

NEVADA COUNTY

Audit Report

PROPERTY TAX ALLOCATION AND APPORTIONMENT SYSTEM

July 1, 2010, through June 30, 2017



BETTY T. YEE
California State Controller

July 2018



BETTY T. YEE
California State Controller

July 6, 2018

The Honorable Marcia L. Salter, Auditor-Controller
Nevada County
950 Maidu Avenue
Nevada City, CA 95959-8617

Dear Ms. Salter:

The State Controller's Office audited the methods employed by Nevada County to allocate and apportion property tax revenues for the period of July 1, 2010, through June 30, 2017. The audit was conducted pursuant to the requirements of Government Code section 12468.

Due to a pending appellate court decision, the audit scope excluded making a determination on the validity of the county's methodology for apportioning the residual balance from the Redevelopment Property Tax Trust Fund, as described in the Observation section of this report.

Without consideration of this legal issue, our audit found that the county complied with California statutes for the allocation and apportionment of property tax revenues for the audit period.

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

Sincerely,

Original signed by

JEFFREY V. BROWNFIELD, CPA
Chief, Division of Audits

JVB/rg

cc: Ed Scofield, Chair
Board of Supervisors
Nevada County
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 Nevada County to allocate and apportion property tax revenues for the period of July 1, 2010, through June 30, 2017.

Due to a pending appellate court decision, the audit scope excluded making a determination on the validity of the county's methodology for apportioning the residual balance from the Redevelopment Property Tax Trust Fund (RPTTF), as described in the Observation section of this report.

Without consideration of this legal issue, our audit found that the county complied with California statutes for the allocation and apportionment of property tax revenues for the audit period.

Background

After the passage of Proposition 13 in 1978, the California State Legislature (Legislature) enacted new methods for allocating and apportioning property tax revenues to local government agencies, school districts, and community college districts. The main objective was to provide local agencies 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 8 (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 allocated and apportioned 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 revenue generated by unitary and nonunitary property and pipelines from the AB 8 system. This revenue now is 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 fund. The fund is subsequently allocated and apportioned 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 allocated and apportioned 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 (BOE).
- *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 allocation and apportionment of property taxes, Senate Bill 418 was enacted in 1985, requiring the State Controller to audit the counties' allocation and apportionment methods and report the results to the Legislature.

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

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

Revenue and Taxation Code 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 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

Our audit objective was to determine whether the county complied with Revenue and Taxation Code requirements pertaining to the allocation and apportionment of property taxes. The audit covered the period of July 1, 2010, through June 30, 2017.

To meet our objective, we:

- Interviewed key personnel to gain an understanding of the county’s property tax allocation and apportionment processes;
- Reviewed the county’s written procedures for allocating and apportioning property tax revenues;
- Performed analytical reviews to assess the reasonableness of property tax revenues for all fiscal years in the audit period; and
- Judgmentally selected a non-statistical sample of five from approximately 48 taxing jurisdictions, including ERAF, within the county for all fiscal years in the audit period (errors found were not projected to the intended population). The actual number of taxing jurisdictions can vary from year to year based on jurisdictional changes, therefore we:
 - Recomputed allocation and apportionment 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,
 - Verified computations used to develop supplemental property tax apportionment factors;
 - Verified unitary and operating nonunitary and regulated railway computations used to develop apportionment factors;

- Reviewed the RPTTF deposits and distributions;
- Reviewed property tax administration cost reports and recomputed administrative costs associated with work performed for allocating and apportioning property tax 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 ERAF and, subsequently, to school and community college districts;
- Reviewed the Sales and Use Tax letter and recomputed Vehicle License Fee computations used to verify the amount of ERAF transferred to counties and cities to compensate for the diversion of these revenues; and
- Reviewed BOE jurisdictional change filing logs and their impact on the tax allocation and apportionment system.

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.

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

This audit was conducted under the authority of GC sections 12410 and 12468, which require SCO to audit the allocation and apportionment of property taxes. 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

Without consideration of the legal issue described in the Observation section of this report, our audit found that the county complied with California statutes for the allocation and apportionment of property tax revenues for the audit period.

Follow-up on Prior Audit Findings

The county has satisfactorily resolved all the findings noted in our prior audit report, issued August 17, 2011.

**Views of
Responsible
Officials**

We issued a draft audit report on January 11, 2018. Marcia Salter, Auditor-Controller, responded by letter dated February 27, 2018 (Attachment), in regards to the Observation; she stated that the county will be monitoring the Superior Court case under review by the appellate court for potential impact on its distribution practices. This final audit report includes the county's response.

Restricted Use

This report is solely for the information and use of Nevada County, the Legislature, and 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 this report which is a matter of public record.

Original signed by

JEFFREY V. BROWNFIELD, CPA
Chief, Division of Audits

July 6, 2018

Observation

OBSERVATION— Redevelopment Property Tax Trust Fund

On May 26, 2015, the Sacramento County Superior Court ruled in Case No. 34-2014-80001723-CU-WM-GDS between the cities of Chula Vista, El Cajon, Escondido, Poway, San Diego, San Marcos, and Vista (petitioners) and the San Diego County Auditor-Controller (respondent) regarding the methodology in apportioning the residual balance from the RPTTF.

The Court stated, in part:

(1) that a cap on the residual amount each entity can receive be imposed in an amount proportionate to its share of property tax revenue in the tax area; and (2) the calculation of the residual share an entity is entitled to receive must be done by considering the property tax available in the Redevelopment Property Tax Trust Fund after deducting only the amount of any distributions under paragraphs (2) and (3) of subdivision (a) of Section 34183.

On September 17, 2015, the respondent appealed the ruling to the Court of Appeal of the State of California, Third Appellate District.

As the appellate court has not decided on the case, we will follow up on this issue in a subsequent audit.

County's Response

We will be monitoring that case for the outcome and potential impact that may have on our distribution practice.

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

State of California
COUNTY OF NEVADA

MARCIA L. SALTER – Auditor-Controller

Auditor-Controller
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Nevada City CA 95959

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February 27, 2018

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

Dear Mr. Spano,

I have reviewed your draft audit report of Nevada County's Property Tax Revenue for the period of July 1, 2010 through June 30, 2017. The audit did not result in any findings in the property tax work performed by my office during that period. The report did include an observation in regards to the Superior Court case, currently under review by the appellate court, with the County of San Diego and its distribution methodology of the residual balance of the RPTTF. We will be monitoring that case for the outcome and potential impact that may have on our distribution practice.

I would like to thank Tuan Tran, of your staff for his time and effort on completing this audit. My staff and I found him to be very knowledgeable, professional, and extremely helpful.

Sincerely,



Marcia L. Salter
Auditor-Controller

**State Controller's Office
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