Code section 95.3, to schools and the ERAF as a result of Health and Safety Code sections 34183 and 34188.

Findings of Individual County Audits

Introduction

The findings and recommendations included below are presented as they were stated in the County Property Tax Apportionment and Allocation reports issued by the State Controller's Office (SCO) in calendar year 2014. Unless otherwise indicated, the counties agreed with the findings and recommendations.

These findings and recommendations are solely for the information and use of the California legislature, the respective counties, the Department of Finance, and SCO; they are not intended to be and should not be used by anyone other than those specified parties. This restriction is not intended to limit distribution of this report or the respective audit reports, which are a matter of public record.

Alameda County (July 1, 2005, through June 30, 2013)

Follow-up on prior audit findings

Our prior audit report, issued August 2006, included no findings related to the apportionment and allocation of property tax revenues by the county.

Conclusion

Our audit found that the county complied with California statutes for the allocation and apportionment of property tax revenues for the period audited.

Butte County (July 1, 2008, through June 30, 2013)

Follow-up on prior audit findings

The county has resolved satisfactorily the findings noted in our prior audit report, issued November 13, 2009.

Conclusion

Our audit found that the county complied with California statutes for the allocation and apportionment of property tax revenues for the period audited.

Del Norte County (July 1, 2005, through June 30, 2014)

Follow-up on prior audit findings

The county satisfactorily has resolved the findings noted in our prior audit report, issued July 2006.

Conclusion

Our audit found that the county complied with California statutes for the allocation and apportionment of property tax revenues for the period audited.

Kern County (July 1, 2009, through June 30, 2012)

Follow-up on prior audit findings

Findings noted in our prior audit, issued April 2010, have been satisfactorily resolved by the county, with the exception of Finding 4.

OBSERVATION 1—Jurisdictional changes

Kern County has had Memorandums of Understanding (MOUs) with the cities in the county since 1995 regarding the annexation of county unincorporated areas into the cities.

Prior to fiscal year (FY) 2012-13, the county computed city annexations using only the city/county split percentages noted in the respective MOU to determine revenue and factor shares.

Prior to the audit of the Kern County Property Tax Procedures in May 2013, the SCO had been contacted by Kern County and the City of Bakersfield regarding the application of the MOU. Specifically, they were concerned with Educational Revenue Augmentation Fund (ERAF) adjustments and the proposal by the county to adjust the computation of city annexations completed since FY 2005-06.

The county has determined that it has been misinterpreting the MOU concerning the ERAF adjustment of revenue to be exchanged. The city disagrees with the county's interpretation and adjustment of annexations since FY 2005-06.

The City of Bakersfield filed suit against Kern County regarding the county's interpretation of the MOU.

FINDING 1—Supplemental property tax

The county included multi-county schools in the supplemental apportionment and negative ERAF Vehicle License Fee (VLF) adjustment. The county also used pre-average daily attendance (ADA) factors for the negative ERAF VLF computation.

The legal requirements for supplemental roll property tax apportionments and allocations are found in Revenue and Taxation Code sections 75.60 through 75.71, and 100.2. When there is a change in assessed property value due to changes in ownership or completion of new construction, the property owner is charged a supplemental property tax. This process enables the counties to retroactively tax property for the period when changes in ownership or completion of new construction occurred, rather than at the time the secured roll is developed.

Recommendation

The county should exclude multi-county schools in all future supplemental apportionments and negative ERAF VLF adjustments. The county also must use post-ADA factors for future negative ERAF VLF computations.

FINDING 2—
Unitary and operating nonunitary apportionments

The County included the ERAF in the unitary and operating nonunitary apportionments.

Requirements for the apportionment and allocation of unitary and operating nonunitary property taxes are found in Revenue and Taxation Code section 100.

Unitary properties are those properties on which the Board of Equalization "may use the principle of unit valuation in valuing properties of an assessee that are operated as a unit in the primary function of the assessee" (i.e., public utilities and railroads). The Revenue and Taxation Code further states, "Operating nonunitary properties are those that the assessee and its regulatory agency consider to be operating as a unit, but the board considers not part of the unit in the primary function of the assessee."

In FY 1988-89, the legislature established a separate system for apportioning and allocating the unitary and operating nonunitary property taxes. The legislature established the unitary and operating nonunitary base year and developed formulas to compute the distribution factors for the fiscal years that followed.

Recommendation

For all future unitary and operating nonunitary tax apportionment computations, the county should not include the ERAF.

FINDING 3—
Unitary qualified electric property apportionments

The county included all school entities in the allocation of qualified electric property tax revenues, rather than only those affected school entities within the tax rate areas. Furthermore, the county recalculated the base factors each year, rather than calculating them for only the new Qualified Electric Properties.

Requirements for the apportionment and allocation of unitary and operating nonunitary property taxes are found in Revenue and Taxation Code section 100.

Unitary properties are those properties on which the Board of Equalization "may use the principle of unit valuation in valuing properties of an assessee that are operated as a unit in the primary function of the assessee" (i.e., public utilities and railroads). The Revenue and Taxation Code further states, "Operating nonunitary properties are those that the assessee and its regulatory agency consider to be operating as a unit, but the board considers not part of the unit in the primary function of the assessee."

In FY 1988-89, the legislature established a separate system for apportioning and allocating the unitary and operating nonunitary property taxes. The legislature established the unitary and operating nonunitary base year and developed formulas to compute the distribution factors for the fiscal years that followed.

Recommendation

The county should recalculate the qualified electric property apportionment factors, beginning in FY 2009-10, to include only the affected school entities within the tax rate areas. Furthermore, the county should only calculate base factors in a year in which there are new qualified electric properties, and only for those new tax rate areas.

FINDING 4—Property tax administrative costs

The county adjusted Property Tax Administrative Fee allocation factors for the VLF and Sales and Use Tax (SUT), substantially increasing the amount of proportionate costs to cities.

Requirements for the reimbursement of county property tax administrative costs are found in Revenue and Taxation Code section 95.3. County property tax administrative costs generally are incurred by the county assessor, tax collector, assessment appeals board, and auditor-controller. The county is allowed, depending on the fiscal year and any corresponding exclusions, to be reimbursed by local agencies and public schools for these administrative costs.

Recommendation

The VLF and SUT should not be included in the administrative costs computation. It was noted that the county deposited the disputed amounts charged into an impound account. The county should refund the over-charged amounts back to the cities.

County's Response

> This office originally did not change the PTAF calculation, but felt obligated to make the revisions and place the money in trust, pending the appeal, once the superior court ruled in favor of the County of Los Angeles' calculation method in the case of City of Alhambra v County of Los Angeles. The Court of Appeal reversed that decision, and in late 2012 the California Supreme Court upheld the decision by the Court of Appeal. In 2013 this office refunded the overcharged amounts to the cities.

SCO Comment

SCO will review the corrections in the next audit.

FINDING 5—Educational Revenue Augmentation Fund (ERAF)

The county did not grow the disaster relief adjustment from FY 1997-98 through FY 2009-10. Furthermore, the county removed the disaster relief adjustment from the AB 8 calculation beginning in FY 2010-11.

The county also reversed all disaster relief adjustments from FY 1997-98 through FY 2009-10, removing $3,295,805 from the ERAF, and distributing the funds to cities and the county.

Requirements for the local agency shift of property tax revenues to the ERAF (ERAF Shift) are found in Revenue and Taxation Code sections 97.1 through 97.3.

In addition to the ERAF Shift, Revenue and Taxation Code section 97.2 requires a Disaster Relief Adjustment, beginning with the 1992-93 fiscal year. The adjustment was a reduction to the amount of reduced city and county funds that were redirected to the ERAF. This reduction was continued, without growth, through the 1996-97 fiscal year.

In FY 1997-98, the Disaster Relief Adjustment was reversed (from here on referred to as the Disaster Relief Reversal), shifting revenue from the county and cities to the ERAF. During that year, the disaster relief reversal was multiplied by the FY 1992-93 over FY 1991-92 growth.

In FY 1998-99, disaster relief reversal is included as part of the ERAF Shift, defined by Revenue and Taxation Code 97.2(e)(3), which states:

> For purposes of allocations made pursuant to section 96.1 for the 1998-99 fiscal year, the amount allocated from the Educational Revenue Augmentation Fund pursuant to this subdivision shall be deemed property tax revenues allocated to the Educational Revenue Augmentation Fund in the prior fiscal year.

Therefore, in FY 1998-99, the prior year disaster relief reversal is deemed to be revenue allocated to the ERAF in that year, and is added to the ERAF shift base, prior to the FY 1998-99 adjustment for growth. Consequently, the disaster relief reversal is grown every year thereafter, as it is included as part of the ERAF base.

Recommendation

The county should adjust the ERAF base for FY 1998-99 to include the FY 1997-98 disaster relief adjustment, prior to the FY 1998-99 adjustment for growth. The county should recalculate the ERAF amount in all subsequent years and use the adjusted ERAF amount going forward.

The county should transfer to the ERAF any underallocated amounts, beginning with FY 2005-06 (totaling approximately $2,732,584).

The county also should transfer to the ERAF the amounts reclassified in error in FY 2009-10 (totaling $3,295,805).

County's Response

> We concur and used the corrected ERAF amount beginning in 2013-14. We have begun the transfer to ERAF of the underallocated amounts from 2005-06 – 2012-13 as well as the amounts reclassified in error in FY 2009-10. In accordance with Revenue and Taxation Code 96.1(c)(3), this will be accomplished over a three year period.

SCO Comment

SCO will review the corrections in the next audit.

Lake County (July 1, 2006, through June 30, 2013)

Follow-up on prior audit findings

The county has resolved satisfactorily the findings noted in our prior audit report, issued March 30, 2007.

FINDING 1—Unitary and operating nonunitary apportionments

For FY 2007-08 through FY 2012-13, the county used incorrect AB 8 revenue amounts when allocating unitary revenues in excess of 102% of prior year revenues. The VLF amounts used also were incorrect.

Requirements for the apportionment and allocation of unitary and operating nonunitary property taxes are found in Revenue and Taxation Code section 100.

Unitary properties are those properties on which the Board of Equalization "may use the principle of unit valuation in valuing properties of an assessee that are operated as a unit in the primary function of the assessee" (i.e., public utilities, railroads, or qualified electric properties). The Revenue and Taxation Code further states, "Operating nonunitary properties are those that the assessee and its regulatory agency consider to be operating as a unit, but the board considers not part of the unit in the primary function of the assessee."

In FY 1988-89, the legislature established a separate system for apportioning and allocating the unitary and operating nonunitary property taxes. The legislature established the unitary and operating nonunitary base year and developed formulas to compute the distribution factors for the fiscal years that followed.

Recommendation

During fieldwork, the county provided corrected calculations. The county should use the corrected amounts going forward.

County's Response

> The county concurs with this finding and as stated in your draft report has provided the corrected calculations. The corrections were processed in fiscal year 2014. The county will use the corrected calculations going forward.

SCO Comment

SCO agrees with the county's corrective action. SCO will review the implementation of the corrections in the next audit.

FINDING 2—Educational Revenue Augmentation Fund

The county carried forward incorrect AB 8 base revenue and ERAF contribution amounts from the prior audit period for the year ending June 30, 2006.

Requirements for the local agency shift of property tax revenues to the ERAF are found primarily in Revenue and Taxation Code sections 97.1 through 97.3. Beginning with FY 1992-93, most local agencies were required to shift an amount of property tax revenues to the ERAF using formulas detailed in the Code.

The property tax revenues in the ERAF subsequently are allocated to the public schools using factors supplied by the county superintendent of schools.

For FY 1992-93, the ERAF shift amount for cities was determined by adding a per capita amount to a percentage of property tax revenues received by each city. The amount for counties was determined by adding a flat amount, adjusted for growth, to a per capita amount. The amount for special districts generally was determined by shifting the lesser of 10% of that district's total annual revenues as shown in the FY 1989-90 edition of the State Controller's Report on Financial Transactions Concerning Special Districts, or 40% of the FY 1991-92 property tax revenues received, adjusted for growth. Specified special districts were exempted from the shift.

For FY 1993-94, the ERAF shift for cities and counties generally was determined by:

- Reducing the FY 1992-93 ERAF shift by the FY 1992-93 per capita shift;
- Adjusting the result for growth; and
- Adding the result to a flat amount and a per capita amount determined by the Department of Finance, adjusted for growth.

The FY 1993-94 ERAF shift for special districts, other than fire districts, generally was determined by:

- Multiplying the property tax allocation for FY 1992-93, pre-ERAF, by the Special District Augmentation Fund (SDAF) factor for the district effective on June 15, 1993;
- Adjusting this amount by subtracting the FY 1992-93 shift to the ERAF;
- If the above amount is greater than zero, adjusting this amount for FY 1993-94 growth (zero is used for negative amounts); and
- Adding this amount to the FY 1992-93 ERAF shift, adjusting for growth.

For fire districts, the FY 1993-94 ERAF shift generally was determined by:

- Deducting the FY 1992-93 ERAF shift for the district from the FY 1992-93 property tax allocation;
- Multiplying the result by the SDAF factor for the district effective on June 13, 1993 (net current-year bailout equivalent);
- For a district governed by a board of supervisors, deducting the amount received from the SDAF in FY 1992-93 from the net current-year bailout equivalent; or, for an independent district, deducting the amount received from the SDAF and the difference between the net current-year bailout equivalent and the amount contributed to the SDAF from the net current-year bailout equivalent;

- Adjusting this amount for growth; and
- Adding this amount to the FY 1992-93 ERAF shift, adjusted for growth.

For fiscal years subsequent to FY 1993-94, the amounts determined are adjusted for growth annually to determine the ERAF shift amounts for that year.

Recommendation

During fieldwork, the county provided corrected calculations, resulting in a net overpayment to the ERAF of $691,282.

The county should make the necessary adjustments to correct this error, and use the corrected calculations going forward.

County's Response

> The county concurs with this finding and as stated in your draft report has provided the corrected calculations. The corrections were processed in fiscal year 2014 up to the amount allowed pursuant to Revenue and Taxation Code 96.1. The county will use the corrected calculations going forward.

SCO Comment

SCO agrees with the county's corrective action. SCO will review the implementation of the corrections in the next audit.

FINDING 3—Vehicle Licensing Fee (VLF) and Sales and Use Tax (SUT) adjustments

The county used incorrect assessed values to compute the VLF growth for the county and cities in FY 2006-07 through FY 2012-13. Requirements for the ERAF adjustment for the VLF and SUT are found in Revenue and Taxation Code sections 97.68-97.70.

In FY 2004-05 the county was given a VLF estimate that was to be transferred from the ERAF to the Vehicle License Fee Property Tax Compensation Fund, and eventually to the county and cities. In FY 2005-06, the county was given another estimate, including true-ups. In FY 2006-07 and subsequent years, the county calculated the VLF adjustment based on the prior year VLF adjusted for growth. The growth for the county's VLF should be based on countywide growth, not only on unincorporated parcels. The growth for each city's VLF should be based on the growth of all incorporated parcels in all Tax Rate Areas (TRAs) within the city.

The SUT amounts for each county and cities within the county are provided by the Department of Finance, on or before September 1 of each fiscal year. These amounts are to be transferred from the ERAF to the Sales and Use Tax Compensation Fund, and eventually to the county and designated cities within each county.

Recommendation

During fieldwork, the county provided corrected VLF calculations, showing a net underpayment to the cities and county from the ERAF of $216,722.

The county should make the necessary adjustments to correct this error, and use the corrected calculations going forward.

County's Response

> The county concurs with this finding and as stated in your draft report has provided the corrected calculations. The corrections were processed in fiscal year 2014 up to the amount allowed pursuant to Revenue and Taxation Code 96.1. The county will use the corrected calculations going forward.

SCO Comment

SCO agrees with the county's corrective action. SCO will review the implementation of the corrections in the next audit.

Lassen County (July 1, 2004, through June 30, 2012)

Follow-up on prior audit findings

Our prior audit report, issued January 2005, disclosed no findings related to the apportionment and allocation of property tax revenues by the county.

FINDING 1—Unitary and operating nonunitary apportionments

During all fiscal years under audit, FY 2004-05 through FY 2011-12, the county included the ERAF in the unitary apportionment.

Requirements for the apportionment and allocation of unitary and operating nonunitary property taxes are found in Revenue and Taxation Code section 100.

Unitary properties are those properties on which the Board of Equalization "may use the principle of unit valuation in valuing properties of an assessee that are operated as a unit in the primary function of the assessee" (i.e., public utilities and railroads). The Revenue and Taxation Code further states, "Operating nonunitary properties are those that the assessee and its regulatory agency consider to be operating as a unit, but the board considers not part of the unit in the primary function of the assessee."

In FY 1988-89, the legislature established a separate system for apportioning and allocating the unitary and operating nonunitary property taxes. The legislature established the unitary and operating nonunitary base year and developed formulas to compute the distribution factors for the fiscal years that followed.

The county corrected the finding during audit fieldwork by recalculating the unitary apportionment to exclude the ERAF. The calculations resulted in an overallocation to the ERAF of $956,107.

Recommendation

The county should transfer funds to correct any misallocated amounts. The county should exclude the ERAF from the unitary apportionment in subsequent years.

County's Response

> The question of whether ERAF should be included in the unitary apportionment has been an ongoing issue across the state, caused by inconsistency in the Revenue and Taxation Code. The methodology historically used by Lassen County to apportion unitary property tax amounts were completed in accordance with documented guidelines.

SCO Comment

In the past, the inclusion of ERAF in the unitary apportionment was accepted as correct. However, it has been determined that this method no longer is correct, and the ERAF should not receive a share of unitary revenues.

FINDING 2—Unitary and operating nonunitary apportionments

In FY 2007-08, the county did not properly establish the base for unitary railroad properties.

Requirements for the apportionment and allocation of unitary and operating nonunitary property taxes are found in Revenue and Taxation Code section 100.

Unitary properties are those properties on which the Board of Equalization "may use the principle of unit valuation in valuing properties of an assessee that are operated as a unit in the primary function of the assessee" (i.e., public utilities and railroads). The Revenue and Taxation Code further states, "Operating nonunitary properties are those that the assessee and its regulatory agency consider to be operating as a unit, but the board considers not part of the unit in the primary function of the assessee."

In FY 1988-89, the legislature established a separate system for apportioning and allocating the unitary and operating nonunitary property taxes. The legislature established the unitary and operating nonunitary base year and developed formulas to compute the distribution factors for the fiscal years that followed.

The county corrected the finding during audit fieldwork by establishing the base year for unitary railroad properties and adjusting all apportionments affected. This included making the appropriate jurisdictional changes in FY 2007-08 and recalculating AB 8 in subsequent years. The county's calculations included an underallocation to the ERAF of $42,467.

Recommendation

The county should transfer funds to correct any misallocated amounts.

FINDING 3—Unitary and operating nonunitary apportionments

During FY 2007-08 through FY 2011-12, the county included the railroad properties as part of the unitary and operating nonunitary apportionment.

Requirements for the apportionment and allocation of unitary and operating nonunitary property taxes are found in Revenue and Taxation Code section 100.

Unitary properties are those properties on which the Board of Equalization "may use the principle of unit valuation in valuing properties of an assessee that are operated as a unit in the primary function of the assessee" (i.e., public utilities and railroads). The Revenue and Taxation Code further states, "Operating nonunitary properties are those that the assessee and its regulatory agency consider to be operating as a unit, but the board considers not part of the unit in the primary function of the assessee."

In FY 1988-89, the legislature established a separate system for apportioning and allocating the unitary and operating nonunitary property taxes. The legislature established the unitary and operating nonunitary base year and developed formulas to compute the distribution factors for the fiscal years that followed.

The county corrected the finding during audit fieldwork by recalculating the unitary and operating non-unitary allocations, excluding railroad. The county also calculated railroad allocations in accordance with Revenue and Taxation Code section 100. The county's calculations showed an underallocation to the ERAF of $117,684.

Recommendation

The county should transfer funds to correct any misallocated amounts. The county should calculate the railroad apportionment separately in subsequent years.

FINDING 4—Property tax administrative costs

In FY 2007-08 through FY 2011-12, the county adjusted the SB 2557 Property Tax Administration (PTA) fee allocation factors for Vehicle Licensing Fee (VLF) and Sales and Use Tax (SUT).

Requirements for the reimbursement of county property tax administrative costs are found in Revenue and Taxation Code section 95.3. County property tax administrative costs generally are incurred by the offices of the county assessor, tax collector, assessment appeals board, and auditor. The county is allowed, depending on the fiscal year and any corresponding exclusions, to be reimbursed by local agencies and public schools for these administrative costs.

Recommendation

The county should recalculate the PTA fee allocation factors and refund the cities any overcharged amounts. The county should provide the SCO with proof of the corrections. In subsequent years, the county should not include SUT and VLF adjustments in its PTA fee allocation factors.

County's Response

> Finding 4 – should not be characterized as an error. The question of whether SUT and VLF adjustments should be included in PTA Fee allocation factors has been an ongoing issue across the state. The question was resolved by a California Supreme Court decision in November 2012. The City of Susanville has been refunded the amount overcharged (check #1059984 – attached).

SCO Comment

The California Supreme Court determined that counties must make retroactive adjustments to their PTA fee allocations. The county has provided corrected calculations; however, the adjustments were made outside of the scope of the audit. Therefore, the initial calculation was deemed an error during the audit period. SCO accepts the county's adjustments with the verification of payment attached to its response to the draft audit report.

FINDING 5—Educational Revenue Augmentation Fund

For FY 2007-08 through FY 2011-12, the county omitted the City of Susanville from the countywide assessed value when calculating VLF growth.

Requirements for the ERAF adjustment for the VLF are found in Revenue and Taxation Code section 97.70. The code requires countywide growth to be calculated based on the entire county, not only on unincorporated parcels.

The county corrected the finding during audit fieldwork by recalculating the VLF.

Recommendation

The county should refund the ERAF any amounts that were under-allocated because of the error. Furthermore, the county should correct its negative ERAF calculations and refund any overcharged amounts to schools. There should be no net effect to the ERAF as a result of these changes. Going forward, the county should include incorporated parcels in the countywide VLF growth calculation.

FINDING 6—Negative bailout (SB 85)

The county incorrectly calculated the negative bailout amount. The county also incorrectly applied the negative bailout amount, resulting in a decrease to its ERAF contribution, totaling $57,935.

After the passage of Proposition 13, the legislature passed SB 154 (Chapter 292, Statutes of 1978), which provided for the distribution of State assistance, or bailout, to make up, in part, for local property tax losses. The relief for counties was $436 million in cash grants plus the State's assumption of $1 billion associated with mandated health and welfare programs.

In the second year following the passage of Proposition 13, the legislature passed AB 8 (Chapter 282, Statutes of 1979), which provided for a long-term solution consisting of a one-time adjustment (shift) that created a new property tax base for each local agency.

Counties received 100% of their SB 154 block grants and a small adjustment for the Aid to Families with Dependent Children program, minus the amount of the indigent health block grant. For some counties, the value of the indigent health block grant was so great that it exceeded the value of the SB 154 block grant. In those cases, the AB 8 shift resulted in a reduction of the property tax base instead of an increase. These counties are referred to as "negative bailout counties." For all but the negative bailout counties, the increased property tax was deducted from the schools' property taxes. For the negative bailout counties, school property taxes were supposed to increase by the negative bailout amount in the respective counties.

Subsequently, it was discovered that the negative bailout counties were not transferring the required property taxes to the schools. Consequently, the legislature passed AB 2162 (Chapter 899, Statutes of 1983), forgiving prior allocation errors but requiring future payments to be made in accordance with statute.

The negative bailout amount has grown each year as the assessed value of property in the counties has grown. In 2010, the legislature passed SB 85 (Chapter 5, Statutes of 2010), which did not eliminate the negative bailout amount, but capped it according to a specified formula.

Recommendation

The county should reverse the decrease to its ERAF contribution for FY 2011-12 ($57,935.33) and all subsequent adjustments.

For FY 2011-12, the county should decrease the AB 8 property tax allocations for school entities by a proportionate amount of the current-year SB 85 negative bailout amount ($64,471). It should then increase the AB 8 property tax allocations for school entities by a proportionate amount of the lesser of current- or prior-year SB 85 negative bailout amounts ($64,471 and $66,233, respectively), with the difference going to the county (in this instance $0).

The county should perform the same process mentioned above for FY 2012-13; the SB 85 negative bailout amount is $62,150.

As the county has been experiencing decrement, the negative bailout adjustment will have no net effect on property tax allocations for FY 2011-12 and FY 2012-13. However, the calculations should be completed, as the adjustment will change the allocation amounts in subsequent years.

For FY 2013-14 and every year thereafter, the county should decrease the AB 8 property tax allocations for school entities by a proportionate amount of the current year SB 85 negative bailout amount ($62,150 adjusted annually for countywide growth). The county should then increase the AB 8 property tax allocations for school entities by a proportionate amount of the increase amount used in the prior year ($62,150), with the difference going to the county.

County's Response

> Finding 6 – I do not agree with this finding. The negative bailout amount was calculated correctly, according to SB 85 with a capped amount of $57,218. However, due to the recommendation in the draft audit the county will adjust the SB 85 negative bailout amount.

SCO Comment

The negative bailout amount provided to the county was based on annual reports of assessed value provided to SCO. The county's calculations rely on assessed values that are updated throughout the year and may more accurately reflect actual assessed value for the given fiscal years. The county may use its calculated negative bailout cap of $57,218, as long as it applies the amount using the prescribed methodology.

Los Angeles County (July 1, 2009, through June 30, 2013)

Follow-up on prior audit findings

The county has satisfactorily resolved the findings noted in our prior audit report, issued December 10, 2010.

Conclusion

Our audit found that the county complied with California statutes for the allocation and apportionment of property tax revenues for the period audited.

Additionally, we made the following observations:

1. The county computed total net administrative costs including VLF and SUT up to FY 2011-12. As a result, the administrative prorata share costs were computed incorrectly, substantially increasing the amount of proportionate costs to cities. The county removed VLF and SUT from the administrative cost calculation for FY 2012-13 forward.

    a. VLF and SUT are not to be included in the administrative costs computation. We noted that the county is in the process of correcting the disputed amounts. The county must complete the refund of the overcharge back to the cities.

    b. This issue will be kept open for follow-up in the next audit.

2. The county's process for calculating and allocating Tax Equity Allocation (TEA) has been accepted in the past; however, a legal challenge in another county has raised the possibility that the TEA may not be in full compliance with the Revenue and Taxation Code.

a. We noted that the county is in the process of completing calculations to ensure proper computation of the TEA.

b. This issue will be kept open for follow-up in a subsequent audit.

Marin County (July 1, 2004, through June 30, 2011)

Follow-up on prior audit findings

Our prior audit report, issued October 15, 2005, included no findings related to the apportionment and allocation of property tax revenues by the county.

FINDING 1—Jurisdictional changes

The county computed new tax rate area (TRA) factors for all entities following jurisdictional changes.

The legal requirements for jurisdictional changes are found in Revenue and Taxation Code section 99. A jurisdictional change involves a change in the organization or boundaries of a local government agency or school district. Normally, these are service area or responsibility changes among the local jurisdictions. As part of the jurisdictional change, the local government agencies are required to negotiate any exchange of base-year property tax revenue and annual tax increment. After the jurisdictional change, the local agency for which responsibility increased, receives additional annual tax increment, and the base property tax revenues are adjusted according to the negotiated agreements.

Recommendation

The county must review and correct all jurisdictional changes to ensure that only entities for which service responsibilities were changed, have adjustments to their TRA factors.

FINDING 2—Unitary and operating nonunitary apportionments

The county included the Educational Revenue Augmentation Fund (ERAF) in the unitary apportionment.

Requirements for the apportionment and allocation of unitary and operating nonunitary property taxes are found in Revenue and Taxation Code section 100.

Unitary properties are those properties on which the Board of Equalization "may use the principle of unit valuation in valuing properties of an assessee that are operated as a unit in the primary function of the assessee" (i.e., public utilities, railroads, or qualified electric properties). The Revenue and Taxation Code further states, "Operating nonunitary properties are those that the assessee and its regulatory agency consider to be operating as a unit, but the board considers not part of the unit in the primary function of the assessee."

In fiscal year 1988-89, the legislature established a separate system for apportioning and allocating the unitary and operating nonunitary property taxes. The legislature established the unitary and operating nonunitary base year and developed formulas to compute the distribution factors for the fiscal years that followed.

Recommendation

The ERAF must be removed from the unitary apportionment and allocation and the ERAF revenue base distributed to all appropriate taxing jurisdictions.

FINDING 3—Property tax administrative costs

The county included the Sales and Tax (SUT) and Vehicle License Fee (VLF) revenues received by cities in the calculation of SB 2557 administrative cost computations.

Requirements for the reimbursement of county property tax administrative costs are found in Revenue and Taxation Code section 95.3. County property tax administrative costs are incurred by the county assessor, tax collector, assessment appeals board, and auditor. The county is allowed, depending on the fiscal year and any corresponding exclusions, to be reimbursed by local agencies and public schools for these administrative costs.

Recommendation

The county must recalculate the administrative costs for all years that included the SUT and/or VLF for cities and reimburse the cities for any amounts charged in excess of the corrected amounts without SUT and VLF.

Modoc County (July 1, 2004, through June 30, 2012)

Follow-up on prior audit findings

Findings noted in our prior audit, issued September 2005, have been satisfactorily resolved by the county, except that the county continues to exclude the State-assessed local utility roll from the tax increment calculations.

FINDING 1—Calculation and distribution of annual tax increment (ATI)

The county's secured assessed value does not include the local utility value for fiscal year (FY) 2006-07, and FY 2008-09 through FY 2011-12.

Requirements for the apportionment and allocation of the annual tax increment (ATI) are found in Revenue and Taxation Code sections 96 through 96.5. The annual increment of property tax, which is the change in assessed value from one year to the next, is allocated to tax rate areas (TRA) on the basis of each TRA's share of the incremental growth in assessed valuations. The tax increment is then multiplied by the jurisdiction's annual tax increment apportionment factors for each TRA. These factors were developed in the 1979-80 base year and are adjusted for jurisdictional changes. The tax increment is then added to the tax computed for the prior fiscal year to develop the apportionment for the current fiscal year.

Recommendation

The county should include local utility assessed values with the secured values.

FINDING 2—Jurisdictional changes

The county included the Cedarville Water District annexation in the FY 2011-12 AB 8 allocation prior to authorization. The State Board of Equalization (BOE) change notice stated the change was to be implemented in FY 2013-14.

In addition, the county did not implement a jurisdictional change for adding Last Frontier Healthcare District to its AB 8 calculations for FY 2011-12.

The legal requirements for jurisdictional changes are found in Revenue and Taxation Code section 99. A jurisdictional change involves a change in the organization or boundaries of a local government agency or school district. Normally, these are service area or responsibility changes between the local jurisdictions. As part of the jurisdictional change, the local government agencies are required to negotiate any exchange of base year property tax revenue and annual tax increment. After the jurisdictional change, the local agency for which responsibility increased, receives additional annual tax increment, and the base property tax revenues are adjusted according to the negotiated agreements.

Recommendation

The county should develop controls to ensure that directives from the Board of Equalization are implemented in a timely manner.

FINDING 3—Supplemental property tax

In verifying the supplemental property tax allocations, we noted that prior to FY 2011-12, the county did not adjust AB 8 factors for school average daily attendance (ADA) revenue.

The legal requirements for supplemental roll property tax apportionments and allocations are found in Revenue and Taxation Code sections 75.60 through 75.71, and 100.2. When there is a change in assessed property values due to changes in ownership or completion of new construction, the property owner is charged a supplemental property tax. This process enables the counties to retroactively tax property for the period when changes in ownership or completion of new construction occurred, rather than at the time the secured roll is developed.

Recommendation

The county should use AB 8 factors adjusted for ADA in the allocation of supplemental property tax revenue.

FINDING 4—Unitary, operating nonunitary, pipeline, and railroad apportionments

In the apportionment of unitary property taxes, the county made the following computations:

- For FY 2011-12, the county used AB 8 factors instead of unitary factors.
- For FY 2004-05 through FY 2011-12, the county included ERAF.
- For FY 2007-08 through FY 2011-12, the county included railroad property taxes.

Requirements for the apportionment and allocation of unitary and operating nonunitary property taxes are found in Revenue and Taxation Code section 100.

Unitary properties are those properties on which the Board of Equalization "may use the principle of unit valuation in valuing properties of an assessee that are operated as a unit in the primary function of the assessee" (i.e., public utilities, railroads, or qualified electric properties). The Revenue and Taxation Code further states, "Operating nonunitary properties are those that the assessee and its regulatory agency consider to be operating as a unit, but the board considers not part of the unit in the primary function of the assessee."

In FY 1988-89, the legislature established a separate system for apportioning and allocating the unitary and operating nonunitary property taxes. The legislature established the unitary and operating nonunitary base year and developed formulas to compute the distribution factors for the fiscal years that followed.

Recommendation

During audit fieldwork, the county corrected the findings by recomputing the pipeline, unitary, and railroad property tax apportionments. In subsequent years, the county should allocate unitary, pipeline, and railroad property tax revenues in accordance with Revenue and Taxation Code 100.

County's Response

> 2. On page 8, under Recommendation for Finding 4, the report states: "The county should transfer funds to correct any misallocated amounts." The first paragraph on page 7 (under finding 4) refers to the inclusion of ERAF in the pipeline allocation, and the second bullet item on page 7 refers to the removal of ERAF from the unitary. These were not misallocations as stated in the recommendation section. It's up to the County to determine whether the SCO's recent opinion will be applied to years before 2012/13. Please specify this in the recommendation section, or clarify on page 7 that the inclusion of ERAF was not a misallocation.

SCO Comment

The finding and recommendation has been modified to reflect the county's concern, noting that the ERAF was included.

FINDING 5—Educational Revenue Augmentation Fund

The county incorrectly calculated the Vehicle Licensing Fee (VLF) adjustment for FY 2006-07 through FY 2011-12, and could not substantiate the assessed values used in the growth computations for FY 2006-07 through FY 2009-10.

Requirements for the local agency shift of property tax revenues to the ERAF primarily are found in Revenue and Taxation Code sections 97.1 through 97.3. Beginning in FY 1992-93, most local agencies were required to shift an amount of property tax revenues to the ERAF using formulas detailed in the code. The property tax revenues in the ERAF

subsequently are allocated to the public schools using factors supplied by the county superintendent of schools.

For FY 1992-93, the ERAF shift amount for cities was determined by adding a per capita amount to a percentage of property tax revenues received by each city. The amount for counties was determined by adding a flat amount, adjusted for growth, to a per capita amount. The amount for special districts generally was determined by shifting the lesser of 10% of that district's total annual revenues as shown in the FY 1989-90 edition of the State Controller's Report on Financial Transactions Concerning Special Districts, or 40% of the FY 1991-92 property tax revenues received, adjusted for growth. Specified special districts were exempted from the shift.

For FY 1993-94, the ERAF shift for cities and counties generally was determined by:

- Reducing the FY 1992-93 ERAF shift by the FY 1992-93 per capita shift;
- Adjusting the result for growth; and
- Adding the result to a flat amount and a per capita amount determined by the Department of Finance, adjusted for growth.

The FY 1993-94 ERAF shift for special districts, other than fire districts, generally was determined by:

- Multiplying the property tax allocation for FY 1992-93, pre-ERAF, by the Special District Augmentation Fund (SDAF) factor for the district effective on June 15, 1993;
- Adjusting that amount by subtracting the FY 1992-93 shift to the ERAF;
- If the above amount is greater than zero, adjusting that amount for FY 1993-94 growth (zero is used for negative amounts); and
- Adding that amount to the FY 1992-93 ERAF shift, adjusting for growth.

For fire districts, the FY 1993-94 ERAF shift generally was determined by:

- Deducting the FY 1992-93 ERAF shift for the district from the FY 1992-93 property tax allocation;
- Multiplying that result by the SDAF factor for the district effective on June 13, 1993 (net current-year bailout equivalent);
- For a district governed by a board of supervisors, deducting the amount received from the SDAF in FY 1992-93 from the net current-year bailout equivalent; or, for an independent district, deducting the amount received from the SDAF and the difference between the net current-year bailout equivalent and the amount contributed to the SDAF from the net current-year bailout equivalent;

- Adjusting that amount for growth; and
- Adding that amount to the FY 1992-93 ERAF shift, adjusted for growth.

For fiscal years after FY 1993-94, the amounts determined are adjusted for growth annually to determine the ERAF shift amounts for that year.

Recommendation

The county should recompute the VLF adjustment for FY 2006-07 through FY 2011-12, using the correct assessed values, and adjust any misapportioned property tax revenues.

During the SCO reviews in FY 2006 and FY 2009, we noted several errors in the Sales and Use Tax and Vehicle License Fee (VLF) computations and apportionments. The county made correcting adjustments during the current audits. Therefore, any reapportionments required by the current audit are limited to FY 2010-11 and FY 2011-12.

The county and the SCO recalculated the VLF in the current audit and found underallocations of $65,694 to the county and $15,225 to the City of Alturas, pertaining to FY 2010-11 and FY 2011-12.

Riverside County (July 1, 2005, through June 30, 2013)

Follow-up on prior audit findings

Our prior audit report, issued March 2007, disclosed no findings related to the apportionment and allocation of property tax revenues by the county.

FINDING—Unitary and operating nonunitary apportionments

The county's unitary allocation system includes the Educational Revenue Augmentation Fund (ERAF). This calculation resulted in an over-apportionment to the ERAF.

Requirements for the apportionment and allocation of unitary and operating nonunitary property taxes are found in Revenue and Taxation Code section 100.

Unitary properties are those properties on which the Board of Equalization "may use the principle of unit valuation in valuing properties of an assessee that are operated as a unit in the primary function of the assessee" (i.e., public utilities, railroads, or qualified electric properties). The Revenue and Taxation Code further states, "Operating nonunitary properties are those that the assessee and its regulatory agency consider to be operating as a unit, but the board considers not part of the unit in the primary function of the assessee."

For fiscal year (FY) 1988-89, the legislature established a separate system for apportioning and allocating the unitary and operating nonunitary property taxes. The legislature established the unitary and operating nonunitary base year and developed formulas to compute the distribution factors for the fiscal years that followed.

Recommendation

The county should remove the ERAF from the unitary apportionment.

City and County of San Francisco (July 1, 2007, through June 30, 2012)

Follow-up on prior audit findings

The county satisfactorily has resolved the findings noted in our prior audit report, issued December 2008.

FINDING 1—Calculation and distribution of annual tax increment (ATI)

In fiscal year (FY) 2010-11 and FY 2011-12, the county rounded the base tax rate (AB 8 factors) to four decimal places.

Requirements for the apportionment and allocation of the annual tax increment (ATI) are found in Revenue and Taxation Code sections 96 through 96.5. The annual increment of property tax, which is the change in assessed value from one year to the next, is allocated to tax rate areas (TRA) on the basis of each TRA's share of the incremental growth in assessed valuations. The tax increment is then multiplied by the jurisdiction's ATI apportionment factors for each TRA. These factors were developed in the 1979-80 base year and are adjusted for jurisdictional changes. The tax increment is then added to the tax computed for the prior fiscal year to develop the apportionment for the current fiscal year.

Recommendation

While the finding per any single fund is immaterial for the periods under audit, over time the dollar amounts incorrectly allocated will grow to a material amount.

The county should use factors with a minimum of eight decimal places.

FINDING 2—Unitary railroad apportionments

From FY 2007-08 through FY 2011-12, the county made the following errors in determining the allocation of unitary railroad property tax revenues:

- Excluded the ERAF
- Used incorrect redevelopment agency (RDA) factors

During the audit period, these errors caused:

- The ERAF to be underallocated by $133,583
- The General Fund to be overallocated by $113,907 (including portions in the Children's, Library Preservation, and Open Space funds)
- RDAs to be overallocated by $22,563

Requirements for the apportionment and allocation of unitary and operating nonunitary property taxes are found in Revenue and Taxation Code section 100.

Unitary properties are those properties on which the Board of Equalization "may use the principle of unit valuation in valuing properties of an assessee that are operated as a unit in the primary function of the assessee" (i.e., public utilities and railroads). The Revenue and Taxation Code further states, "Operating nonunitary properties are those that the assessee and its regulatory agency consider to be operating as a unit, but the board considers not part of the unit in the primary function of the assessee."

In FY 1988-89, the legislature established a separate system for apportioning and allocating the unitary and operating nonunitary property taxes. The legislature established the unitary and operating nonunitary base year and developed formulas to compute the distribution factors for the fiscal years that followed.

Recommendation

The county should remit from the General Fund its portion of the underpayment to the ERAF ($113,907).

RDAs have since been dissolved and misapportioned revenues have either been used for a debt obligation or redistributed to the affected entities.

FINDING 3—Unitary qualified electric property apportionments

In FY 2011-12, the county made the following errors in determining the allocation of unitary qualified electric property tax revenues:

- Excluded the ERAF
- Included RDAs

During the audit period, these errors caused:

- The ERAF to be underallocated by $255,405
- The General Fund to be overallocated by $255,516 (including portions in the Children's, Library Preservation, and Open Space funds)
- RDAs to be overallocated by $199,678

Requirements for the apportionment and allocation of unitary and operating nonunitary property taxes are found in Revenue and Taxation Code section 100.

Unitary properties are those properties on which the Board of Equalization "may use the principle of unit valuation in valuing properties of an assessee that are operated as a unit in the primary function of the assessee" (i.e., public utilities and railroads). The Revenue and Taxation Code further states, "Operating nonunitary properties are those that the assessee and its regulatory agency consider to be operating as a unit, but the board considers not part of the unit in the primary function of the assessee."

In FY 1988-89, the legislature established a separate system for apportioning and allocating the unitary and operating nonunitary property taxes. The legislature established the unitary and operating nonunitary base year and developed formulas to compute the distribution factors for the fiscal years that followed.

Recommendation

The county should remit from the General Fund the underpayment to the ERAF in the amount of $255,405.

RDAs have since been dissolved and misapportioned revenues have either been used for a debt obligation or redistributed to the affected entities.

Santa Clara County (July 1, 2007, through June 30, 2013)

Follow-up on prior audit findings

Findings noted in our prior audit, issued December 31, 2009, have been resolved satisfactorily by the county, with the exception of having included the ERAF in the unitary apportionment. However, the county has begun implementing the removal of the ERAF as of FY 2013-14. The SCO will review the implementation during the next audit.

Conclusion

Our audit found that the county complied with California statutes for the allocation and apportionment of property tax revenues for the period audited.

Santa Cruz County (July 1, 2006, through June 30, 2013)

Follow-up on prior audit findings

Our prior audit report, issued July 2008, included no findings related to the apportionment and allocation of property tax revenues by the county.

Conclusion

Our audit found that the county complied with California statutes for the allocation and apportionment of property tax revenues for the period audited.

Additionally, we made the following observation:

The county computed total net administrative costs, including vehicle license fee/sales and use tax (VLF/SUT), up until FY 2011-12. As a result, the administrative prorata share of costs was overstated, substantially increasing the amount of proportionate costs to cities. The county removed VLF/SUT from the administrative cost calculation for FY 2012-13 forward.

VLF and SUT is not to be included in the administrative costs computation. We noted that the county is in the process of negotiating the disputed amounts. The county must complete the refund or agreement of the over-charge back to the cities.

This issue will be kept open for follow-up in the subsequent audit.

San Mateo County (July 1, 2005, through June 30, 2013)

Follow-up on prior audit findings

Findings noted in our prior audit, issued February 13, 2009, have been satisfactorily resolved by the county, with the exception of having included the ERAF in unitary and operating nonunitary apportionments.

FINDING 1—Unitary and operating nonunitary apportionments

The county's unitary allocation system includes the ERAF. This calculation resulted in an under-apportionment to all agencies receiving unitary property tax revenues.

Requirements for the apportionment and allocation of unitary and operating nonunitary property taxes are found in Revenue and Taxation Code section 100.

Unitary properties are those properties on which the Board of Equalization "may use the principle of unit valuation in valuing properties of an assessee that are operated as a unit in the primary function of the assessee" (i.e., public utilities, railroads, or qualified electric properties). The Revenue and Taxation Code further states, "Operating nonunitary properties are those that the assessee and its regulatory agency consider to be operating as a unit, but the board considers not part of the unit in the primary function of the assessee."

For FY 1988-89, the legislature established a separate system for apportioning and allocating the unitary and operating nonunitary property taxes. The legislature established the unitary and operating nonunitary base year and developed formulas to compute the distribution factors for the fiscal years that followed.

Recommendation

The county should not include the ERAF in unitary apportionments.

County's Response

> Whether or not to include ERAF in the unitary and operating nonunitary apportionments is an unsettled question across the State. Our understanding is that the California Property Tax Managers Group has been working closely with the SCO to develop a revised methodology for apportioning unitary property tax revenues. We intend to revise our unitary apportionment methodology as needed once that process is complete and further guidance has been issued.

SCO Comment

SCO agrees with the county's corrective action and will review the corrections in the next audit.

FINDING 2—Unitary railroad apportionments

The county included redevelopment agencies (RDAs) and excluded the ERAF in the base unitary railroad allocation, instead of excluding RDAs and including the ERAF.

Requirements for the apportionment and allocation of unitary and operating nonunitary property taxes are found in Revenue and Taxation Code section 100.

Unitary properties are those properties on which the Board of Equalization "may use the principle of unit valuation in valuing properties of an assessee that are operated as a unit in the primary function of the assessee" (i.e., public utilities, railroads, or qualified electric properties). The Revenue and Taxation Code further states, "Operating nonunitary properties are those that the assessee and its regulatory agency consider to be operating as a unit, but the board considers not part of the unit in the primary function of the assessee."

For FY 1988-89, the legislature established a separate system for apportioning and allocating the unitary and operating nonunitary property taxes. The legislature established the unitary and operating nonunitary base year and developed formulas to compute the distribution factors for the fiscal years that followed.

Recommendation

The county should apportion unitary railroad revenues based on the corrected factors.

County's Response

> The County Controller's Office identified that the redevelopment agencies were incorrectly included in the FY 2007-08 base year unitary railroad allocations and accordingly made a prior period adjustment in FY 2008-09. The County has provided SCO staff with the supporting documentation showing the correction was made in FY 2008-09.
>
> We agree that ERAF should have been included in the FY 2007-08 base year unitary railroad allocations. Based on the recommendations provided by the SCO, the County had taken steps to ensure our calculations are correct going forward.

SCO Comment

SCO has reviewed the corrections to railroad apportionments to RDAs and agrees with the county's corrective actions. SCO will review additional corrections in the next audit.

FINDING 3—Unitary railroad apportionments

In FY 2009-10 through FY 2012-13, the county apportioned unitary railroad revenues up to 102% of prior year revenues using base-year factors, instead of using the prior-year unitary railroad apportionment factors.

Requirements for the apportionment and allocation of unitary and operating nonunitary property taxes are found in Revenue and Taxation Code section 100.

Unitary properties are those properties on which the Board of Equalization "may use the principle of unit valuation in valuing properties of an assessee that are operated as a unit in the primary function of the assessee" (i.e., public utilities, railroads, or qualified electric properties). The Revenue and Taxation Code further states, "Operating nonunitary properties are those that the assessee and its regulatory agency consider to be operating as a unit, but the board considers not part of the unit in the primary function of the assessee."

In FY 1988-89, the legislature established a separate system for apportioning and allocating the unitary and operating nonunitary property taxes. The legislature established the unitary and operating nonunitary base year and developed formulas to compute the distribution factors for the fiscal years that followed.

During audit fieldwork, the county recalculated the FY 2009-10 through FY 2012-13 apportionments. The county used the prior-year unitary railroad factors for the apportionment of up to 102% in accordance with the Revenue and Taxation Code.

Recommendation

The county should apportion unitary railroad revenues up to 102% of prior year revenues based on prior year unitary railroad factors.

County's Response

> We agree that the unitary railroad revenues up to 102% of the prior year amount should be apportioned based on the prior year unitary railroad factors rather that base year factors. Based on recommendations provided by the SCO, the County has taken steps to ensure our calculations are correct going forward.

SCO Comment

SCO agrees with the county's corrective action and will review the corrections in the next audit.

Stanislaus County (July 1, 2006, through June 30, 2013)

Follow-up on prior audit findings

Findings noted in our prior audit, issued December 2008, have been resolved satisfactorily by the county, with the exception of having included the ERAF in the unitary apportionments.

FINDING 1—Calculation and distribution of annual tax increment (ATI)

In FY 2006-07, FY 2007-08, and FY 2009-10 through FY 2012-13, the county did not carry forward gross tax amounts from the prior year.

Requirements for the apportionment and allocation of the annual tax increment (ATI) are found in Revenue and Taxation Code sections 96 through 96.5. The annual increment of property tax, which is the change in assessed value from one year to the next, is allocated to tax rate areas (TRA) on the basis of each TRA's share of the incremental growth in

assessed valuations. The tax increment is then multiplied by the jurisdiction's annual tax increment apportionment factors for each TRA. These factors were developed in the 1979-80 base year and are adjusted for jurisdictional changes. The tax increment is then added to the tax computed for the prior fiscal year to develop the apportionment for the current fiscal year.

Recommendation

The county should review the issue and make the necessary corrections to the tax amounts used to calculate AB 8 factors. Going forward, the county should use the corrected tax amounts in calculating AB 8 factors.

County's Response

> The county agrees with the finding and will follow the recommendation to use the corrected tax amounts and AB 8 factors going forward.

FINDING 2—Unitary and operating nonunitary apportionments

For FY 2006-07 through FY 2012-13, the county included the ERAF in the unitary apportionment.

Requirements for the apportionment and allocation of unitary and operating nonunitary property taxes are found in Revenue and Taxation Code section 100.

Unitary properties are those properties on which the Board of Equalization "may use the principle of unit valuation in valuing properties of an assessee that are operated as a unit in the primary function of the assessee" (i.e., public utilities, railroads, or qualified electric properties). The Revenue and Taxation Code further states, "Operating nonunitary properties are those that the assessee and its regulatory agency consider to be operating as a unit, but the board considers not part of the unit in the primary function of the assessee."

In FY 1988-89, the legislature established a separate system for apportioning and allocating the unitary and operating nonunitary property taxes. The legislature established the unitary and operating nonunitary base year and developed formulas to compute the distribution factors for the fiscal years that followed.

Recommendation

The county should not include the ERAF in future unitary apportionments.

County's Response

> To address this statewide issue, the State Association of County Auditors has revised the California Property Tax Managers' Manual. The county will be following the procedures in the manual for removing ERAF from future unitary apportionments.

Trinity County (July 1, 2005, through June 30, 2013)

Follow-up on prior audit findings

Our prior audit report, issued December 8, 2006, did not disclose findings related to the apportionment and allocation of property tax revenues by the county.

FINDING 1—Calculation and distribution of annual tax increment (ATI)

In FY 2012-13, the county did not carry forward prior-year revenues when adding the annual tax increment. This error caused the countywide AB 8 factors to be incorrect, resulting in a misallocation of property tax revenues to all jurisdictions, including an underallocation of approximately $42,700 to the county and $50,500 to the ERAF.

Requirements for the apportionment and allocation of the annual tax increment (ATI) are found in Revenue and Taxation Code sections 96 through 96.5. The annual increment of property tax, which is the change in assessed value from one year to the next, is allocated to tax rate areas (TRA) on the basis of each TRA's share of the incremental growth in assessed valuations. The tax increment is then multiplied by the jurisdiction's annual tax increment apportionment factors for each TRA. These factors were developed in the 1979-80 base year and are adjusted for jurisdictional changes. The tax increment is then added to the tax computed for the prior fiscal year to develop the apportionment for the current fiscal year.

Recommendation

The county should recalculate the AB 8 factors and correct any misallocations of property tax revenues. The county should use the corrected calculations in the future.

County's Response

> We concur with the finding and the recommendation. We have completed all necessary corrections and submitted them to the State Controller's Office for review.

SCO Comment

SCO accepts the county's corrections and will confirm the application in the next audit.

FINDING 2—Negative bailout

The county incorrectly calculated the negative bailout amount. The county also incorrectly applied the negative bailout amount, reducing its contribution to the ERAF. These errors resulted in an overallocation to the county of approximately $533,299, an underallocation to the ERAF of approximately $537,528, and a misallocation to all school jurisdictions.

After the passage of Proposition 13, the legislature passed SB 154 (Chapter 292, Statutes of 1978), providing for the distribution of State assistance or bailout to make up, in part, for local property tax losses. The relief for counties was $436 million in cash grants, plus the State's assumption of $1 billion associated with mandated health and welfare programs.

In the second year following the passage of Proposition 13, the legislature passed AB 8 (Chapter 282, Statutes of 1979), which provided for a long-term solution, consisting of a one-time adjustment (shift) that created a new property tax base for each local agency.

Counties received 100% of their SB 154 block grant and a small adjustment for Aid to Families with Dependent Children, minus the amount of the indigent health block grant. For some counties, the value of the indigent health block grant was so great that it exceeded the value of the SB 154 block grant. In those cases, the AB 8 shift resulted in a reduction of property tax base instead of an increase. These counties are referred to as "negative bailout counties." For all but the negative bailout counties, the increased property tax was deducted from the property tax allocation to school entities. For the negative bailout counties, property tax allocations to school entities were supposed to increase by the negative bailout amount in the respective counties.

Subsequently, it was discovered that the negative bailout counties were not transferring the required property taxes to the schools. Consequently, the legislature passed AB 2162 (Chapter 899, Statutes of 1983), forgiving prior allocation errors but requiring future payments to be made in accordance with statute.

The negative bailout amount has grown each year as the assessed value of property in the counties has grown. For many years, the negative bailout counties tried unsuccessfully to have the negative bailout amount eliminated. In 2010, the legislature passed SB 85 (Chapter 5, Statutes of 2010), which did not eliminate the negative bailout amount, but capped it according to a specified formula.

Recommendation

The county should reverse the decrease to its ERAF contribution for FY 2011-12 and FY 2012-13 ($645,304.53 and $13,441.69, respectively), and all subsequent adjustments.

For FY 2011-12, the county should decrease the AB 8 property tax allocations for school entities by a proportionate amount of the current-year SB 85 negative bailout amount ($511,580). The county should then increase the AB 8 property tax allocations for school entities by a proportionate amount of the lesser of current or prior year SB 85 negative bailout amounts ($511,580 and $499,181, respectively), with the difference going to the county (in this instance, $12,399).

The county should perform the same process mentioned above for FY 2012-13, reducing the allocations to school entities by a proportionate amount of the current-year SB 85 negative bailout amount ($522,518), then increasing the allocations to school entities by a proportionate amount of the lesser of current-year or prior-year negative bailout amounts (in this case, $522,518 and $499,181, respectively). The difference should go to the county (in this instance, $23,337).

For FY 2013-14 and every year thereafter, the county should decrease the AB 8 property tax allocations for school entities by a proportionate amount of the current year SB 85 negative bailout amount ($522,518 adjusted

annually for countywide growth). The county should then increase the AB 8 property tax allocations for school entities by a proportionate amount of the increase amount used in the prior year ($499,181), with the difference going to the county.

County's Response

> The county states that it is experiencing incremental growth. The county also asserts that the SCO provided erroneous guidance in implementing the SB 85 Negative Bailout calculation. However, the county has completed all necessary changes and submitted them to the SCO for review, and has obtained confirmation that the changes were made appropriately.

SCO Comment

SCO concurs that the county is experiencing incremental growth and that there was an initial misunderstanding regarding the SB 85 negative bailout calculation, that was subsequently clarified. SCO accepts the county's corrections and will confirm the application in the next audit.

FINDING 3—Unitary debt service rate

The county made the following errors in its calculation of the unitary debt service rate:

- In FY 2006-07, the county did not carry forward the prior-year unitary debt service rate.
- In FY 2011-12, the county incorrectly calculated the immediate prior-year countywide secured debt service levy.
- In FY 2012-13, the county incorrectly calculated the second prior-year countywide secured debt service levy.

These errors resulted in an undercollection of property tax revenues in the amount of approximately $6,566.

Requirements for the apportionment and allocation of unitary and operating nonunitary property taxes are found in Revenue and Taxation Code section 100.

Unitary properties are those properties on which the Board of Equalization "may use the principle of unit valuation in valuing properties of an assessee that are operated as a unit in the primary function of the assessee" (i.e., public utilities, railroads, or qualified electric properties). The Revenue and Taxation Code further states, "Operating nonunitary properties are those that the assessee and its regulatory agency consider to be operating as a unit, but the board considers not part of the unit in the primary function of the assessee."

In FY 1988-89, the legislature established a separate system for apportioning and allocating the unitary and operating nonunitary property taxes. The legislature established the unitary and operating nonunitary base year and developed formulas to compute the distribution factors for the fiscal years that followed.

Recommendation

The county should recalculate the unitary debt service rate, beginning with FY 2006-07. The county should use the corrected rate in subsequent unitary debt service rate calculations.

County's Response

> We concur with the finding and the recommendation. We have completed all necessary corrections and submitted them to the State Controller's Office for review.

SCO Comment

SCO accepts the county's corrections and will confirm the application in the next audit.

FINDING 4—Unitary and operating nonunitary apportionments

The county incorrectly allocated unitary property tax revenues by making the following errors:

- In FY 2006-07, FY 2009-10, and FY 2012-13, the county did not carry forward prior-year unitary factors for the allocation of up to 102% of prior-year revenues.
- During all fiscal years audited (FY 2005-06 through FY 2012-13), the county included the ERAF in the apportionment of unitary revenues.
- During all fiscal years audited (FY 2005-06 through FY 2012-13), the estimated tax collection was greater than 1% of assessed value (AV). The prior audit showed estimated tax collection at 1% in FY 2004-05.

These errors resulted in a misallocation to all jurisdictions that receive unitary property tax.

Requirements for the apportionment and allocation of unitary and operating nonunitary property taxes are found in Revenue and Taxation Code section 100.

Unitary properties are those properties on which the Board of Equalization "may use the principle of unit valuation in valuing properties of an assessee that are operated as a unit in the primary function of the assessee" (i.e., public utilities, railroads, or qualified electric properties). The Revenue and Taxation Code further states, "Operating nonunitary properties are those that the assessee and its regulatory agency consider to be operating as a unit, but the board considers not part of the unit in the primary function of the assessee."

In FY 1988-89, the legislature established a separate system for apportioning and allocating the unitary and operating nonunitary property taxes. The legislature established the unitary and operating nonunitary base year and developed formulas to compute the distribution factors for the fiscal years that followed.

Recommendation

The county should recalculate the unitary property tax allocation factors beginning with FY 2006-07, correcting all errors noted above except for the inclusion of the ERAF. The county should remove the ERAF in the FY 2013-14 calculations. The county should use these corrected factors in all subsequent unitary calculations and apportionments.

County's Response

> The county stated that the assessed valuation (AV) used in determining current year unitary revenues for FY 2008-09 through FY 2012-13 match the values provided to the county by the Board of Equalization. The county provided the SCO with verification.
>
> The county concurs with the remainder of the finding and recommendation. The county has submitted the corrections to the SCO for review.

SCO Comment

The county does not bill parcels for which the tax is $20.00 or less ($2,000.00 in AV). Once these parcels are removed from the unitary total, the AVs used by the county to calculate unitary revenues for FY 2008-09 through FY 2012-13 should match the values provided to the county by the Board of Equalization.

SCO accepts the county's corrections and will confirm the application in the next audit.

FINDING 5—Educational Revenue Augmentation Fund

In FY 2005-06, the county carried forward incorrect ERAF amounts for the County General Fund and Hayfork Lighting. The error compounded over subsequent years, resulting in an underallocation of approximately $154,397 and $3,107, respectively (combined overallocation to the ERAF of $157,504).

Requirements for the local agency shift of property tax revenues to the ERAF primarily are found in Revenue and Taxation Code sections 97.1 through 97.3. Beginning in FY 1992-93, most local agencies were required to shift an amount of property tax revenues to the ERAF using formulas detailed in the code. The property tax revenues in the ERAF are subsequently allocated to the public schools using factors supplied by the county superintendent of schools.

For FY 1992-93, the ERAF shift amount for cities was determined by adding a per capita amount to a percentage of property tax revenues received by each city. The amount for counties was determined by adding a flat amount, adjusted for growth, to a per capita amount. The amount for special districts generally was determined by shifting the lesser of 10% of that district's total annual revenues as shown in the FY 1989-90 edition of the SCO's Report on Financial Transactions Concerning Special Districts or 40% of the FY 1991-92 property tax revenues received, adjusted for growth. Specified special districts were exempted from the shift.

For FY 1993-94, the ERAF shift for cities and counties generally was determined by:

- Reducing the FY 1992-93 ERAF shift by the FY 1992-93 per capita shift;
- Adjusting the result for growth; and
- Adding the result to a flat amount and a per capita amount determined by the Department of Finance, adjusted for growth.

The FY 1993-94 ERAF shift for special districts, other than fire districts, was generally determined by:

- Multiplying the property tax allocation for FY 1992-93, pre-ERAF, by the Special District Augmentation Fund (SDAF) factor for the district effective on June 15, 1993;
- Adjusting that amount by subtracting the FY 1992-93 shift to the ERAF;
- If the above amount is greater than zero, adjusting that amount for FY 1993-94 growth (zero is used for negative amounts); and
- Adding that amount to the FY 1992-93 ERAF shift, adjusting for growth.

For fire districts, the FY 1993-94 ERAF shift generally was determined by:

- Deducting the FY 1992-93 ERAF shift for the district from the FY 1992-93 property tax allocation;
- Multiplying the result by the SDAF factor for the district effective on June 13, 1993 (net current-year bailout equivalent);
- For a district governed by a board of supervisors, deducting the amount received from the SDAF in FY 1992-93 from the net current-year bailout equivalent; or, for an independent district, deducting the amount received from the SDAF and the difference between the net current-year bailout equivalent and the amount contributed to the SDAF from the net current-year bailout equivalent;
- Adjusting that amount for growth; and
- Adding that amount to the FY 1992-93 ERAF shift, adjusted for growth.

For fiscal years after FY 1993-94, the amounts determined are adjusted for growth annually to determine the ERAF shift amounts for that year.

Recommendation

The county should recalculate the ERAF shift beginning with FY 2005-06 and correct any misallocated amounts. The county should use these corrected calculations going forward.

County's Response

> We concur with the finding and the recommendation. We have completed all necessary corrections and submitted them to the State Controller's Office for review.

SCO Comment

SCO accepts the county's corrections and will confirm the application in the next audit.

FINDING 6—Educational Revenue Augmentation Fund (ERAF)-Vehicle Licensing Fee (VLF)

In FY 2008-09 and FY 2009-10, the county adjusted the Vehicle Licensing Fee (VLF) for growth twice, resulting in an overallocation to the county and an underallocation to the ERAF of approximately $441,069 each.

While this error does have an effect on the county's calculation of unitary and supplemental apportionments, the only material impact is to secured/unsecured property tax revenues.

Requirements for the ERAF adjustment for the VLF are found in Revenue and Taxation Code section 97.70.

Recommendation

The county should recalculate the VLF amount beginning with FY 2008-09. The county should repay the ERAF any underallocated amounts, and correct the negative ERAF adjustments to schools. These adjustments should result in a zero net effect to the ERAF.

The county should use the recalculated VLF amounts in the future.

County's Response

> We concur with the finding and the recommendation. We have completed all necessary corrections and submitted them to the State Controller's Office for review.

SCO Comment

SCO accepts the county's corrections and will confirm the application in the next audit.

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