# GLENN COUNTY

Audit Report

## APPORTIONMENT AND ALLOCATION OF PROPERTY TAX REVENUES

*July 1, 2014, through June 30, 2020*

BETTY T. YEE
California State Controller

December 2021

BETTY T. YEE
California State Controller

December 6, 2021

Humberto Medina, CPA, Director of Finance
Glenn County
516 West Sycamore Street
Willows, CA 95988

Dear Mr. Medina:

The State Controller's Office audited Glenn County's process for apportioning and allocating property tax revenues to determine whether the county complied with California statutes for the period of July 1, 2014, through June 30, 2020. We conducted the audit pursuant to the requirements of Government Code section 12468.

Our audit found that the county incorrectly calculated the:

- Unitary and operating nonunitary apportionment and allocation;
- Unitary regulated railway apportionment and allocation;
- Educational Revenue Augmentation Fund shift; and
- Vehicle license fee adjustments.

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

Sincerely,

*Original signed by*

KIMBERLY TARVIN, CPA
Chief, Division of Audits

KT/as

cc: Susan Storz, Fiscal Analyst II
Glenn County Department of Finance
Keith Corum, Chairman
Glenn County Board of Supervisors
Chris Hill, Principal Program Budget Analyst
Local Government Unit
California Department of Finance

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# Audit Report

## Summary

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Our audit found that the county incorrectly calculated the:

- Unitary and operating nonunitary apportionment and allocation;
- Unitary regulated railway apportionment and allocation;
- Educational Revenue Augmentation Fund (ERAF) shift; and
- Vehicle license fee (VLF) adjustments.

## 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 these agencies and 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 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 are 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. In general, the amount of revenue an agency or district receives is based on the amount received in the prior year plus a share of the property tax growth within its boundary.

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 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 California 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 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 owed to 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.

## Audit Authority

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 on a one-, three-, or five-year cycle, depending on the county's population. The audit results are reported annually to the Legislature along with any recommendations for corrective action.

## Objective, Scope, and Methodology

Our audit objective 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.

A property tax bill contains the property tax levied at a one percent tax rate pursuant to the requirement of Proposition 13. A tax 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.

The audit period was July 1, 2014, through June 30, 2020.

To achieve our objective, we completed the following tasks:

- We gained an understanding of the county's process for apportioning and allocating property tax revenues, and of the relevant criteria.
- We interviewed key personnel to gain an understanding of the county's process for apportioning and allocating property tax revenues.

- We reviewed the county's written procedures for apportioning and allocating property tax revenues.
- We reviewed documents supporting the transaction flow for apportioning and allocating property tax revenues.
- We judgmentally selected a non-statistical sample of five from approximately 50 taxing jurisdictions within the county for all fiscal years in the audit period.[1] 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 computations and unitary regulated railway computations used to develop apportionment factors (see Findings 1 and 2);
  - 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 (see Finding 3);
  - Reviewed the Sales and Use Tax 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 (see Finding 4); and
  - Reviewed California BOE jurisdictional change filing logs and their impact on the tax apportionment and allocation system.

  Errors found were not projected to the intended (total) population.

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

[1] The actual number of taxing jurisdictions, which include the ERAF, can vary from year to year based on jurisdictional changes. The five sampled taxing jurisdictions include a special district, a school district, a city, the county, and the ERAF. We selected only one of each type of local agency because when the apportionment and allocation for one jurisdiction is incorrect, the error affects every other taxing jurisdiction.

reasonable basis for our findings and conclusions based on our audit objective.

We did not audit the county's financial statements.

## Conclusion

Our audit found that Glenn County did not comply with California statutes for the apportionment and allocation of property tax revenues for the audit period. We found that the county incorrectly calculated the:

- Unitary and operating nonunitary excess apportionment factors by used the prior-year AB 8 factors, pre-ERAF shift, for FY 2014-15 through FY 2018-19;
- Unitary regulated railway excess apportionment factors by using the prior-year AB 8 factors, pre-ERAF shift, for FY 2015-16;
- ERAF shift for Hamilton City Community Services District (CSD), Northeast Willows CSD, and Glenn County Mosquito Abatement and Vector Control special districts by using incorrect prior year revenue amounts for FY 2015-16; and
- VLF adjustment for the City of Orland by not adjusting the Assessed Valuation growth for an annexation in FY 2016-17.

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

## Follow-up on Prior Audit Findings

The county has satisfactorily resolved the findings noted in our prior audit report, for the period of July 1, 2007, through June 30, 2014, issued on October 9, 2015, as shown in the Appendix.

## Views of Responsible Officials

We issued a draft audit report on October 1, 2021. Humberto Medina, Director of Finance, responded by letter dated October 29, 2021 (Attachment), agreeing with the audit results.

## Restricted Use

This audit report is solely for the information and use of Glenn County, the Legislature, the California Department of Finance, 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 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*

KIMBERLY TARVIN, CPA
Chief, Division of Audits

December 6, 2021

# Findings and Recommendations

**FINDING 1— Unitary and Operating Nonunitary Apportionment and Allocation**

During testing of the unitary and operating nonunitary (unitary) apportionment and allocation process, we found that the county incorrectly calculated the unitary excess apportionment factors by using the prior-year AB 8 factors, pre-ERAF shift, for FY 2014-15 through FY 2018-19. The error occurred because the county did not correctly implement procedures for RTC section 100; the error resulted in misallocations to all affected taxing entities. We did not quantify the monetary impact for each affected taxing entity due to various errors affecting the computation and allocation.

RTC section 100 provides the legal requirements for the apportionment and allocation of the unitary and operating nonunitary property tax revenues.

Unitary properties are those properties on which California 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). RTC section 723.1 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 tax revenues. The system created the unitary and operating nonunitary base year, and developed formulas to compute the distribution factors for the fiscal years that followed.

<u>Recommendation</u>

We recommend that the county:

- Review RTC section 100 and update its procedures;
- Recalculate the unitary apportionment factors for FY 2014-15 through FY 2018-19; and
- Make monetary adjustments to school districts and community college districts. Monetary adjustments to all other affected taxing entities will be necessary, if the errors are significant.

<u>County's Response</u>

> We have reviewed the finding and we agree with your comment. We will be recalculating the Unitary Factors for the years indicated and we'll make the necessary adjustments to the prior year's allocations. We have added mitigating controls to avoid the same issue from happening again in the future.

**FINDING 2— Unitary Regulated Railway Apportionment and Allocation**

During testing of the unitary regulated railway apportionment and allocation process, we found that the county incorrectly calculated the regulated railway excess apportionment factors by using the prior-year AB 8 factors, pre-ERAF shift, for FY 2015-16. The error occurred due to an oversight in implementing procedures for RTC section 100.11 and resulting in misallocations to all affected taxing entities. We did not quantify the monetary impact for each affected taxing entity due to various errors affecting the computation and allocation.

RTC section 100.11 provides the legal requirements for the apportionment and allocation of unitary regulated railway property tax revenues.

Unitary regulated railway properties are facilities that were completely constructed and placed in service after January 1, 2007. RTC section 723 defines unit valuation of a property that is operated as a unit in a primary function of the assessee.

Recommendation

We recommend that the county:

- Review RTC section 100.11 and update its procedures; and
- Recalculate the regulated railway excess apportionment factors for FY 2015-16 through FY 2019-20.

County's Response

> We have reviewed the finding and we agree with your comment. We will be recalculating the Unitary Railroad Factors for the years indicated and we will make the necessary adjustments to the prior year's allocations. We have added mitigating controls to avoid the same issue from happening again in the future.

**FINDING 3— Educational Revenue Augmentation Fund**

During testing of the ERAF shift process, we found that the county incorrectly calculated the ERAF shift for Hamilton City CSD, Northeast Willows CSD, and the Glenn County Mosquito Abatement and Vector Control special district by using incorrect prior-year revenue amounts for FY 2015-16. The mistake was due to a clerical error, and resulted in misallocations to the three taxing entities. We did not quantify the monetary impact for the three taxing entities due to various errors affecting the computation and allocation.

RTC sections 96.1 through 96.5 and 97 through 97.3 provide the legal requirements for calculation of the ERAF shift.

In FY 1992-93 and FY 1993-94, some local agencies were required to shift an amount, subsequently annually adjusted for growth, of property tax revenues to the ERAF using formulas detailed in the Revenue and Taxation Code.

Recommendation

We recommend that the county:

- Review RTC sections 96.1 through 96.5 and 97 through 97.3, and update its procedures;
- Recalculate the ERAF shift for FY 2015-16 through FY 2019-20; and
- Make monetary adjustments to the ERAF from the Hamilton City CSD, Northeast Willows CSD, and Glenn County Mosquito Abatement and Vector Control special district.

County's Response

> We have reviewed the finding and we agree with your comment. A correction has been made by recalculating the ERAF Shift for the FY 2015-16 through FY 2019-20, and we will make corrections to the allocations made for those years. We will add mitigating controls to avoid the same issue from happening again in the future.

## FINDING 4—Vehicle License Fee Adjustments

During testing of the VLF adjustment process, we found that the county incorrectly calculated the VLF adjustment for the City of Orland. The county did not adjust the Assessed Valuation growth for annexation in FY 2016-17. The mistake was due to a clerical error, and resulted in an over-allocation of funds to the City of Orland. We did not quantify the monetary impact due to various errors affecting the computation and allocation.

RTC section 97.70 provides the legal requirements for VLF adjustments.

The VLF permanently provided additional property tax revenues to cities and counties in lieu of the discretionary VLF revenues that these agencies previously received.

Recommendation

We recommend that the county:

- Review RTC sections 97.69 and 97.70, and update its procedures;
- Recalculate the VLF adjustments for FY 2016-17 through FY 2019-20; and
- Make monetary adjustments to the ERAF and the City of Orland.

County's Response

> We have reviewed the finding and we agree with your comment. A correction has been made as indicated for the FY 2016-17 Assessed Valuation Growth and we have re-calculated the VLF adjustments for all years. We have added mitigating controls to avoid the same issue from happening again in the future.

# Appendix— Summary Schedule of Prior Audit Findings

The following table shows the implementation status of Glenn County's corrective actions related to the findings contained in the county's prior audit report dated October 9, 2015:

| Prior Audit Finding Number | Prior Audit Finding Title | Implementation Status |
|---|---|---|
| 1 | Calculation and distribution of annual tax increment | Fully implemented |
| 2 | Jurisdictional changes | Fully implemented |
| 3 | Unitary railroad apportionment | Fully implemented |
| 4 | Property tax administrative costs | Fully implemented |
| 5 | Educational Revenue Augmentation Fund | Fully implemented |

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

Humberto Medina, CPA
Interim Director of Finance

# GLENN COUNTY

DEPARTMENT OF FINANCE
516 West Sycamore Street
Willows, California 95988
Auditor-Controller: (530) 934-6476
Treasurer-Tax Collector: (530) 934-6410
FAX (530) 934-6421

Joshua Crane
Assistant Director of Finance

10/29/21

California State Controller's Office, Division of Audits
Attn: Lisa Kurokawa, Chief, Compliance Audits Bureau, Division of Audits
PO Box 942850
Sacramento, CA 94250

Ms Kurokawa:

Please find our responses in reply to the Property Tax Audit Draft Report that was presented to our office on October 1, 2021:

**Finding #1: Unitary Operating Nonunitary Apportionment and Allocation:**

Response: We have reviewed the finding and we agree with your comment. We will be recalculating the Unitary Factors for the years indicated and we'll make the necessary adjustments to the prior year's allocations. We have added mitigating controls to avoid the same issue from happening again in the future.

**Finding #2: Unitary Regulated Railway Apportionment and Allocation:**

Response: We have reviewed the finding and we agree with your comment. We will be recalculating the Unitary Railroad Factors for the years indicated and we will make the necessary adjustments to the prior year's allocations. We have added mitigating controls to avoid the same issue from happening again in the future.

**Finding #3: Educational Revenue Augmentation Fund:**

Response: We have reviewed the finding and we agree with your comment. A correction has been made by recalculating the ERAF Shift for the FY 2015-16 through FY 2019-20, and we will make corrections to the allocations made for those years. We will add mitigating controls to avoid the same issue from happening again in the future.

**Finding #4: Vehicle License Fee Adjustments**

Response: We have reviewed the finding and we agree with your comment. A correction has been made as indicated for the FY 2016-17 Assessed Valuation Growth and we have re-calculated the VLF adjustments for all years. We have added mitigating controls to avoid the same issue from happening again in the future.

Humberto Medina, CPA
Interim Director of Finance

# GLENN COUNTY

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Joshua Crane
Assistant Director of Finance

If you have any questions or concerns, feel free to contact me.

Sincerely,

Humberto Medina, CPA
Director of Finance

Cc: Susan Storz, Fiscal Analyst II

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