

# **LAKE COUNTY**

Audit Report

## **APPORTIONMENT AND ALLOCATION OF PROPERTY TAX REVENUES**

*July 1, 2013, through June 30, 2018*



**BETTY T. YEE**  
California State Controller

February 2020



**BETTY T. YEE**  
California State Controller

February 7, 2020

Cathy Saderlund, Auditor-Controller/County Clerk  
Lake County  
255 N. Forbes Street, 2<sup>nd</sup> Floor  
Lakeport, CA 95453

Dear Ms. Saderlund:

The State Controller's Office audited the methods employed by Lake County to apportion and allocate property tax revenues for the period of July 1, 2013, through June 30, 2018. 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. Specifically, we determined that Lake County incorrectly calculated the:

- Unitary and operating nonunitary apportionment and allocation factors; and
- Property tax administrative fee 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/hf

Attachment

cc: Amanda Johnson, Property Tax Coordinator  
Lake County Auditor-Controller  
Moke Simon, Chair  
Lake 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 Lake County to apportion and allocate property tax revenues for the period of July 1, 2013, through June 30, 2018.

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

- Unitary and operating nonunitary apportionment and allocation factors; and
- Property tax administrative fee (PTAF) factors.

## 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 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 (QE) 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 (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.

## **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, 2013, through June 30, 2018.

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 62 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 (total) 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, computations used to develop apportionment factors;
  - Reviewed Redevelopment Property Tax Trust Fund deposits;
  - 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;
  - Reviewed the Sales and Use Tax letter and recomputed Vehicle License Fee computations used to verify the amount transferred from the ERAF 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 apportionment and allocation 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.

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 Lake 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 unitary and operating nonunitary apportionment and allocation factors; and
- Incorrectly calculated the PTAF factors.

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, 2006, through June 30, 2013, issued on September 26, 2014.

**Views of Responsible Officials**

We issued a draft audit report on December 23, 2019. Cathy Saderlund, Auditor-Controller/County Clerk, responded by letter dated January 5, 2020, agreeing with the audit results. The county's response is included as an attachment to this audit report.

**Restricted Use**

This audit report is solely for the information and use of Lake 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

February 7, 2020



# Findings and Recommendations

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

During our testing of the unitary and operating nonunitary process, we found that the county incorrectly calculated the unitary factors in FY 2013-14. When restating its FY 2013-14 factors to remove the ERAF share, the county inadvertently reapportioned the revenue in excess of the prior-year 102% twice. This error affected the subsequent years.

We did not quantify the monetary impact due to the various components involved in the calculation.

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 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 QE 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.

### Recommendation

We recommend that the county:

- Recalculate the unitary factors for FY 2013-14 through FY 2017-18;
- Make monetary adjustments to schools, the ERAF, and community college districts; and
- Make monetary adjustments to other affected taxing jurisdictions, if significant.

### County’s Response

The county concurs with the finding and indicates that it has recalculated the unitary factors. The county also stated that it will use the corrected calculations in the future, and will make any necessary monetary adjustments.

**FINDING 2—  
Reimbursement of  
Property Tax  
Administrative Costs**

During our testing of the property tax administrative costs process for FY 2016-17 and FY 2017-18, we found that the county incorrectly calculated the PTAF factors because the AB 8 revenues used included pre-ERAF adjustments instead of post-ERAF adjustments. The county informed us that it made the same error for FY 2013-14, FY 2014-15, and FY 2015-16.

We did not quantify the monetary effect due to a concurrent finding in the unitary and operating nonunitary process, which directly affects the PTAF factor calculation.

The error occurred because the county misinterpreted the applicable statutes.

RTC section 95.3 provides the legal requirements for reimbursement of property tax administrative costs.

The County Assessor, the County Tax Collector, the Assessment Appeals Board, and the Auditor-Controller all incur administrative costs associated with the apportionment and allocation of property tax revenues. Applicable statutes enable the county to be reimbursed by local agencies for the aforementioned costs.

**Recommendation**

We recommend that the county:

- Update its policies and procedures to ensure that the AB 8 revenues used in the PTAF factor calculation include post-ERAF adjustments;
- Recalculate the PTAF factors for FY 2013-14 through FY 2017-18; and
- Make monetary adjustments to the affected entities, if significant.

**County's Response**

The county concurs with the finding and indicates that it processed corrections for FY 2013-14 up to the amount allowed by RTC section 96.1. The county also indicated that it will use the corrected calculations in future, and will make necessary adjustments.

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

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**COUNTY OF LAKE**  
**Office of the County Clerk/Auditor-Controller**  
**Courthouse-255 North Forbes Street**  
Lakeport, CA 95453  
Telephone (707) 263-2311  
FAX (707) 263-2310  
Email: auditor@lakecountyca.gov

**Cathy Saderlund**  
Auditor-Controller/County Clerk

**Marcy Harrison**  
Chief Deputy Auditor-Controller

**Lisa Caslan**  
Chief Deputy Auditor-Controller

Ref. No. 20L-066

January 5, 2020

Lisa Kurokawa, Chief  
Compliance Audits Bureau  
State Controller's Office  
Division of Audits  
PO Box 942650  
Sacramento CA 94250

Dear Ms. Kurokawa,

Thank you for the draft audit report pertaining to our property tax allocation and apportionment for the period of July 1, 2013 through June 30, 2018. We received the draft report on December 27, 2019 and our responses are as follows:

**Finding 1—Unitary and operating non-unitary apportionment factors**


The county concurs with this finding and has recalculated the unitary factors as recommended. Due to the complexity of the correction and to ensure complete and accurate factors going forward, the county has obtained the assistance of a property tax expert in a neighboring county for review and dual validation of our prepared correction. The county will use the corrected calculations going forward and make any necessary monetary adjustments.

**Finding 2—Property tax administrative fee factors**

The county concurs with this finding. The corrections were processed for fiscal year 2013-2014 up to the amount allowed pursuant to Revenue and Taxation Code 96.1. The county will use the corrected calculations going forward and any necessary adjustments will be made. This correction will also be reviewed as noted in Finding 1 above.

We would like to extend our appreciation to your staff auditor, Trisha Qulambo and to her manager Scott Freeman for their consideration of our property tax schedule and the cooperative manner in which the audit was conducted.

Respectfully,

  
Cathy Saderlund  
Auditor-Controller

**State Controller's Office  
Division of Audits  
Post Office Box 942850  
Sacramento, CA 94250**

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