

ALPINE COUNTY

Reissued Audit Report

APPORTIONMENT AND ALLOCATION OF PROPERTY TAX REVENUES

July 1, 2010, through June 30, 2016



BETTY T. YEE
California State Controller

June 2019



BETTY T. YEE
California State Controller

June 17, 2019

Carol McElroy, Chief Accounting Officer and Finance Director
Alpine County
P.O. Box 266
Markleeville, CA 96120

Dear Ms. McElroy:

The State Controller's Office audited the methods employed by Alpine County to apportion and allocate property tax revenues for the period of July 1, 2010, through June 30, 2016. The audit was conducted pursuant to the requirements of Government Code section 12468.

This reissued report updates our previous report dated October 10, 2017. We are reissuing this report to update the Objective, Scope, and Methodology section. We also provide additional information in the Revised Background section and the Revised Findings and Recommendations section. These revisions do not affect the audit conclusion.

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 Alpine County incorrectly calculated:

- Supplemental property tax apportionment factors; and
- Unitary and operating nonunitary apportionment factors.

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/lis

cc: David Griffith, Chair
Alpine County Board of Supervisors
Chris Hill, Principal Program Budget Analyst
Local Government Unit
California Department of Finance

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Reissued Audit Report

Summary

The State Controller's Office (SCO) audited the methods employed by Alpine County to apportion and allocate property tax revenues for the period of July 1, 2010, through June 30, 2016.

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:

- Supplemental property tax apportionment factors; and
- Unitary and operating nonunitary apportionment factors.

Revised 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) annual tax increment (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 revenues 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 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.

Revised 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, 2010, through June 30, 2016.

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;
- Selected all five taxing jurisdictions within the county for all fiscal years in the audit period. 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;
 - Verified computations used to develop supplemental property tax apportionment factors;
 - Verified unitary and operating nonunitary computations used to develop apportionment factors;
 - 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 Sales and Use Tax letter and recomputed Vehicle License Fee (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 Alpine County did not comply with California statutes for the apportionment and allocation of property tax revenues for the audit period. We determined that the county:

- Incorrectly calculated the supplemental property tax apportionment factors; and
- Incorrectly calculated the unitary and operating nonunitary apportionment factors.

These instances of noncompliance are described in the Revised Findings and Recommendation section of this audit report.

Follow-up on Prior Audit Findings

Our prior audit report, for the period of July 1, 2004, through June 30, 2010, issued April 15, 2011, included no findings related to the apportionment and allocation of property tax revenues by the county.

Views of Responsible Officials

We issued a draft audit report on August 15, 2017. Carol McElroy, Chief Accounting Officer and Finance Director, responded by letter dated August 18, 2017, agreeing with the audit results. The county's response is included as an attachment to this report.

On November 15, 2018, we informed Ms. McElroy of this reissued audit report and the reason for the reissuance.

**Reason for
Reissuance**

This reissued report updates our previous report dated October 10, 2017. We are reissuing this report to update the Objective, Scope, and Methodology section. We also provide additional information in the Revised Background section and the Revised Findings and Recommendations section. These revisions do not affect the audit conclusion.

Restricted Use

This audit report is solely for the information and use of Alpine 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.

Original signed by

JIM L. SPANO, CPA
Chief, Division of Audits

June 17, 2019

Revised Findings and Recommendations

REVISED FINDING 1— Supplemental Property Tax Apportionment

During testing of the county’s supplemental property tax apportionment and allocation process, we found that the county incorrectly used the VLF adjusted AB 8 factors for the supplemental property tax calculation for FY 2014-15 and FY 2015-16. We do not have all the necessary information to quantify the monetary impact of this error. The error is due to the county misinterpreting the statutes.

The legal requirements for supplemental roll property tax apportionment and allocation are found in RTC 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

We recommend that the county:

- Review the aforementioned sections of the Revenue and Taxation Code, and establish and implement procedures to properly calculate supplemental property taxes; and
- Exclude the VLF adjustment from the supplemental property tax calculation in future years.

County’s Response

The county concurs with this recommendation and going forward will exclude the VLF adjustment [from] the supplemental property tax calculation.

REVISED FINDING 2— Unitary and Operating Nonunitary Apportionment

During testing of the county’s unitary and operating nonunitary apportionment and allocation process, we found that the county did not use the prior-year unitary factors for up to 102 percent of revenues for all fiscal years in the audit period. In addition, the county incorrectly used the VLF adjusted AB 8 factors for excess over 102 percent of revenues for FY 2015-16. We are unable to quantify the monetary impact due to the various components involved in the calculation. The error is due to procedural mistakes made by county staff.

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

Unitary properties are those properties on which BOE “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). Revenue and Taxation Code 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

We recommend that the county:

- Review the aforementioned section of the Revenue and Taxation Code, and establish and implement procedures to properly calculate unitary and operating nonunitary apportionment factors;
- Recompute the unitary and operating nonunitary apportionment factors beginning with FY 2010-11; and
- Make monetary adjustments using the corrected apportionment factors for FY 2010-11 through FY 2015-16.

County's Response

The county concurs with this recommendation and will re-compute the unitary and non-unitary apportionment factors and corresponding apportionments beginning with FY 2010-11 and use the corrected factors along with any adjusting journal entries as necessary.

**Attachment—
County's Response to Draft Audit Report**



COUNTY OF ALPINE

Administration

Carol McElroy- CAO/Director of Finance

Sarah Simis- Deputy CAO to Personnel/Risk Management

California State Controller Office
Division of Audits
Jim L. Spano, CPA, Assistant Division Chief
PO Box 942850
Sacramento, CA 94250-5874

August 18, 2017

Dear Mr. Spano:

The following are the County responses to the Property Tax Apportionment Audit for the period of July 1, 2010 through June 30, 2016.

Finding 1-Supplemental Property Tax Apportionment:

The county incorrectly used the VLF adjusted AB 8 factors for supplemental property tax calculation in FY 2014-15 and FY 2015-16.

State Recommendation:

The county, going forward, exclude VLF adjustment in the supplemental property tax calculation.

County's Response:

The county concurs with this recommendation and going forward will exclude the VLF adjustment in the supplemental property tax calculation.

Finding 2- Unitary and Operating Non-unitary Apportionment:

The county did not use the prior year unitary factors for up to 102% of revenues for all years. Also, in FY 2015-16, the county incorrectly used the VLF adjusted AB 8 factors for excess 102% of revenues.

State Recommendation:

The county, going forward:

*Re-compute the unitary and non-unitary apportionment factors and corresponding apportionments beginning with FY 2010-11 and then use the corrected factors; and

*Make adjusting journal entries as necessary.

County's Response:

The county concurs with this recommendation and will re-compute the unitary and non-unitary apportionment factors and corresponding apportionments beginning with FY 2010-11 and use the corrected factors along with any adjusting journal entries as necessary.

Sincerely,

A handwritten signature in black ink, appearing to read "Carol McElroy".

Carol McElroy
CAO-Finance Director Alpine County

**State Controller's Office
Division of Audits
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Sacramento, CA 94250**

<http://www.sco.ca.gov>