

# SIERRA COUNTY

Audit Report

## APPORTIONMENT AND ALLOCATION OF PROPERTY TAX REVENUES

*July 1, 2009, through June 30, 2017*



**BETTY T. YEE**  
California State Controller

April 2019



**BETTY T. YEE**  
California State Controller

April 2, 2019

The Honorable Van A. Maddox, CPA,  
Auditor-Controller/Treasurer/Tax Collector  
Sierra County  
P.O. Box 425  
Downieville, CA 95936

Dear Mr. Maddox:

The State Controller's Office audited the methods employed by Sierra County to apportion and allocate property tax revenues for the period of July 1, 2009, through June 30, 2017. We conducted the audit pursuant to the requirements of Government Code section 12468.

Our audit found instances of noncompliance with California statutes for the apportionment and allocation of property tax revenues for the audit period. We determined that Sierra County incorrectly calculated the:

- Annual tax increment;
- Supplemental property tax apportionment; and
- Sales and use tax.

In addition, we found that the county has not established a Vehicle License Fee Property Tax Compensation Fund in the county treasury.

If you have any questions, please contact Lisa Kurokawa, Chief, Compliance Audits Bureau, by telephone at (916) 327-3138.

Sincerely,

*Original signed by*

JIM L. SPANO, CPA  
Chief, Division of Audits

JLS/as

cc: Paul Roen, Chair  
Sierra County Board of Supervisors  
Chris Hill, Principal Program Budget Analyst  
Local Government Unit  
California Department of Finance

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# Audit Report

## Summary

The State Controller's Office (SCO) audited the methods employed by Sierra County to apportion and allocate property tax revenues for the period of July 1, 2009, through June 30, 2017.

Our audit found instances of noncompliance with California statutes for the apportionment and allocation of property tax revenues for the audit period. We determined that the county incorrectly calculated the:

- Annual tax increment (ATI);
- Supplemental property tax apportionment; and
- Sales and Use Tax (SUT).

In addition, we found that the county has not established a Vehicle License Fee (VLF) Property Tax Compensation Fund in the county treasury.

## Background

After the passage of Proposition 13 in 1978, the California State Legislature (Legislature) enacted new methods for apportioning and allocating property tax revenues to local government agencies, school districts, and community college districts. The main objective was to provide local government agencies, school districts, and community college districts with a property tax base that would grow as assessed property values increased. The method has been further refined in subsequent laws passed by the Legislature.

One key law was Assembly Bill (AB) 8, Chapter 282, Statutes of 1979, 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 government agencies receive each fiscal 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 government agencies, school districts, and community college districts 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 school and community college districts to local government agencies (AB 8 shift) and the development of the tax rate area (TRA) ATI apportionment factors, which determine the amount of property tax revenues to be allocated to each jurisdiction.

The total amount to be allocated to each jurisdiction 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 from the AB 8 process revenues generated by unitary and operating nonunitary properties, pipelines, regulated railway companies, and qualified electric properties. These properties are now apportioned and allocated under separate processes.

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 fund. The fund is subsequently apportioned and allocated to school and community college districts by the county auditor according to instructions received from the county superintendent of schools or the chancellor of the California community colleges.

Revenues generated by the different types of property tax are apportioned and allocated to local government agencies, school districts, and community college districts 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 other intrinsic qualities to guarantee payment of taxes levied against it.
- *State-Assessed Roll*—Utility properties composed of unitary and operating 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.

To mitigate problems associated with the apportionment and allocation of property tax revenues, Senate Bill (SB) 418, which requires the State Controller to audit the counties' apportionment and allocation methods and report the results to the Legislature, was enacted in 1985.

Apportionment and allocation of property tax revenues can result in revenues to an agency or agencies being overstated, understated, or misstated. Misstated revenues occur when at least one taxing agency receives more revenue than it was entitled to, while at least one taxing agency receives less revenue than it was entitled to.

The agency that received less tax revenue than its statutory entitlement would have standing to require that adjustments be made by the county, either on a retroactive or prospective basis. SCO does not have enforcement authority or standing to require the county to take corrective action with respect to misallocation of tax revenues, unless the

misallocation resulted in overpaid state funds (funds intended for the ERAF, school districts, or community college districts). SCO has authority to recover misallocations resulting in overpaid state funds pursuant to Government Code (GC) sections 12410, 12418, and 12419.5.

GC section 12410 provides the State Controller with broad authority to “superintend the fiscal concerns of the state.” GC section 12418 provides the State Controller with the authority to “direct and superintend the collection of all money due the State, and institute suits in its name” against all debtors of the State. GC section 12419.5 provides the State Controller with the authority to offset any amounts due the State against any amounts owing the debtor by the State.

Revenue and Taxation Code (RTC) section 96.1(b) allows a reallocation of current audit findings and unresolved prior audit findings.

RTC section 96.1(c)(3) limits a cumulative reallocation or adjustment to one percent of the total amount levied at a one-percent rate of the current year’s original secured tax roll. For reallocation to the ERAF, school districts, or community college districts, a reallocation must be completed in equal increments within the following three fiscal years, or as negotiated with the State Controller.

## **Objective, Scope, and Methodology**

The objective of our audit was to determine whether the county complied with Revenue and Taxation Code, Health and Safety Code, and Government Code requirements pertaining to the apportionment and allocation of property tax revenues.

The audit period was July 1, 2009, through June 30, 2017.

To achieve our objective, we:

- Interviewed key personnel to gain an understanding of the county’s process for apportioning and allocating property tax revenues;
- Reviewed the county’s written procedures for apportioning and allocating property tax revenues;
- Performed analytical reviews to assess the reasonableness of property tax revenues;
- Judgmentally selected a non-statistical sample of five from approximately 26 taxing jurisdictions within the county for all fiscal years in the audit period (the actual number of taxing jurisdictions, which include the ERAF, can vary from year to year based on jurisdictional changes). Errors found were not projected to the intended population. Then, we:
  - Recomputed apportionment and allocation reports to verify computations used to develop property tax apportionment factors;
  - Tested TRA reports to verify that the correct TRA factors were used in the computation of the ATI;
  - Reviewed supplemental property tax administrative costs and fees to determine whether recovery costs associated with

- administering supplemental taxes were based on actual costs and did not exceed five percent of revenues collected, as prescribed in statute;
- Verified computations used to develop supplemental property tax apportionment factors;
  - Verified unitary and operating nonunitary and unitary regulated railway computations used to develop apportionment factors;
  - Reviewed property tax administration cost reports and recomputed administrative costs associated with work performed for apportioning and allocating property tax revenues to local government agencies, school districts, and community college districts;
  - Reviewed ERAF reports and verified computations used to determine the shift of property taxes from local government agencies to the ERAF and, subsequently, to school and community college districts; and
  - Reviewed the SUT letter and recomputed VLF computations used to verify the amount transferred from the ERAF to counties and cities to compensate for the diversion of these revenues.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

We limited our review of the county's internal controls to gaining an understanding of the transaction flow to develop appropriate auditing procedures. We did not evaluate the effectiveness of internal controls relevant to the apportionment and allocation of property tax revenues. We did not audit the county's financial statements.

We conducted this audit under the authority of GC section 12468, which requires the SCO to audit the apportionment and allocation of property tax revenues. A property tax bill contains the property tax levied at a one percent tax rate pursuant to the requirement of Proposition 13. A bill may also contain special taxes, debt service levies on voter-approved debt, fees, and assessments levied by the county or a city. The scope of our audit is concerned with the distribution of the one percent tax levy. Special taxes, debt service levies on voter-approved debt, fees, and assessments levied by the county or a city are beyond the scope of our audit and were not reviewed or audited.

## Conclusion

Our audit found that Sierra County did not comply with California statutes for the apportionment and allocation of property tax revenues for the audit period, as it:

- Incorrectly calculated the ATI;

- Incorrectly calculated supplemental property tax apportionment; and
- Incorrectly calculated the SUT.

In addition, we found that the county has not established a VLF Property Tax Compensation Fund in the county treasury.

These instances of noncompliance are described in the Findings and Recommendations section of this report.

### **Follow-up on Prior Audit Findings**

In our prior audit report, for the period of July 1, 2003, through June 30, 2009, issued April 14, 2010, we found that the county did not comply with the implementation requirements of SB 1096, as neither a SUT Compensation Fund nor a VLF Property Tax Compensation Fund were established in the county treasury. The establishment of a SUT Compensation Fund is no longer an issue because the SUT “Triple Flip” tax swap ended on December 31, 2015, when the bonds were completely paid. However, the county has yet to comply with the requirements of SB 1096, as a VLF Property Tax Compensation Fund has not yet been established in the county treasury (see Finding 1).

### **Views of Responsible Officials**

We issued a draft audit report on January 7, 2019. Van A. Maddox, CPA, Auditor-Controller/Treasurer/Tax Collector, responded by email agreeing with the audit results with the exception of Finding 1. Mr. Maddox also requested that the SCO approve a repayment plan for the City of Loyalton. We have addressed the county’s request in the Other Issues section.

### **Restricted Use**

This audit report is solely for the information and use of Sierra County, the Legislature, the California Department of Finance, and the SCO; it is not intended to be and should not be used by anyone other than these specified parties. This restriction is not intended to limit distribution of this audit report, which is a matter of public record and is available on the SCO website at [www.sco.ca.gov](http://www.sco.ca.gov).

*Original signed by*

JIM L. SPANO, CPA  
Chief, Division of Audits

April 2, 2019



# Findings and Recommendations

## **FINDING 1— VLF Property Tax Compensation Fund (REPEAT)**

In our prior audit report, for the period of July 1, 2003, through June 30, 2009, dated April 14, 2010, we found that the county failed to comply with the implementation requirements of SB 1096, as neither the SUT Compensation Fund nor the VLF Property Tax Compensation Fund were established in the county treasury. The revenue adjustments were made directly to the AB 8 apportionment system.

Our current audit found that the county did not correct the finding. The establishment of a SUT Compensation Fund is no longer an issue because the SUT “Triple Flip” tax swap ended on December 31, 2015, when the bonds were completely paid; however, the county still has not complied with the requirements of SB 1096, as the VLF Property Tax Compensation Fund has not yet been established in the county treasury.

### Recommendation

We recommend that the county establish a VLF Property Tax Compensation Fund as required by SB 1096.

### County’s Response

Setting up the additional fund when the county only has one school district is form over substance. This would make more work for no change in outcome.

### SCO Comment

Our finding and recommendation remain unchanged.

## **FINDING 2— Computation and Distribution of Property Tax Revenues**

During testing of the ATI process, we found that the county incorrectly computed the countywide apportionment (AB 8) factors because it used the incorrect prior-year revenue in FY 2010-11, resulting in a misstatement of property tax revenues for all subsequent years. The largest affected jurisdiction was the county’s General Fund, which was overstated by \$8,871 in FY 2016-17. The error occurred because the county misinterpreted the criteria outlined in the Revenue and Taxation Code.

RTC sections 96 through 96.5 provide the legal requirements for the computation of the ATI and the apportionment and allocation of property tax revenues.

ATI is the difference between the total amount of property tax revenues computed each year using the equalized assessment roll and the sum of the amounts allocated pursuant to RTC section 96.1(a). Each TRA will receive an increment based on its share of the incremental growth in assessed valuations. ATI added to the tax computed for the prior fiscal year will develop the apportionments for the current fiscal year.

Recommendation

We recommend that the county:

- Review the aforementioned Revenue and Taxation Code sections and update procedures to properly compute the AB 8 factors;
- Recalculate the property tax revenues for FY 2010-11 and subsequent years; and
- Make appropriate monetary adjustments to the ERAF.

County's Response

The county concurs with the finding.

**FINDING 3—  
Supplemental  
Property Tax  
Administrative Costs**

During testing of the supplemental property tax administrative costs, we found that the county incorrectly computed the supplemental apportionment factors because it included VLF revenue in the calculation for FY 2014-15 through FY 2016-17. The largest affected jurisdiction was the ERAF, which was understated by \$5,175 in FY 2016-17. The error occurred because the county misinterpreted the criteria outlined in the Revenue and Taxation Code.

RTC section 75.60 provides the legal requirements for supplemental property tax administrative costs reimbursements.

The statute allows a county to charge an administrative fee for supplemental property tax revenue collections. This fee is not to exceed five percent of the supplemental property tax revenues collected.

Recommendation

We recommend that the county:

- Review the aforementioned Revenue and Taxation Code section and update procedures to exclude VLF revenue from the supplemental factors; and
- Make appropriate monetary adjustments to the ERAF.

County's Response

The county concurs with the finding.

**FINDING 4—  
Sales and Use Tax  
Adjustments**

During testing of the SUT process, we found that the county incorrectly distributed SUT revenue for FY 2009-10 and FY 2013-14. The SUT revenue distributed by the county did not agree with the revenue reported by the California Department of Finance. The largest affected jurisdiction was the City of Loyalton, whose SUT revenue was overstated by approximately \$18,904 in FY 2009-10. The error occurred because the county misinterpreted the criteria outlined in the Revenue and Taxation Code.

RTC sections 97.68 and 97.69 provide the legal requirements for SUT adjustments.

The California Department of Finance annually, on or before September 1, provides SUT amounts for counties and cities. These amounts are transferred from the ERAF to the SUT Compensation Fund, and eventually to each county and cities within each county.

Recommendation

As the SUT has ended, we recommend that the county make appropriate monetary adjustments to the ERAF.

County's Response

The county concurs with the finding.

## Other Issue

### **OTHER ISSUE— Repayment Plan**

Based on documentation provided by the county during the audit, a total of approximately \$60,000 was over-distributed to the City of Loyalton and is due to the county. In the county's January 7, 2019 response to the draft audit report, it stated that it had begun to recover one-third of the over-payment and requested that the SCO approve a nine-year repayment plan for the City of Loyalton.

The SCO does not have enforcement authority or standing to require that the county take corrective action regarding the misallocation of tax revenues, unless the misallocation resulted in overpaid state funds. Therefore, the negotiation for repayment is between the city and the county, and does not include the State.

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