MADERA COUNTY

Audit Report

PROPERTY TAX APPORTIONMENT AND ALLOCATION SYSTEM

July 1, 2005, through June 30, 2014

BETTY T. YEE

California State Controller

September 2015

BETTY T. YEE
California State Controller

September 9, 2015

The Honorable Todd Miller
Auditor Controller
Madera County
200 W 4th Street, 2nd Floor
Madera, CA 93637

Dear Mr. Miller:

The State Controller's Office audited the methods employed by Madera County to apportion and allocate property tax revenues for the period of July 1, 2005, through June 30, 2014. The audit was conducted pursuant to the requirements of Government Code section 12468.

Our audit disclosed that the county complied with California statutes, except that it:

- Made transfer errors in the jurisdictional changes we sampled.
- Made calculation errors in its unitary and operating nonunitary process.
- Made carry-forward errors in its unitary railroad computations.
- Made calculation errors in its vehicle licensing fee calculations.

If you have any questions, please contact Elizabeth González, Chief, Local Government Compliance Bureau, by telephone at (916) 324-0622.

Sincerely,

Original signed by

JEFFREY V. BROWNFIELD, CPA
Chief, Division of Audits

JVB/as

Attachment

cc: James Boyajian, Assistant Auditor-Controller
Madera County

Contents

Audit Report

Summary 1

Background 1

Objective, Scope, and Methodology 2

Conclusion 4

Follow-Up on Prior Audit Findings 4

Views of Responsible Officials 4

Restricted Use 5

Findings and Recommendations 6

Schedule 1—Summary of Misallocations to the Educational Revenue Augmentation Fund 10

Attachment—County's Response to Draft Audit Report

Audit Report

Summary

The State Controller's Office (SCO) audited the methods employed by Madera County to apportion and allocate property tax revenues for the period of July 1, 2005, through June 30, 2014.

Our audit disclosed that the county complied with California statutes for the allocation and apportionment of property tax revenues, except that it:

- Made transfer errors in the jurisdictional changes we sampled.
- Made calculation errors in its unitary and operating nonunitary process.
- Made carry-forward errors in its unitary railroad computations.
- Made calculation errors in its vehicle licensing fee (VLF) calculations.

Background

After the passage of Proposition 13 in 1978, the California State Legislature enacted new methods for allocating and apportioning property tax revenues to local government agencies and public schools. The main objective was to provide local government agencies with a property tax base that would grow as assessed property values increased. These methods have 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.

The 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 agencies and schools using prescribed formulas and methods defined in the Revenue and Taxation Code.

The AB 8 base process involved numerous steps, including the transfer of revenues from schools to local agencies (AB 8 shift) and the development of the tax rate area annual tax increment apportionment factors (ATI 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 apportionment 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 revenues generated by unitary and nonunitary properties, regulated railway companies, and qualified electric properties from the AB 8 process. These revenues are now allocated and apportioned 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 allocated and apportioned to schools by the county auditor according to instructions received from the county superintendent of schools or the State Chancellor of Community Colleges.

Revenues generated by the different types of property tax are allocated and apportioned to local agencies and schools 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 maintained primarily by the county assessor. Tax rolls contain an entry for each parcel of land, including the parcel number, the owner's name, and the value. Following are the types of property tax rolls:

- *Secured Roll*—This roll contains property that, in the opinion of the assessor, has sufficient value to guarantee payment of the tax levies and that, if necessary, can be sold by the tax collector to satisfy unpaid tax levies.

- *Unsecured Roll*—This roll contains property that, in the opinion of the assessor, does not have sufficient "permanence" or have other intrinsic qualities to guarantee payment of taxes levied against it.

- *State-Assessed Roll*—This roll contains public utility, railroad, and qualified electric properties, assessed as either unitary or nonunitary property by the State Board of Equalization.

- *Supplemental Roll*—This roll contains 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 taxes, Senate Bill 418 was enacted in 1985 requiring the State Controller to audit the counties' apportionment and allocation methods and report the results to the California State Legislature.

Objective, Scope, and Methodology

Our audit objective was to review the county's apportionment and allocation of property tax revenues to local government agencies and public schools within its jurisdiction to determine whether the county complied with Revenue and Taxation Code requirements.

To meet the objective, we reviewed the county's procedures for apportioning and allocating property tax revenues used by the county auditor and the processes used by the tax collector and the assessor.

We performed the following procedures:

- Conducted tests to determine whether the county correctly apportioned and allocated property tax revenue.
- Interviewed key personnel and reviewed supporting documentation to gain an understanding of the county's property tax apportionment and allocation processes.
- Reviewed apportionment and allocation reports prepared by the county showing the computations used to develop the property tax distribution factors.
- Reviewed tax rate area (TRA) reports to verify that the annual tax increment was computed properly.
- Reviewed county unitary and operating nonunitary reports and Board of Equalization reports and verified the computations used by the county to develop the unitary and operating nonunitary property tax distribution factors.
- Reviewed redevelopment agency (RDA) reports prepared by the county and verified the computations used to develop the project base amount and the tax increment distributed to the RDA.
- Reviewed successor agency Recognized Obligation Payment Schedules (ROPS) and county apportionment and allocation reports addressing the Redevelopment Property Tax Trust fund (RPTTF).
- Reviewed property tax administration cost reports prepared by the county and verified administrative costs associated with procedures used for apportioning and allocating property tax to local government agencies and school districts.
- Reviewed ERAF reports prepared by the county and verified the computations used to determine the shift of property taxes from local agencies to the ERAF and, subsequently, to public schools.
- Reviewed SUT and VLF reports and computations used to verify the amount of ERAF transferred to counties and cities to compensate for the diversion of these revenues.

We conducted this performance audit under the authority of Government Code sections 12468 and 12410. We did not audit the county's financial statements. 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 objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

The audit covered the period of July 1, 2015, through June 30, 2014. Our audit scope was limited to:

- Reviewing operational procedures and significant applicable controls over the apportionment and allocation process;
- Examining selected property tax apportionment and allocation records; and
- Reviewing related property tax revenue data used to determine the apportionment and allocation computation process.

A property tax bill contains the property tax levied at a 1% tax rate pursuant to the requirement of Proposition 13. A bill may also contain special taxes, debt services 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 1% 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.

We limited our review of the county's internal controls to gaining an understanding of the transaction flow in order to develop appropriate auditing procedures. We did not evaluate the effectiveness of all internal controls.

In addition, we tested transactions used to apportion and allocate property taxes and performed other procedures deemed necessary. This report relates solely to the method used by the county to apportion and allocate property taxes.

Conclusion

Our audit disclosed that, except for the items discussed in the Findings and Recommendations section of this report, Madera County complied with California statutes for the apportionment and allocation of property tax revenues for the period of July 1, 2005, through June 30, 2014. The county should correct the items discussed in the Findings and Recommendations section.

Follow-up on Prior Audit Findings

The county has satisfactorily resolved the findings noted in our prior audit report, issued July 2006.

Views of Responsible Officials

We issued a draft report on June 18, 2015. Todd Miller, Auditor-Controller, responded by letter dated July 2, 2015 (Attachment), agreeing with the audit results.

Restricted Use

This report is solely for the information and use of the County, the California 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

September 9, 2015

Findings and Recommendations

FINDING 1—Jurisdictional changes

In fiscal year (FY) 2010-11, the county transferred the assessed value and corresponding parcels for the sampled jurisdictional changes a year later than specified in the Board of Equalization (BOE) change notice. More importantly, one of the transfers was made to an incorrect Tax Rate Area (TRA). As the TRA has the same increment factors as the specified TRA, no increment impact will be noted. However, county maps will not agree with BOE maps.

The legal requirements for jurisdictional changes are found in Revenue and Taxation Code section 99. A jurisdictional change involves a change in the organization or boundaries of a local government agency or school district. Normally, these are service area or responsibility changes between the local jurisdictions. As part of the jurisdictional change, the local government agencies are required to negotiate any exchange of base year property tax revenue and annual tax increment. After the jurisdictional change, the local agency whose responsibility increased receives additional annual tax increment, and the base property tax revenues are adjusted according to the negotiated agreements.

Recommendation

The county should reconcile its mapping with the BOE to correct the noted error.

County Response

> The mismapping of parcels in fiscal year 2010-11, as referred to in the finding, was corrected in a subsequent fiscal year. The County's parcel mapping now agrees with BOE's mapping for Madera County.

SCO's Comment

The SCO agrees with the county's corrective action. The SCO will review the implementation of the corrections in the next audit.

FINDING 2—Unitary and operating nonunitary apportionment

Beginning with FY 2006-07, the county carried forward incorrect prior-year revenues.

In FY 2007-08 through FY 2013-14, the county included railroad in the unitary calculations.

The county attempted to correct the unitary factor computations in 2014. In this correction, the computation for FY 2005-06 through FY 2006-07 and FY 2007-08 through FY 2008-09 was incorrect. The county carried forward incorrect prior-year revenues, resulting in incorrect computations for all following years. These changes have not been used to adjust prior allocations at this time.

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

Unitary properties are those properties on which the Board of Equalization "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). The Revenue and Taxation Code further 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

The county should re-compute unitary and operating nonunitary revenues for all fiscal years noted above.

County Response

> The County Auditor-Controller recalculated apportionments of Unitary and Operating Nonunitary revenues from 2006-07 through 2013-14. The recalculations result in the carryforward of correct prior year Unitary and Operating Nonunitary revenues to fiscal year 2014-15 apportionments. The recalculations produce immaterial reapportionments of Unitary and Operating Nonunitary revenues from 2006-07 through 2013-14.

SCO's Comment

The SCO agrees with the county's corrective action. The SCO will review the implementation of the corrections in the next audit.

FINDING 3—Unitary railroad apportionment

The county did not properly establish the railroad property tax in FY 2007-08, as required. The county attempted to correct the railroad factor computation in 2014. The FY 2007-08 base-year computation was computed correctly; however, for FY 2008-09, the railroad computation did not carry forward prior-year revenues, including excess growth, as required. This practice was continued throughout the audit period. These changes have not been used to adjust prior allocations at this time.

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

Unitary properties are those properties on which the Board of Equalization "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). The Revenue and Taxation Code further 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

The county should re-compute the unitary railroad revenues for all fiscal years noted above.

County Response

> County Auditor-Controller recalculated apportionments of Railroad Unitary revenues from fiscal year 2007-08 through 2013-14. The recalculations result in the carryforward of correct prior year Railroad Unitary revenues to fiscal year 2014-15. The recalculations produce immaterial reapportionments of Railroad Unitary revenues from 2007-08 through 2013-14.

SCO's Comment

The SCO agrees with the county's corrective action. The SCO will review the implementation of the corrections in the next audit.

FINDING 4—
Vehicle Licensing Fee adjustments

The county used incorrect prior year assessed values when calculating the vehicle licensing fee (VLF) swap growth in FY 2006/07, causing the VLF swap to be misallocated for FY 2006-07 forward in the amount of $5,856,457 (owed from the Educational Revenue Augmentation Fund [ERAF]).

Requirements for the ERAF adjustment for the VLF and sales and use tax (SUT) are found in Revenue and Taxation Code sections 97.68-97.70. In FY 2004-05, the county was given a VLF estimate that was to be transferred from the ERAF to the Vehicle License Fee Property Tax Compensation Fund, and eventually to the county and cities. In FY 2005-06, the county was given another estimate, including true-ups. In FY 2006-07 and subsequent years, the county calculates the VLF adjustment based on the prior-year VLF adjusted for growth. The growth for the county's VLF should be based on countywide growth, not only on unincorporated parcels. The growth for each city's VLF should be based on the growth of all incorporated parcels in all Tax Rate Areas within the city.

The SUT amounts for each county and cities within the county are provided by the Department of Finance, on or before September 1st of each fiscal year. These amounts are to be transferred from the ERAF to the SUT Compensation Fund, and eventually to each designated county and cities within each county.

Recommendation

The county should recalculate the VLF amounts, beginning in FY 2006-07, and correct the misallocated amounts. The county should use the corrected calculations going forward.

County Response

> County Auditor-Controller has recalculated the VLF amounts for 2006-07 through 2013-14. The corrected VLF allocations were carried forward and used in the 2014-15 VLF allocations to the County and Cities. During fiscal year 2015-16 Auditor-Controller will transfer $1,228,734 from the Educational Revenue Augmentation Fund to correct the 2006-07 through 2013-14 VLF allocations to the County and cities, as allowed under R & T Code Section 96.1.

SCO's Comment

The SCO agrees with the county's corrective action. The SCO will review the implementation of the corrections in the next audit.

Schedule 1—
Summary of Misallocations to the Educational Revenue Augmentation Fund July 1, 2005, through June 30, 2014

Finding No.	Years Affected	Amount Due to (owed from) the ERAF
4	2006-07 – 2013-14	$ (5,856,457)
Total		$ (5,856,457)

Note: Revenue and Taxation Code section 96.1 limits the maximum amount of cumulative reallocation to 1% of the 1% tax levied on the current (2014-15) fiscal-year secured-assessed value. This amount for Madera County is $1,228,734.

Attachment—
County's Response to
Draft Audit Report

TODD E. MILLER
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July 2, 2015

Elizabeth González, Chief
Local Government Compliance Bureau
State Controller's Office
Division of Audits
P.O. Box 942850
Sacramento, CA 94250-5874

Enclosed please find County of Madera Auditor-Controller responses to State Controller's findings in the Audit of Madera County's Property Tax Apporionment and Allocation System covering fiscal years 2005-06 though 2013-14.

I want to take this opportunity to thank the State Controller for the assistance we received in administering the property tax apportionment and allocation process in Madera County. I commend the State Controller's audit staff for their knowledge and dilligence in their review and recommendations for corrections to the process in Madera County. We look forward to the State Controller's future regularly scheduled audits of the County's tax apportionment and allocation process.

Sincerely,

Todd E. Miller
Madera County Auditor-Controller

Response to Findings in the Audit Report of Property Tax Apportionment and Allocation System of Madera County, July 1, 2005, through June 30, 2014

Finding 1. Jurisditional Changes.

The mismapping of parcels in fiscal year 2010-11, as referred to in the finding, was corrected in a subsequent fiscal year. The County's parcel mapping now agrees with BOE's mapping for Madera County.

Finding 2. Unitary and Operating Nonunitary Apportionment.

The County Auditor-Controller recalculated apportionments of Unitary and Operating Nonunitary revenues from 2006-07 through 2013-14. The recalculations result in the carryforward of correct prior year Unitary and Operating Nonunitary revenues to fiscal year 2014-15 apportionments. The recalculations produce immaterial reapportionments of Unitary and Operating Nonunitary revenues from 2006-07 through 2013-14.

Finding 3. Unitary Railroad Apportionment.

County Auditor-Controller recalculated apportionments of Railroad Unitary revenues from fiscal year 2007-08 through 2013-14. The recalculations result in the carryforward of correct prior year Railroad Unitary revenues to fiscal year 2014-15. The recalculations produce immaterial reapportionments of Railroad Unitary revenues from 2007-08 through 2013-14.

Finding 4. Vehicle Licensing Fee adjustments.

County Auditor-Controller has recalculated the VLF amounts for 2006-07 through 2013-14. The corrected VLF allocations were carried forward and used in the 2014-15 VLF allocations to the County and Cities. During fiscal year 2015-16 Auditor-Controller will transfer $1,228,734 from the Educational Revenue Augmentation Fund to correct the 2006-07 through 2013-14 VLF allocations to the County and cities, as allowed under R & T Code Section 96.1.

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