

# **SAN MATEO COUNTY**

Audit Report

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

*July 1, 2017, through June 30, 2023*



**MALIA M. COHEN**  
CALIFORNIA STATE CONTROLLER

March 2025



MALIA M. COHEN  
CALIFORNIA STATE CONTROLLER

March 28, 2025

The Honorable Juan Raigoza, Auditor-Controller  
San Mateo County  
555 County Center, Floor 4  
Redwood City, CA 94063

Dear Auditor-Controller Raigoza:

The State Controller's Office audited San Mateo County's (the county) process for apportioning and allocating property tax revenues for the period of July 1, 2017, through June 30, 2023. We conducted the audit pursuant to the requirements of Government Code section 12468.

Our audit found that the county did not comply with California statutes for the apportionment and allocation of property tax revenues during the audit period because it incorrectly calculated the excess Educational Revenue Augmentation Fund amount.

The county has disputed certain facts related to the finding and recommendation contained in this audit report. The State Controller's Office has an informal audit review process by which to resolve a dispute of facts. To request a review, the county should submit, in writing, a request for a review and all information pertinent to the disputed issues within 60 days after receiving this audit report.

The request and supporting documents should be submitted to Ryan Seeley, Chief Counsel, State Controller's Office, Post Office Box 942850, Sacramento, California 94250. In addition, please provide a copy of the request letter to Lisa Kurokawa, Chief, Compliance Audits Bureau, State Controller's Office, Division of Audits, Post Office Box 942850, Sacramento, California 94250.

If you have any questions regarding this report, please contact Lisa Kurokawa, Chief, Compliance Audits Bureau, by telephone at 916-327-3138, or email at [lkurokawa@sco.ca.gov](mailto:lkurokawa@sco.ca.gov). Thank you.

Sincerely,

*Original signed by*

Kimberly A. Tarvin, CPA  
Chief, Division of Audits

Mr. Juan Raigoza

March 28, 2025

Page 2 of 2

KAT/ac

Copy: Amanda Johnson, Manager

Property Tax Division

San Mateo County Auditor-Controller's Office

The Honorable Warren Slocum, President

San Mateo County Board of Supervisors

Chris Hill, Principal Program Budget Analyst

Local Government Unit

California Department of Finance

Ryan Seeley, Chief Counsel

State Controller's Office

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# Audit Report

## Summary

The State Controller's Office (SCO) audited San Mateo County's (the county) process for apportioning and allocating property tax revenues to determine whether the county complied with California statutes for the period of July 1, 2017, through June 30, 2023.

Our audit found that the county did not comply with California statutes for the apportionment and allocation of property tax revenues during the audit period because it incorrectly calculated the excess Educational Revenue Augmentation Fund (ERAF) amount.

## 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.

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 and subsequent fiscal years. The methodology is commonly referred to as the "AB 8 process."

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 that 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 boundaries.

The AB 8 process involves several steps, including the transfer of revenues from school and community college districts to local government agencies 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 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 apportionment factors.

Subsequent laws 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 laws 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.

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.
- *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 SCO 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. The 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 (e.g., funds intended for the ERAF, school districts, or community college districts). The 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 SCO with broad authority to "superintend the fiscal concerns of the state." GC section 12418 provides the SCO 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 SCO 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 SCO.

## **Audit Authority**

We conducted this audit in accordance with GC section 12468, which authorizes 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**

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 during the period of July 1, 2017, through June 30, 2023.

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 limited to 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.

To achieve our objective, we performed the following procedures:

- We gained an understanding of the county’s processes and internal controls by interviewing key personnel, reviewing the county’s written procedures, and reviewing the county’s transaction flow for apportioning and allocating property tax revenues.
- We assessed the reliability of data from the property tax system by interviewing county staff members knowledgeable about the system, tracing transactions through the system, and recalculating data produced by the system. We determined that the data was sufficiently reliable for purposes of this report.
- We judgmentally selected a non-statistical sample of five from approximately 132 taxing jurisdictions within the county for all fiscal years in the audit period.

The actual number of taxing jurisdictions can vary from year to year based on jurisdictional changes. For testing purposes, we included the ERAF in our sample of taxing jurisdictions. We also tested a special district, a school district, a city, and the county. We only selected 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.

We tested the sampled jurisdictions as follows:

- We tested apportionment and allocation reports to verify computations used to develop property tax apportionment factors.
- We tested TRA reports to verify that the correct TRA factors were used in the computation of the ATI.
- We 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.
- We verified computations used to develop supplemental property tax apportionment factors.
- We verified unitary and operating nonunitary, and unitary regulated railway computations used to develop apportionment factors.
- We reviewed redevelopment agency reports and verified computations used to develop the project base amount and the tax increment distributed to the redevelopment agency.
- We reviewed Redevelopment Property Tax Trust Fund deposits.
- We reviewed property tax administrative 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.
- We 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.
- We verified Vehicle License Fee computations used to determine the amount transferred from the ERAF to counties and cities to compensate for the diversion of these revenues.
- We reviewed tax equity allocation reports to determine any increases in property tax revenues due cities having low or nonexistent property tax amounts.
- We reviewed California State Board of Equalization 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 reasonable basis for our findings and conclusions based on our audit objective.

**Conclusion**

Our audit found that the county did not comply with California statutes for the apportionment and allocation of property tax revenues for the audit period because it incorrectly calculated the excess ERAF amount.

This instance of noncompliance is described in the Finding and Recommendation section.

**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, 2013, through June 30, 2017, issued on March 10, 2020. The implementation status of corrective actions is described in the Appendix.

**Views of Responsible Officials**

We issued a draft audit report on October 17, 2024. The county's representative responded by letter dated November 1, 2024, disagreeing with the audit results. This final audit report includes the county's response as an attachment.

**Restricted Use**

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

Kimberly A. Tarvin, CPA  
Chief, Division of Audits

March 28, 2025

# Finding and Recommendation

**FINDING—  
Excess Educational  
Revenue Augmentation  
Fund amount**

During our testing of the county's excess ERAF calculations, we found that the county included residual revenues from former redevelopment agencies in its excess ERAF calculations beginning with FY 2019-20. Instead, the county should have excluded those residual revenues from its excess ERAF calculations.

This error contributed to an increase in excess ERAF, totaling \$49,830,201, for FY 2019-20 through FY 2022-23. The error occurred because the county incorrectly implemented Health and Safety Code (HSC) section 34188(d), RTC section 97.2(d)(4)(B), and RTC section 97.3(d)(4)(B).

HSC section 34188(d) prohibits increasing allocations of excess, additional, or remaining funds to cities, counties, cities and counties, or special districts that would otherwise have received allocations pursuant to RTC sections 97.2(d)(4)(B)(i), 97.3(d)(4)(B)(i), or 98 et seq.

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 HSC section 34188(d), RTC section 97.2(d)(4)(B), and RTC section 97.3(d)(4)(B);
- Exclude residual revenue from former redevelopment agencies from its excess ERAF calculations;
- Recalculate its excess ERAF for FY 2019-20 through FY 2022-23; and
- Make monetary adjustments to increase the ERAF by \$49,830,201.

## County's Response

We respectfully disagree with the SCO's proposed audit finding and object to its recommendations. The County has lawfully and fully complied with HSC § 34188(d), and RTC §§ 97.2(d)(4)(B), and 97.3(d)(4)(B). SCO's recommendation to "exclude" former RDA [Redevelopment Agency] residual revenues from the County's excess ERAF calculations, even though those revenues would not result in an increase in excess ERAF as compared to the excess ERAF had HSC § 34188(d) "not been enacted," is contrary to the plain language of the statute. Such an interpretation would also be contrary to the pro rata

distribution of property tax revenues required by the Health & Safety Code and state constitutional provisions.

In view of the above, the County's calculations of excess ERAF are proper and the County objects to the SCO's recommendation to recalculate excess ERAF from FY 2019-20 through FY 2022-23; and to make monetary adjustments to the ERAF in the amount of \$29,880,825. Following the SCO's recommendation would be contrary to the express requirements of HSC § 34188(d), RTC §§ 97.2(d)(4)(B), and 97.3(d)(4)(B), and unconstitutional...

...HSC § 34188(d) does not state that RDA residual must be "excluded" from excess ERAF calculations or that RDA residual distributions cannot increase excess ERAF. Rather, the statute states that these distributions shall not increase excess ERAF "that otherwise would have been allocated . . . had this section [i.e., HSC § 34188] not been enacted."

...the SCO's own counsel confirmed by letter, dated July 7, 2021, to the auditors of Marin, Napa, Santa Clara, and San Mateo Counties that the above interpretation is "in harmony with" the directives in the SCO excess ERAF Guidance, released February 16, 2021. The SCO's letter did not state that RDA residual should be "excluded" altogether from excess ERAF calculations or that the auditors' interpretation was incorrect.

...While we strongly believe there should be no finding against the County in any amount, the SCO's improper exclusion of RDA residual from the basic aid determination (and thus from basic aid school districts) is further contrary to law and materially inflates its improper finding. The total impact on excess ERAF if RDA residual is excluded only from non-basic aid school districts would be \$30,286,985, not \$49,830,201, for FY 2019-20 through FY 2022-23. If our understanding of the SCO's calculation methodology is incorrect or you have questions, please let us know.

#### SCO Comment

Our finding and recommendation remain unchanged.

The county's April 2021 letter to the SCO states that the county is in compliance with the SCO's "Excess Educational Revenue Augmentation Fund Revenue Guidance" ("Excess ERAF Guidance"; see Attachment B) without providing excess ERAF calculations. Our Chief Counsel relied on the county's representation that the county was complying with the "Excess ERAF Guidance" when he stated that the county was "in harmony" with it. Furthermore, the Chief Counsel's letter should not be used to verify any excess ERAF calculations.

The SCO's directions for calculating excess ERAF are as follows:

1. Determine the amount of ERAF revenues.
2. Reduce ERAF allocations to required funding levels or "ERAF Entitlement" for school entities/programs.
3. Remaining ERAF revenues are considered "Excess ERAF."

In its response to the finding, the county neglected to mention a key part of the “Excess ERAF Guidance,” which is that ERAF allocations are to be reduced to required funding levels for school entities and programs. When calculating excess ERAF revenues, the county did not properly reduce allocations for school entities to the required funding levels. Moreover, the county included residual property tax revenues when it determined its amount of ERAF revenues. As a result, the excess ERAF was overstated.

Per HSC section 34188(d), the residual property tax revenues cannot contribute to an increase in excess ERAF. Accordingly, counties must exclude revenues distributed under HSC section 34188 from their excess ERAF calculations. Furthermore, we have interpreted RTC section 34188(d) as a cap on excess ERAF such that the county must calculate its ERAF allocations prior to making distributions under RTC section 34188. Accordingly, for purposes of calculating excess ERAF, school districts should only be considered basic aid if they were basic aid prior to the receipt of RDA residual distributions.

We express no opinion as to the constitutionality of HSC section 34188. However, counties may not choose to disregard the requirements of HSC section 34188 on the basis of such an argument.

Article 3, section 3.5, subdivision (a) of the California Constitution prohibits administrative agencies from declaring that a statute is unenforceable, or refusing to enforce a statute on the basis of it being unconstitutional unless an appellate court has determined that the statute is in fact unconstitutional. To date, we are unaware of any appellate court decision ruling that HSC section 34188 is unconstitutional or otherwise unenforceable. As a result, counties must continue to adhere to the requirements of HSC section 34188.

In addition, we should clarify that the amount due the ERAF is \$49,830,201, not \$29,880,825. The limitations under RTC section 96.1(c)(3) are not applicable in this instance, as it only applies in instances of “allocations” of property tax monies. In this situation, the county has misapplied the requirements of HSC section 34188.

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**Schedule—**  
**Summary of Misallocations to the**  
**Educational Revenue Augmentation Fund**  
**July 1, 2017, through June 30, 2023**

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| <u>Fiscal Years Affected</u>  | <u>Amount Due<br/>to the<br/>ERAF</u> |
|-------------------------------|---------------------------------------|
| FY 2019-20 through FY 2022-23 | \$49,830,201                          |

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## Appendix— Summary of Prior Audit Findings

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The following table shows the implementation status of the San Mateo County's corrective actions related to the findings contained in our prior audit report dated March 10, 2020:

| <b>Prior Audit Finding Number</b> | <b>Prior Audit Finding Title</b>                      | <b>Implementation Status</b> |
|-----------------------------------|---|------------------------------|
| 1                                 | Computation and distribution of property tax revenues | Fully implemented            |
| 2                                 | Reimbursement of property tax administrative costs    | Fully implemented            |
| 3                                 | Vehicle License Fee adjustments                       | Fully implemented            |

**Attachment A—  
San Mateo County’s Response to Draft Audit Report**

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**COUNTY OF SAN MATEO**  
**OFFICE OF THE CONTROLLER**

**Juan Raigoza**  
Controller

**Kristie Silva**  
Assistant Controller

**Kim-Anh Le**  
Deputy Controller

**Patrick Enriquez**  
Deputy Controller

**County Government Center**  
555 County Center, 4th Floor  
Redwood City, CA 94063  
650-363-4777  
<https://smcgov.org/controller>

November 1, 2024

Via email: [lkurokawa@sco.ca.gov](mailto:lkurokawa@sco.ca.gov)

Ms. Lisa Kurokawa  
Chief, Compliance Audits Bureau  
Division of Audits  
State Controller's Office  
P.O. Box 942850  
Sacramento, California 94250

Re: Response to SCO's San Mateo County Draft Audit Report, Apportionment and Allocation of Property Tax Revenues, July 1, 2017 through June 30, 2023

Dear Ms. Kurokawa:

We are in receipt of the draft *San Mateo County Audit Report, Apportionment and Allocation of Property Tax Revenues, July 1, 2017 through June 30, 2023*, issued by the State Controller's Office (SCO), dated October 17, 2024. This letter provides our response to the draft report and our views as to its proposed conclusion, finding, and recommendation. The SCO's single proposed finding and associated recommendations are based on an erroneous interpretation of Health & Safety Code § 34188(d) and related statutes; an interpretation that is the subject of legal challenge against the SCO in two pending lawsuits by other counties. We disagree with the proposed finding and request that the SCO withdraw it.

**Summary of Draft Report Finding and Recommendations**

The draft report covers six fiscal years and contains one proposed finding, referred to as "Excess Educational Revenue Augmentation Fund Amount." The draft report asserts that "the county included residual revenues from former redevelopment agencies in its excess ERAF calculations beginning with FY 2019-20. Instead, the county should have excluded those residual revenues from its excess ERAF calculation."



The draft report contends that this "error contributed to an increase in excess ERAF, totaling an estimated \$49.8 million, for FY 2019-20 through FY 2022-23. The error occurred because the county incorrectly implemented Health and Safety Code (HSC) section 34188(d), [Revenue & Taxation Code (RTC)] section 97.2(d)(4)(B), and RTC section 97.3(d)(4)(B)."

The draft report notes that pursuant to RTC § 96.1(c)(3), the maximum amount of cumulative reallocation for the alleged error is limited to \$29,880,825 which is equal to one percent of the County's total amount levied at the one-percent rate of the current year's (FY 2023-24) original secured tax roll assessed value.

The draft report refers to HSC § 34188(d), **but notably omits** critical language in the statute that contradicts the SCO's statutory interpretation. The draft report states that HSC § 34188(d) "prohibits increasing allocations of excess, additional, or remaining funds to cities, counties, cities and counties, or special districts that would otherwise have received allocations pursuant to RTC sections 97.2(d)(4)(B)(i), 97.3(d)(4)(B)(i), or 98 et seq." But, as discussed in this letter, HSC § 34188(d) only applies to former redevelopment agency residual distributions that increase excess ERAF allocations as compared to what those allocations would have been "had this section [§ 34188] not been enacted."

The draft report recommends that the County:

- Review HSC section 34188(d), RTC section 97.2(d)(4)(B), and RTC section 97.3(d)(4)(B);
- Exclude residual revenue from former RDAs [i.e., redevelopment agencies] from its excess ERAF calculations;
- Recalculate its excess ERAF from FY 2019-20 through FY 2022-23; and
- Make monetary adjustments to the ERAF.

#### **County's Response to Draft Report**

We respectfully disagree with the SCO's proposed audit finding and object to its recommendations. The County has lawfully and fully complied with HSC § 34188(d), and RTC §§ 97.2(d)(4)(B), and 97.3(d)(4)(B). SCO's recommendation to "exclude" former RDA residual revenues from the County's excess ERAF calculations, even though those revenues would not result in an increase in excess ERAF as compared to the excess ERAF had HSC § 34188(d) "not been enacted," is contrary to the plain language of the statute. Such an interpretation would also be contrary to the pro rata distribution of property tax revenues required by the Health & Safety Code and state constitutional provisions.

In view of the above, the County's calculations of excess ERAF are proper and the County objects to the SCO's recommendation to recalculate excess ERAF from FY 2019-20 through FY 2022-23; and to make monetary adjustments to the ERAF in the amount of \$29,880,825. Following the

SCO's recommendation would be contrary to the express requirements of HSC § 34188(d), RTC §§ 97.2(d)(4)(B), and 97.3(d)(4)(B), and unconstitutional, as further explained below.

**The County Has Complied with Revenue & Taxation Code §§ 97.2(d)(4)(B), and 97.3(d)(4)(B)**

The County accounts for ERAF contributions at the jurisdictional level, while RDA residual revenues are allocated at the tax rate area (TRA) level using increment factors. Since there is no increment factor for ERAF at the TRA level, the County does not allocate RDA residual revenues to the ERAF. As the County does not allocate residual revenues to the ERAF, such residual does not contribute to an increase in excess ERAF for purposes of HSC § 34188(d).

The County's jurisdictional shift to ERAF pursuant to RTC §§ 97.2 and 97.3 has never been the subject of an audit finding.

The County applies RTC § 97.2(d)(4)(B) and 97.3(d)(4)(B) to return excess ERAF to the county, cities, and special districts in proportion to their contributions of property tax revenue to the ERAF after non-basic aid school districts are funded to their LCFF level and certain special education funding is provided, as required by law.

**The County Has Complied with HSC § 34188(d)**

HSC § 34188(d) reads in full as follows:

This section shall not be construed to increase any allocations of excess, additional, or remaining funds that would otherwise have been allocated to cities, counties, cities and counties, or special districts pursuant to clause (i) of subparagraph (B) of paragraph (4) of subdivision (d) of Section 97.2, clause (i) of subparagraph (B) of paragraph (4) of subdivision (d) of Section 97.3, or Article 4 (commencing with Section 98) of Chapter 6 of Part 0.5 of Division 1, of the Revenue and Taxation Code, **had this section not been enacted**. (emphasis added).

HSC § 34188(d) does not state that RDA residual must be "excluded" from excess ERAF calculations or that RDA residual distributions cannot increase excess ERAF. Rather, the statute states that these distributions shall not increase excess ERAF "that otherwise would have been allocated . . . had this section [*i.e.*, HSC § 34188] not been enacted." This subdivision thus requires a comparison between how RDA residual distributions might increase the amount of excess ERAF allocated pursuant to HSC § 34188 and the amount of excess ERAF allocated had HSC § 34188 "not been enacted."

The amount of excess ERAF allocated by the County under both scenarios would be the same, such that the County's approach fully complies with the section's requirements. The application of HSC § 34188 to the distribution of residual RDA funds does not cause an increase in allocations of excess ERAF beyond what would be allocated had HSC § 34188 not been enacted. This is because certain provisions of HSC § 34188 requiring adjustments to RDA residual distributions

have been ruled inoperable by the appellate court's decision in *Chula Vista v. Sandoval*, 49 Cal.App.5th 539, 562-63 (2020). Specifically, the adjustments or "haircuts" to RDA residuals based on passthrough payments received by taxing agencies contemplated by HSC § 34188(a)(2) - adjustments that *would* affect excess ERAF allocations - are no longer operable after *Chula Vista*. In the absence of such adjustments, the RDA residual is distributed pro rata to the affected taxing entities under HSC § 34188. Notably, the draft report does not suggest that the County should apply the now inoperable HSC § 34188(a)(2) to adjust RDA residual distributions.

This result is the same had HSC § 34188 not been enacted: Without HSC § 34188, RDA residual would still be distributed pro rata as property taxes to the respective taxing entities, as required by the California Constitution and HSC. See Cal. Const., Art. XVI, § 16(b); HSC § 33670(b). Thus, under the correct application of the statute, there is no difference in the amount of excess ERAF allocated pursuant to HSC § 34188 and the amount that would be allocated had HSC § 34188 "not been enacted." Accordingly, no adjustment to the excess ERAF calculations is required or allowed under HSC § 34188(d).

Consistent with this methodology, the SCO's own counsel confirmed by letter, dated July 7, 2021, to the auditors of Marin, Napa, Santa Clara, and San Mateo Counties that the above interpretation is "in harmony with" the directives in the SCO excess ERAF Guidance, released February 16, 2021. The SCO's letter did not state that RDA residual should be "excluded" altogether from excess ERAF calculations or that the auditors' interpretation was incorrect. SCO's current and different interpretation of HSC § 34188(d) as reflected in the draft audit report has resulted in legal challenges by Marin County and Santa Clara County.

The County's approach to excess ERAF calculations has been and remains in full compliance with HSC § 34188(d), the ERAF statutes, and the SCO Guidance. The pro rata distributions of RDA residual to non-basic aid school districts do not increase allocations of excess ERAF as compared to those allocations had HSC § 34188(d) not been enacted, thus, no adjustments to the excess ERAF calculations are required. We note that adopting the County's proper application of HSC § 34188(d) does not require the SCO to declare any statute unconstitutional or to otherwise exceed its authority. The SCO need only apply HSC 34188(d) in accordance with its plain terms and in compliance with the *Chula Vista* decision. By contrast, the SCO's interpretation would violate statutory and constitutional provisions that require distribution of property taxes pro rata and prohibit reductions of property tax allocations to local agencies to offset state obligations. Cal. Const., Article XIII, § 25.5.

Further, the County understands that the SCO is directing the County to comply with HSC § 34188(d) by excluding RDA residual revenues allocated to school districts from the County's excess ERAF calculations. While we disagree with this recommendation, the limited calculations the SCO has provided indicate that the SCO would also require exclusion of RDA residual revenues from the initial determination of a school district's basic aid/LCFF status. This additional proposed change would incorrectly alter the status (basic aid vs LCFF) of some school districts in San Mateo County and violate the law on several grounds, including Education Code (EC) §

42238.02(j)(7), which expressly requires inclusion of such RDA residual revenues in determining a district's basic aid/LCFF status.

Moreover, by law, basic aid school districts cannot receive ERAF (RTC §§ 95(n), 97.2(d)(2)(A) and (d)(3), 97.3(d)(2) and (d)(3); EC § 42238.02(o)); therefore, RDA residuals received by such basic aid school districts should have no impact on the allocation of excess ERAF. But by converting basic aid districts into non-basic aid districts, the SCO's calculations would provide ERAF to districts that should be considered basic aid, which in turn improperly impacts excess ERAF. SCO's application of the law, as recommended, violates HSC § 34188(d), a statute that only concerns itself with excess ERAF allocations and which has no impact on the determination of school districts' basic aid status that is defined by EC 42238.02.

While we strongly believe there should be no finding against the County in any amount, the SCO's improper exclusion of RDA residual from the basic aid determination (and thus from basic aid school districts) is further contrary to law and materially inflates its improper finding. The total impact on excess ERAF if RDA residual is excluded only from non-basic aid school districts would be \$30,286,985, not \$49,830,201, for FY 2019-20 through FY 2022-23. If our understanding of the SCO's calculation methodology is incorrect or you have questions, please let us know.

Last, we note that the SCO's misapplication of HSC § 34188(d) would improperly reduce excess ERAF allocations to offset the State's obligation to fund the Vehicle License Fee Adjustment Amount (VLFAA) owed to the counties and cities under RTC § 97.70. We believe the Department of Finance (DOF) favors this misapplication, regardless of its legal authority, because it subverts constitutional limitations against state raids of local government property tax revenues and the statutory mandate that the VLFAA not reduce excess ERAF allocations. See RTC 97.70(f). We believe that the SCO, as an impartial auditor, should apply state laws without regard to the DOF's flawed interpretation.

Thank you for your consideration of our position regarding the proposed audit finding.

Sincerely,

*Juan Raigoza*

Juan Raigoza  
San Mateo County Controller

**Attachment B—  
SCO Excess Educational Revenue Augmentation Fund  
Guidance**

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**BETTY T. YEE**  
California State Controller

February 16, 2021

**SUBJECT: Excess Educational Revenue Augmentation Fund Revenue Guidance**

Dear County Official:

The State Controller's Office is sending this notice to provide guidance to counties regarding the calculation and allocation of excess Educational Revenue Augmentation Fund (ERAF) revenues, in accordance with Revenue and Taxation Code (RTC) section 97.2(d)(2)(B). This guidance is effective beginning in fiscal year 2019-20.

**BACKGROUND**

The State Constitution requires that the proceeds of property taxes be allocated among the local government agencies in the county where the revenue is collected. Recipients of property tax revenue include cities, counties, special districts, K-12 school districts, and community college districts. Proposition 98 (approved by California voters in 1988) established a minimum funding requirement for school and community college districts, commonly known as the "minimum guarantee." The guaranteed funding level is met through a combination of revenues from the state General Fund and local property taxes. A set of formulas in the State Constitution determines the "minimum guarantee" calculation each year.

In 1992, the California State Legislature (Legislature) permanently redirected a portion of property tax revenue from cities, counties, and special districts into a county-held account known as ERAF. Revenue from ERAF is allocated to school and community college districts to offset the funding that these entities would otherwise receive from the state General Fund. In the mid-1990s, the Legislature enacted a law returning the portion of ERAF not needed for school and community colleges districts to cities, counties, and special districts in proportion to the amount of property taxes that the non-educational local government agencies contributed to ERAF. The returned ERAF funds are known as Excess ERAF.

In accordance with the state laws noted in the guidance below, beginning in fiscal year 2019-20, counties should complete the following steps when calculating and allocating Excess ERAF.

**GUIDANCE**

To calculate Excess ERAF pursuant to RTC sections 97.2(d) and 97.3(d):

1. Determine the amount of ERAF revenues<sup>1, 2</sup>
2. Reduce ERAF allocations to required funding levels or “ERAF Entitlement” for the following school entities/programs:
  - K-12 school districts<sup>3</sup> and the County Office of Education (non-excess tax school entities only); see RTC sections 97.2(d)(2) and 97.3(d)(2)
  - Community college districts (non-excess tax school entities only); see RTC sections 97.2(d)(3) and 97.3(d)(3)
  - Special Education; see RTC sections 97.2(d)(4)(B)(i)(II) and 97.3(d)(4)(B)(i)(II)
3. Remaining ERAF revenues are considered “Excess ERAF.” If Excess ERAF exists, distribute it as follows pursuant to RTC sections 97.2(d)(4)(B)(i)(III) and 97.3(d)(4)(B)(i)(III):
  - Determine the taxing entities that contributed to ERAF (e.g. cities, county, and special districts)
  - Allocate the Excess ERAF revenues among the affected taxing entities in proportion to the amounts of ad valorem property tax revenue otherwise required to be shifted from those local agencies to the county's ERAF for the relevant fiscal year.

If you have any questions regarding this letter, please contact the Local Government Policy Unit at [LocalGovPolicy@sco.ca.gov](mailto:LocalGovPolicy@sco.ca.gov).

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<sup>1</sup> Redevelopment Agencies' (RDA) residual revenues from the Redevelopment Property Tax Trust Fund and revenues from other RDA functions, such as asset sale proceeds, may not contribute to an increase in Excess ERAF pursuant to Health and Safety Code (HSC) section 34188(d). However, the distribution of pass-through payments is not subject to the limitations of HSC section 34188(d) and should not be excluded from the calculation of Excess ERAF.

<sup>2</sup> Former RDA revenues distributed to basic aid school districts pursuant to HSC section 34188(d) should not be included in the Excess ERAF calculation.

<sup>3</sup> Charter schools are not included in the definition of school districts for the calculation of Excess ERAF because they do not directly receive property tax revenue pursuant to RTC sections 97.2 and 97.3, but from the sponsoring district in accordance with Education Code section 47635.

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

**[www.sco.ca.gov](http://www.sco.ca.gov)**