

# **RIVERSIDE COUNTY**

Audit Report

## **PROPERTY TAX ALLOCATION AND APPORTIONMENT SYSTEM**

*July 1, 2013, through June 30, 2016*



**BETTY T. YEE**  
California State Controller

July 2018



**BETTY T. YEE**  
California State Controller

July 3, 2018

The Honorable Paul Angulo, CPA, Auditor-Controller  
Riverside County  
4080 Lemon Street, 11<sup>th</sup> Floor  
Riverside, CA 92502

Dear Mr. Angulo:

The State Controller's Office audited the methods employed by Riverside County to allocate and apportion property tax revenues for the period of July 1, 2013, through June 30, 2016. 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.

Our audit found instances of noncompliance. The county incorrectly calculated:

- Supplemental administrative fees; and
- Qualified electric property tax revenue allocations.

If you have any questions, please contact Jim L. Spano, CPA, Assistant Division Chief, by telephone at (916) 323-5849.

Sincerely,

*Original signed by*

JEFFREY V. BROWNFIELD, CPA  
Chief, Division of Audits

JVB/as

Attachment

cc: The Honorable Chuck Washington, Chairman  
Riverside County Board of Supervisors  
Frankie Ezzat, MPA, Assistant Auditor-Controller  
Riverside County  
Pamela Elias, Property Tax Division Chief  
Riverside County  
Chris Hill, Principal Program Budget Analyst  
Local Government Unit  
California Department of Finance

# Contents

## **Audit Report**

<b>Summary</b> .....	1
<b>Background</b> .....	1
<b>Objective, Scope, and Methodology</b> .....	3
<b>Conclusion</b> .....	5
<b>Follow-up on Prior Audit Findings</b> .....	5
<b>Views of Responsible Officials</b> .....	5
<b>Restricted Use</b> .....	5
<b>Findings and Recommendations</b> .....	6
<b>Observation</b> .....	8
<b>Attachment—County’s Response to Draft Audit Report</b>	

# Audit Report

## Summary

The State Controller's Office (SCO) audited the methods employed by Riverside County to allocate and apportion property tax revenues for the period of July 1, 2013, through June 30, 2016.

Our audit found instances of noncompliance. The county incorrectly calculated:

- Supplemental administrative fees; and
- Qualified electric (QE) property tax revenue allocations.

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) because of a pending appellate court decision, as described in the Observation section of this report.

## 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 government 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), 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 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 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 adjustments to 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, 2013, through June 30, 2016.

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 all fiscal years; and
- Judgmentally selected a non-statistical sample of five out of approximately 351 taxing jurisdictions within the county for all fiscal years in the audit period (the actual number of taxing jurisdictions, including the ERAF, can vary from year to year due to jurisdictional changes). Errors found were not projected to the intended population:
  - 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 regulated railway QE property computations used to develop apportionment factors;
- Reviewed redevelopment agency (RDA) reports and verified computations used to develop the project base amount and the tax increment distributed to the RDA;
- 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;
- Reviewed reports to determine any increases in property tax revenues due cities having low or nonexistent property tax amounts; 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 requires the 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 issues described in the Observation section of this report, our audit found the following instances of non-compliance with the requirements outlined in the Objective, Scope, and Methodology section:

- The county incorrectly computed the supplemental administrative fee on penalties and interest; and
- The county incorrectly excluded non-enterprise special districts within the annual QE Tier 1 allocation.

These instances of non-compliance are described in the Findings and Recommendations section of this report.

**Follow-up on Prior Audit Findings**

The county has satisfactorily resolved the findings noted in our prior audit report, issued March 21, 2014.

**Views of Responsible Officials**

We issued a draft audit report on December 17, 2017. Pamela Elias, Property Tax Division Chief, responded by letter dated December 29, 2017 (Attachment), stating that the county has implemented our recommendation identified in the two audit findings. The county's response is included as an attachment to this report.

**Restricted Use**

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

*Original signed by*

JEFFREY V. BROWNFIELD, CPA  
Chief, Division of Audits

July 3, 2018



# Findings and Recommendations

## **FINDING 1— Supplemental Property Tax Administrative Fee**

During our audit of the supplemental property tax administrative fee process, we found that the county’s property tax system currently computes supplemental administrative fees on penalties and interest, when these fees should be computed based only on actual supplemental property taxes collected. This error resulted in the county’s over-collection of supplemental administrative fees for FY 2013-14 through FY 2015-16. We did not quantify each affected taxing entities’ dollar impact, due to the complexity of the collection process for supplemental administrative fees.

Revenue and Taxation Code section 75.60 allows a county to charge an administrative fee for supplemental property tax collections. This fee is not to exceed five percent of the supplemental property taxes collected.

### Recommendation

We recommend that the county reprogram the property tax system for this section, to exclude penalties and interest from the five percent fee computation.

### County’s Response

As of August 24, 2017, the County has reprogrammed the property tax system for this section, to exclude penalties and interest from the five percent fee computation.

### SCO Comment

We will review the correction in our next audit.

## **FINDING 2— Qualified Electric Allocation**

During our audit of the county’s QE allocation process, we found that the county excluded some non-enterprise special districts within the Tier 1 allocation process. This error resulted in misallocation of the QE revenue to the affected taxing entities. Due to the various errors affecting the computations and apportionments, we did not quantify the dollar impact for each affected taxing entity.

Requirements for the allocation and apportionment of QE property taxes are found in Revenue and Taxation Code section 100.95 beginning in FY 2007-08. QE properties are “all plant and associated equipment, including substation facilities and fee-owned land and easements, placed in service by the public utility on or after January 1, 2007.”

### Recommendation

We recommend that the county include Supervisorial Road District 4 and all other non-enterprise special districts in the county’s annual QE Tier 1 allocation.

County's Response

The County has changed the apportionment process and procedures to include Supervisorial Road District 4 into the Qualified Electric (QE) Tier 1 allocation. We have also reviewed all the non-enterprise special districts to ensure we have included appropriate districts in the Qualified Electric (QE) Tier 1 allocation.

SCO Comment

We will review the correction in our next audit.

# Observation

## **OBSERVATION— Redevelopment Property Tax Trust Fund**

On May 26, 2015, the Sacramento County Superior Court ruled in Case No. 34-2014-80001723-CY-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. As the appellate court has not decided on the case, we will follow up on this issue in a subsequent audit.

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

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**AO | AUDITOR  
CONTROLLER  
COUNTY OF RIVERSIDE**

Paul Angulo, CPA, M.A.  
County Auditor-Controller  
Frankie Ezzat, MPA  
Assistant Auditor-Controller

December 29, 2017

Mr. Jim Spano, CPA, Assistant Division Chief  
State Controller's Office, Division of Audits  
Post Office Box 942850  
Sacramento, CA 94250-5874

Subject: Audit Report Response

Dear Mr. Spano,

On December 14, 2017, we received the draft Riverside County Audit Report of the Property Tax Apportionment and Allocation System for the period of July 1, 2013 through June 30, 2016. This letter is in response to the Findings and Recommendations.

**FINDING 1 – Supplemental Property Tax Administrative Fee**

As of August 24, 2017, the County has reprogrammed the property tax system for this section, to exclude penalties and interest from the five percent fee computation.

**FINDING 2 – Qualified Electric Allocation**

The County has changed the apportionment process and procedures to include Supervisorial Road District 4 into the Qualified Electric (QE) Tier 1 allocation. We have also reviewed all the non-enterprise special districts to ensure we have included the appropriate districts in the Qualified Electric (QE) Tier 1 allocation.

If you have any comments or questions, please contact Pam Elias at 951-955-0320.

Sincerely,

Pamela M. Elias  
Chief Accountant, Property Tax Division

Cc: Jeffrey V. Brownfield, CPA, Chief, Division of Audits  
Paul Angulo, CPA, MA, Auditor-Controller  
Frankie Ezzat, MPA, Assistant Auditor-Controller

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