

# STATE OF CALIFORNIA

Report to the California State Legislature

## PROPERTY TAX APPORTIONMENTS

*Calendar Year 2008*



JOHN CHIANG  
California State Controller

March 2009



**JOHN CHIANG**  
California State Controller

March 16, 2009

To the Members of the State Legislature  
and the People of California:

Re: Property Tax Apportionments Report to the Legislature for Calendar Year 2008

I am pleased to present the Property Tax Apportionments report for calendar year 2008. This report, prepared pursuant to Government Code section 12468, is intended to help mitigate problems associated with the counties' apportionment and allocation of property tax revenues.

The audits completed by the State Controller's Office in 2008 found the audited counties to be generally in compliance with the legal requirements for allocating property tax revenues. However, this report notes specific problem areas relative to individual counties.

I hope you find the report informative and useful for future policy decisions.

Sincerely,

*Original signed by*

**JOHN CHIANG**  
California State Controller

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# Executive Summary

This report summarizes the results of the State Controller's Office (SCO) audit of county property tax apportionments and allocations during the 2008 calendar year. After the passage of Proposition 13 in 1978, the California 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 agencies with a property tax base that would grow as assessed property values increase.

Property tax revenues that local governments receive each year are based on the amount received the prior year plus a share of the property tax growth within their boundaries. Property tax revenues are then allocated to local agencies and schools using prescribed formulas and methods defined in the Revenue and Taxation code. This methodology is commonly referred to as the AB 8 process or the AB 8 system. These methods have been further refined in subsequent laws passed by the Legislature.

The SCO's property tax audit program began on July 1, 1986, pursuant to Revenue and Taxation Code section 95.6 (now Government Code section 12468). The statute mandates that the SCO perform audits of the allocation and apportionment of property tax revenues by counties and make specific recommendations to counties concerning their property tax administration. The statute also specifies that the SCO is to prepare an annual report summarizing the results of its findings under this audit program.

We developed and implemented a comprehensive audit program that includes, but is not limited to, a detailed analysis of past and current requirements of property tax laws and an examination of property tax systems, processes, and records at the county level. Each audit encompasses an evaluation of a county's property tax apportionment methodology, allocation procedures, and compliance with applicable laws and regulations. We applied procedures considered necessary and appropriate to provide a basis for reporting on the areas examined.

Government Code section 12468 requires that audits be conducted periodically for each county according to a prescribed schedule based on county population. During 2008, the SCO completed audits of nine counties' property tax apportionment and allocation systems, processes, and records. The nine counties include El Dorado, Monterey, San Francisco, San Luis Obispo, Santa Cruz, Stanislaus, Tulare, Ventura, and Yuba.

As a part of our audit, we performed follow-up reviews to ensure that the counties properly addressed the findings identified in our previous audit reports. We are pleased to note that eight of the nine counties have successfully resolved the prior audit findings. In addition, we had no reportable audit findings or conditions in two of the nine counties audited during 2008.

Therefore, except for the findings and recommendations noted in this report, all nine counties audited during 2008 complied with the requirements for the apportionment and allocation of property tax revenues.

Our audit report findings for the remaining seven counties are broadly classified as follows:

- One county has not resolved a prior audit issue regarding an ERAF contribution.
- One county did not reconcile the AB 8 apportionment amounts to assessed values provided by the assessor.
- One county computed AB 8 factors incorrectly.
- One jurisdictional revenue exchange was computed incorrectly.
- One county did not properly apportion supplemental property taxes to K-12 schools.
- Two counties included redevelopment agencies in the supplemental apportionment factor computations.
- One county did not include the ERAF in the supplemental property tax apportionment computations.
- One county did not document supplemental property tax system costs.
- One county overstated their supplemental property tax system costs.
- One county redevelopment project base value did not reconcile to assessed parcel values.
- One county accepted a consolidated debt statement for a redevelopment agency.
- One county computed unitary property tax factors incorrectly.
- Five counties included the ERAF in the unitary property tax factor computations.
- One county computed ERAF contribution growth without adjusting for redevelopment increment losses.

There were two issues noted, that have pending legal action, that could have an impact on many counties:

- The first concerns the computation of administrative cost pro rata shares chargeable to local agencies and whether certain subvention revenues are to be included in the computation.
- The second concerns the computation of tax equity allocation amounts for low- and no-tax cities.

The counties generally agreed with most findings, except as noted in the findings of individual audits, and have stated that corrective action has been or will be taken to rectify the issues noted in our audit reports.

# Overview

## Introduction

This report presents the results of nine audits of county property tax apportionments and allocations completed by the State Controller's Office (SCO) in calendar year 2008. The following counties were audited: El Dorado, Monterey, San Francisco, San Luis Obispo, Santa Cruz, Stanislaus, Tulare, Ventura, and Yuba. Government Code section 12468 requires that such audits be conducted periodically for each county according to a prescribed schedule based on county population. The purpose of the audits is to help mitigate problems associated with property tax apportionment and allocation.

Except for the findings and recommendations noted in this report, all nine audited counties complied with the requirements for the apportionment and allocation of property tax revenues.

Two of the counties audited—San Luis Obispo and Santa Cruz—had no reportable findings.

## 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 agencies with a property tax base that would grow as assessed property values increase. These methods have been further refined in subsequent laws passed by the Legislature.

One key law was Assembly Bill 8, 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 governments receive each fiscal year are based on the amount received 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 process involved several steps, including the transfer of revenues from schools to local agencies and the development of the tax rate area annual tax increment growth factors (ATI factors), which determine the amount of property tax revenues allocated to each entity (local agency and school). The total amount allocated to each entity 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 has removed revenues generated by unitary and operating nonunitary property and pipelines from the AB 8 system. This revenue is now allocated and apportioned under a separate system.

Other legislation established an Educational Revenue Augmentation Fund (ERAF) in each county. Most local government agencies are required to transfer a portion of their property tax revenues to the ERAF. The fund is subsequently allocated and apportioned by the county auditor according to instructions received from the local superintendent of schools or 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 unpaid, 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 constitute sufficient “permanence” or have other intrinsic qualities to guarantee payment of taxes levied against it.
- *State-Assessed Roll*—Utility properties, composed of unitary and nonunitary value, assessed by the 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.

## **Audit Program**

The property tax audit program began on July 1, 1986, under Revenue and Taxation Code section 95.6 (now Gov. Code section 12468). The statute mandates that the State Controller periodically perform audits of the allocation and apportionment of property tax revenues by counties and make specific recommendations to counties concerning their property tax administration. However, the State Controller's authority to compel resolution of its audit findings is limited to those findings involving an overpayment of state funds.

Overpayment of state general fund money is recoverable by the State under several provisions of law (e.g., Education Code section 42237.7 et seq., and Government Code section 12420 et seq.). In addition, the State Controller has broad authority to recover overpayments made from the State Treasury. If an audit finds overpayment of state funds, and the state agency that made or authorized the payment does not seek repayment, the SCO is authorized to pursue recovery through a variety of means (e.g., Government Code sections 12418–12419.5). The specific remedy employed by the SCO depends on the facts and circumstances of each situation.

To carry out the mandated duties of the State Controller, the SCO developed and implemented a comprehensive audit program that includes, but is not limited to, a detailed analysis of past and current requirements of property tax laws and an examination of property tax records, processes, and systems at the county level.

These property tax apportionment audits have identified and aided in the correction of property tax underpayments to public schools. The underallocation of property taxes by individual counties to their public schools results in a corresponding overpayment of state funds to those schools by the same amount. This, in turn, causes public schools in other counties to receive less state funding because the total funds available are limited. Subsequent legislation forgave some counties for underpayments to schools without requiring repayment or assessment of penalties. However, the legislation required that the cause of the underallocations, as identified by the audits, be corrected.

## **Audit Scope**

Each audit encompasses an evaluation of a county's property tax apportionment methodology, allocation procedures, and compliance with applicable laws and regulations. The auditors used procedures considered necessary to provide a basis for reporting on the areas examined. In conducting the audits, the auditors focused on the following areas to determine if:

- The apportionment and allocation of the annual tax increment (ATI) was in accordance with Revenue and Taxation Code sections 96 through 96.5;
- The methodology for redevelopment agencies' base-year calculations and apportionment and allocation of the ATI was in accordance with Revenue and Taxation Code sections 96.4 and 96.6 and Health and Safety Code sections 33670 through 33679;
- The effect of jurisdictional changes on base-year tax revenues and the ATI was in accordance with Revenue and Taxation Code section 99;
- The apportionment and allocation of property tax revenues from supplemental assessments was in accordance with Revenue and Taxation Code sections 75.60 through 75.71;
- The apportionment and allocation of state-assessed unitary and operating nonunitary property taxes was in accordance with Revenue and Taxation Code section 100;
- The computation and apportionment of property tax revenues to low- and no-tax cities was in accordance with Revenue and Taxation Code section 98;
- The computation and collection of local jurisdictions' property tax administrative costs was in accordance with Revenue and Taxation Code sections 95.2 and 95.3;

- The computation and apportionment of property tax revenues to the ERAF was in accordance with Revenue and Taxation Code sections 97 through 97.3; and
- For eligible counties, the computation of the county credit against the county's ERAF shift was in accordance with Revenue and Taxation Code sections 97.3(a)(5) and 97.36.

## **Conclusion**

The property tax allocation and apportionment system is generally operating as intended. In the interest of efficiency and cost control for both the counties and the State, we submit the Summary of Findings and Recommendations in this report to assist in initiating changes that will help improve the system.

# Summary of Findings and Recommendations

## Introduction

Except for the findings and recommendations cited in this report, the audit reports issued in 2008 indicated that the counties complied with the legal requirements for the apportionment and allocation of property tax revenues. However, problem areas were identified and are described below. Recommendations to resolve the problems are included with the individual county findings.

## Unresolved Prior Audit Findings

As part of the audit process, auditors review the prior audit report to determine which issues, if any, require follow-up action. Auditors perform procedures to determine whether the county has resolved previously noted findings, and they restate in the current audit any unresolved prior audit findings.

One county has a continuing unresolved issue regarding an ERAF contribution amount for a city that transferred most of its property tax revenue to a fire district in exchange for fire protection services.

## Computation of Annual Tax Increment Factors

The Revenue and Taxation Code requires that each jurisdiction in a tax rate area (TRA) must be allocated property tax revenues in an amount equal to the property tax revenues allocated to it in the prior fiscal year. The difference between this amount and the total amount of property tax assessed in the current year is known as the annual tax increment (ATI). The computation of the annual tax increment results in a percentage that is used to allocate growth in assessed valuation to a county's local government jurisdictions and schools from the base year forward. Revenue and Taxation Code sections 96 through 96.5 prescribe this methodology. (Some exceptions to this allocation are contained in the Revenue and Taxation Code for specified TRAs.)

The total revenue available to apportion in one county could not be reconciled to assessed valuation for the county. The differences vary from year to year and do not appear to be reflective of actual value growth in any year. In another county the unitary tax revenue of redevelopment agencies is included in their AB 8 factor computation, resulting in an overstatement of their AB 8 factor with a corresponding understatement of factors for all other jurisdictions.

## Jurisdictional Changes

Revenue and Taxation Code section 99 prescribes the procedures the county must perform in order to make adjustments for the apportionment and allocation of property taxes resulting from changes in jurisdictional controls or changes in responsibilities of local government agencies and schools. The statute requires the county to prepare specific documentation that takes into consideration services and responsibilities.

One county computed revenue exchange amounts for jurisdictional changes using the effective change date rather than the effective roll year. In addition, the actual change within the county system often was delayed, resulting in additional incorrect distribution amounts for affected jurisdictions.

## **Supplemental Property Tax Apportionments**

When a revaluation of property occurs during the fiscal year due to changes in ownership or completion of new construction, supplemental taxes are usually levied on the property. Revenue and Taxation Code sections 75.70, 75.71, and 100.2 provide for the apportionment and allocation of these supplemental taxes.

One county did not apportion supplemental property taxes to its school district in fiscal year 2004-05 due to incorrect school information. The revenue was apportioned to all other taxing jurisdictions within the county. Three other counties also had errors in this area, two incorrectly included redevelopment agencies in the supplemental factor computation, and the other excluded the ERAF from the revenue computations.

## **Supplemental Property Tax Administrative Fees**

In addition to the fee allowed by Revenue and Taxation Code section 95.3 for the administration of the secured tax roll, Revenue and Taxation Code section 75.60 allows the charging of a fee for the administration of the supplemental tax roll. Once they adopt a method of identifying the actual administrative costs associated with the supplemental roll, counties are allowed to charge an administrative fee for supplemental property tax collections. This fee is not to exceed 5% of the supplemental taxes collected.

Two counties had errors in this area, one did not document the costs required to collect expenses and the other did not have sufficient costs to justify the amount collected.

## **Redevelopment Agencies**

The legal requirements for the apportionment and allocation of property tax to redevelopment agencies (RDA) are found in Revenue and Taxation Code sections 96.4 and 96.6 and Health and Safety Code sections 33670 through 33679. California community redevelopment law entitles a community redevelopment agency to all of the property tax revenue realized from growth in values since the redevelopment project's inception, with specified exceptions.

One county failed to reconcile the base value of a redevelopment project to the assessor's roll by parcel and also accepted an incorrect debt statement for the project.

## **Unitary and Operating Nonunitary Property Taxes**

The process for allocating and apportioning property taxes from certain railroad and utility companies functions through the unitary and operating nonunitary tax system employed by the State Board of Equalization. Unitary properties are those properties on which the State Board of Equalization "may apply 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 and railroads). 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." Revenue and Taxation Code section 100 prescribes the procedures counties must perform to allocate

unitary and operating nonunitary property taxes beginning in fiscal year (FY) 1988-89.

Five counties included the ERAF as a taxing jurisdiction within the unitary property tax apportionment computations.

## **Property Tax Administrative Fees**

Counties are allowed to collect from each appropriate jurisdiction, that jurisdiction's share of the cost of assessing, collecting, and apportioning property taxes. Revenue and Taxation Code section 95.3 prescribes the requirements for computing and allocating property tax administrative fees. The assessor, tax collector, and auditor generally incur county property tax administrative costs. The county is generally allowed to be reimbursed for these costs.

For FY 2004-05 and FY 2005-06, the county is prohibited by Revenue and Taxation Code section 97.75 from charging a fee for the services provided under Revenue and Taxation Code sections 97.68 and 97.70.

Prior to fiscal year 2006-07, counties could not impose a fee, charge, or other levy on a city, nor reduce a city's allocation of ad valorem property tax revenue, in reimbursement for services performed by the county under Revenue and Taxation Code sections 97.68 and 97.70. Pursuant to Revenue and Taxation Code section 97.75, beginning with fiscal year 2006-07, a county may impose a fee, charge, or other levy on a city for these services, but the fee, charge, or other levy can not exceed the actual cost of providing the services.

A legal challenge has arisen regarding the method some counties have used to impose the fee for the services provided under Revenue and Taxation Code sections 97.68 and 97.70. Though none of the counties included in this report have used this method to impose the fee, an observation is noted until the legal issues are resolved. After all legal challenges are resolved, this process will be reviewed again to determine if any adjustments are warranted and reports will be modified accordingly, including allowing the counties to modify their method of imposing the fee.

## **Educational Revenue Augmentation Fund (ERAF)**

The legal requirements for the local agency shift of property tax revenues to the ERAF are contained in Revenue and Taxation Code sections 97 through 97.3. Beginning in FY 1992-93, each local agency was required to shift an amount of property tax revenues to the ERAF using formulas prescribed by the Revenue and Taxation Code. The property tax revenues in the ERAF are subsequently allocated to schools and community colleges using factors supplied by the county superintendent of schools or chancellor of the California community colleges.

Since the passage of the ERAF shift requirements, the Legislature has enacted numerous bills that affect the shift requirements for various local government agencies. One bill was AB 1589 (Chapter 290, Statutes of 1997). This bill primarily addressed three areas related to the ERAF shift: (1) ERAF shift requirements for certain county fire funds for FY 1992-93 (Revenue and Taxation Code section 97.2(c)(4)(B)); (2) a

special provision for counties of the second class when computing the ERAF shift amount for county fire funds in FY 1993-94 (Revenue and Taxation Code section 97.3(c)(4)(A)(I)); and (3) ERAF shift requirements for county libraries for FY 1994-95 and subsequent years. After the passage of AB 1589, the State Controller requested advice from the California Attorney General regarding the application of Chapter 290, Statutes of 1997. The Attorney General responded in May 1998.

The Attorney General advised that the amendment to Revenue and Taxation Code section 97.2(c)(4)(B) significantly narrowed the scope of the exemption granted by the code section and was to be given retroactive application. The result is that many counties and special fire protection districts that were able to claim an exemption under the section as it formerly read lost the exemption retroactive to FY 1992-93. Consequently, those counties and special districts were required to shift additional funds to the county ERAF.

In response to the advice by the Attorney General, and noting the severe fiscal impact the loss of the exemption would have on local government agencies, the State Controller recommended that the Legislature consider restoring the exemption previously granted to fire protection districts and county fire funds that was eliminated as a result of Chapter 290, Statutes of 1997. Subsequently, the Legislature enacted AB 417 (Chapter 464, Statutes of 1999), restoring the exemption to fire districts.

One County improperly computed ERAF growth by not adjusting jurisdictions' growth factor computations to reflect revenue lost to redevelopment agencies.

## **Tax Equity Allocation**

Revenue and Taxation Code section 98 and the Guidelines for County Property Tax Administration Charges and No/Low Property Tax Cities Adjustment, provided by the County Accounting Standards and Procedures Committee, provide a formula for increasing the amount of property tax allocated to a city that had either no- or low-property tax revenues.

In the past, SCO auditors have accepted the tax equity allocation formula computations completed by the counties. However, a legal challenge has raised the possibility that the methods used may not be in compliance with the Revenue and Taxation Code. At this time, this is noted as an observation until the legal issues are addressed. After all legal challenges are resolved, these procedures will be reviewed again to determine if any adjustments or corrections are warranted and any reports will be modified accordingly.

# Findings of Individual County Audits

## Introduction

The findings and recommendations included below are presented as they were stated in the County Property Tax Apportionment and Allocation reports issued by the SCO in calendar year 2008. Unless otherwise indicated, the counties agreed with the findings and recommendations.

The findings and recommendations listed below are solely for the information and use of the California Legislature, the respective counties, the Department of Finance, and the SCO; they are not intended to be and should not be used by anyone other than those specified parties. This restriction is not intended to limit distribution of this report or the respective audit reports, which are a matter of public record.

## El Dorado County (July 1, 2002, through June 30, 2006)

### Follow-up on Prior Audit Findings

Findings noted in our prior audit, issued April 25, 2003, have been satisfactorily resolved by the county, except for the finding involving the ERAF contributions for the City of Placerville, as discussed in the Finding and Recommendation section of this report.

### FINDING— Educational Revenue Augmentation Fund (ERAF)

As noted in the prior audit report issued April 25, 2003, the county has not resolved the prior audit finding regarding its failure to pay the full ERAF amount due for the City of Placerville.

Requirements for the local agency shift of property tax revenues to the ERAF are generally found in Revenue and Taxation Code sections 97.1 through 97.3. Beginning in fiscal year (FY) 1992-93, each local agency is required to shift an amount of property tax revenues to the ERAF using formulas detailed in the code. The property tax revenues in the ERAF are subsequently allocated to the public schools using factors supplied by the county superintendent of schools.

For FY 1992-93, the ERAF shift amount for cities was generally determined by adding a per capita amount to a percentage of property tax revenues received by each city. The amount for counties was generally determined by adding a flat amount, adjusted for growth, to a per capita amount. The amount for special districts was generally determined by shifting the lesser of 10% of that district's total annual revenues as shown in the FY 1989-90 edition of the SCO's *Report on Financial Transactions Concerning Special Districts* or 40% of the FY 1991-92 property tax revenues received, adjusted for growth. Specified special districts were exempted from the shift.

For FY 1993-94, the ERAF shift for cities and counties was generally determined by:

- Reducing the FY 1992-93 ERAF shift by the FY 1992-93 per capita shift;
- Adjusting the result for growth; and

- Adding the result to a flat amount and a per capita amount determined by the Department of Finance, adjusted for growth.

The FY 1993-94 ERAF shift for special districts, other than fire districts, was generally determined by:

- Multiplying the property tax allocation for FY 1992-93, pre-ERAF, by the Special District Augmentation Fund (SDAF) factor for the district effective on June 15, 1993;
- Adjusting this amount by subtracting the FY 1992-93 shift to the ERAF;
- If the above amount is greater than zero, adjusting this amount for FY 1993-94 growth (zero is used for negative amounts); and
- Adding this amount to the FY 1992-93 ERAF shift, adjusting for growth.

For fire districts, the FY 1993-94 ERAF shift was generally determined by:

- Deducting the FY 1992-93 ERAF shift for the district from the FY 1992-93 property tax allocation;
- Multiplying the result by the SDAF factor for the district effective on June 13, 1993 (net current-year bailout equivalent);
- For a district governed by a board of supervisors, deducting the amount received from the SDAF in FY 1992-93 from the net current-year bailout equivalent; or, for an independent district, deducting the amount received from the SDAF and the difference between the net current-year bailout equivalent and the amount contributed to the SDAF from the net current-year bailout equivalent;
- Adjusting this amount for growth; and
- Adding this amount to the FY 1992-93 ERAF shift, adjusted for growth.

For fiscal years subsequent to FY 1993-94, the amounts determined are adjusted for growth annually to determine the ERAF shift amounts for that year.

#### Recommendation

The county should determine the past due amount, including growth, and begin collecting the proper amount of ERAF from the City of Placerville.

#### County's Response

Pursuant to my response for the audit for the six years ended June 30, 2002, we implemented the following beginning FY2003/04:

Absent an agreement between the City of Placerville and the State Controller's Office, the El Dorado County Auditor-Controller is prepared to execute the following. Effective FY2003/04, the Auditor-Controller will adjust the AB-8 factors for the annual amount shown on the draft audit

(adjusted for prior years' growth) for the purpose of shifting property tax revenues from the City of Placerville to the ERAF fund. Effective FY2003/04, the FY2002/03 AB-8 factors will be adjusted to reflect the annual ERAF shift (with growth). These factors will be used for any "prior year" property tax revenues during FY2003/04. Effective FY2003/04, the FY2003/04 AB-8 factor will be adjusted to reflect the annual ERAF shift. These factors will be used for any "current year" property tax revenues during FY2003/04. The process will then be repeated for future years.

Therefore, the only items remaining for discussion are FY1993/94 through FY2002/03. However, it is my understanding that SB1096 forgives issues prior to FY2001/02 and simply require a correction forward from that time. This office has corrected the issue forward starting in FY2003/04. This leaves only FY 2001/02 and FY2002/03 remaining. Because of growth, the FY2001/02 amount should be reflected as \$9,648 while the FY2002/03 should be reflected as \$11,335 for a total of \$20,983. This \$20,983 amount will be deducted from the City of Placerville in the FY2007/08, bringing the entire matter to a close.

#### SCO's Comment

As stated in the previous audit, it is our understanding that the City of Placerville agreed to transfer its share of property tax revenue to the El Dorado County Fire District and retain only a small factor for growth (ATI). The district agreed to assume the city's required ERAF shift amount related to percentage of property taxes received. There was no agreement on the city's required population shift amount to the ERAF. The net result is that the city agreed to transfer to the district property tax revenue that should have, by statute, been shifted to the ERAF. In return, the ERAF was underallocated property tax revenue in the amount of the city's required population shift amount.

The \$49,916 charged to the City of Placerville as noted on Schedule 1 (Allocated by County) and the additional \$20,983 proposed to be charged in FY 2007-08, only addresses part of the unpaid City of Placerville ERAF.

The remaining audit adjustment amount... is the 1993-94 ERAF responsibility. This amount still must be paid by the City of Placerville or the Fire District as part of the property tax exchange negotiated between the City and the Fire District.

The Auditor-Controller is responsible for the proper allocation and apportionment of property tax revenues.

The SCO recommends that the county act as a facilitator between the City of Placerville and El Dorado County Fire District to negotiate a plan to repay the net underallocated ERAF amount of \$507,134. . . .

Further, we have adjusted Schedule 1 [of the original report issued 01/31/08] to account for the effects of SB 1096. We will review the county's computation during the next audit.

## Monterey County (July 1, 2003, through June 30, 2006)

### Follow-up on Prior Audit Findings

The county has satisfactorily resolved the findings noted in our prior audit report, issued December 7, 2005.

### FINDING 1— Calculation and distribution of ATI

The AB 8 amounts could not be reconciled to the 1% of the Assessor’s certified assessed values. The totals between systems appear to differ for each fiscal year.

Requirements for the apportionment and allocation of the annual tax increment (ATI) are found in Revenue and Taxation Code sections 96 through 96.5. The annual increment of property tax, which is the change in assessed value from one year to the next, is allocated to TRAs on the basis of each TRA’s share of the incremental growth in assessed valuations. The tax increment is then multiplied by the jurisdiction’s annual tax increment apportionment factors for each TRA. These factors were developed in the 1979-80 base year and are adjusted for jurisdictional changes. The tax increment is then added to the tax computed for the prior fiscal year to develop the apportionment for the current fiscal year.

#### Recommendation

Once the annual tax increment is added to the AB 8 system, the county should reconcile the AB 8 balances to the Assessor’s certified values.

#### County’s Response

Beginning with the 2007-08 fiscal year, Monterey County will reconcile the AB 8 amounts with the Assessor’s certified assessed values.

### FINDING 2— Jurisdictional changes

The county computed revenue exchange amounts for jurisdictional changes in the AB 8 system using effective date values rather than effective roll year. In addition, the Assessor’s Office was untimely in moving the existing TRA Assessor’s Parcel Numbers (APN) to the resulting TRA’s.

The legal requirements for jurisdictional changes are found in Revenue and Taxation Code section 99. A jurisdictional change involves a change in organization or boundaries of local government agencies and school districts. 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 has increased receives additional annual tax increment, and the base property tax revenues are adjusted according to the negotiated agreements.

Recommendation

Unless wording to the contrary appears in the revenue exchange agreement, the revenue exchange calculation for the AB 8 system to be used by the county should be the approved roll year. The Assessor's Office must move existing TRA APNs to the resulting TRAs in a timely manner.

County's Response

Monterey County feels that the use of the effective date for computing revenue exchange is a County policy and should not be an audit finding. This policy has been in effect before the prior two State audits and the agency most affected is the County itself in that it gives up its own revenue.

SCO's Comment

In accordance with the Revenue and Taxation Code section 99, local government agencies are required to negotiate any exchange of base year property tax revenue and annual tax increment. The jurisdictional change agreement reviewed in this audit specifically states, "the following formulas for property tax base and increment distribution within Tax Rate Area 126-011 *after change of organization/reorganization.*" (Emphasis added). We understand this to mean the roll year approved by the State Board of Equalization and not the effective date of the resolution. The finding remains unchanged.

**FINDING 3—  
Supplemental  
property tax-  
administrative costs**

The county was reimbursed for actual supplemental administrative costs rather than the maximum allowed of 5% of supplemental revenue collection.

Revenue and Taxation Code section 75.60 allows a county to charge an administrative fee for supplemental property tax collections. This fee is not to exceed 5% of the supplemental property taxes collected.

Recommendation

Since the county includes supplemental administrative costs in the SB 2557 reimbursement system, the maximum allowed for supplemental administrative costs reimbursement in the supplemental system is a maximum of 5% of supplemental revenue collection. The county was over-reimbursed by \$117,645. This amount must be returned to all paying entities in the supplemental apportionment system.

County's Response

The \$117,465 was allocated back to the paying entities in 2006-07.

**FINDING 4—  
Redevelopment  
agencies**

The revenue base value for the City of Greenfield amended redevelopment agency (RDA) did not reconcile to the list of APNs provided by the Assessor's Office to the RDA.

The county accepted a consolidated Statement of Indebtedness (SOI) report from the City of Greenfield RDA and apportioned the increment without verifying the total debt.

Requirements for the apportionment and allocation of property tax to RDAs are found in Revenue and Taxation Code sections 96.4 and 96.5. California Community Redevelopment Law generally entitles a community redevelopment agency to all of the property tax revenues that are realized from growth in values since the redevelopment project's inception.

**Recommendation**

The County Assessor's Office must reconcile the mapped APNs for all jurisdictional changes to the values in the TRAs prior to shifting values. In addition, all resulting TRAs identified by the State Board of Equalization must be accounted for in the property tax systems. Furthermore, the shift of APNs must be done on a timely basis so that the County Controller's Office computes revenue correctly and in a timely manner.

The County Controller should not apportion property taxes impacted by jurisdictional changes unless assured that the value to be used is correct.

The County Controller should examine each RDA project's SOI and apportion property tax increments only for those projects that report debts. The purpose of the SOI is to determine the maximum amount of increment an RDA project can receive for each fiscal year.

**County's Response****Auditor-Controller**

Monterey County was unaware that an amendment to an existing RDA project required a separate SOI and will review them more carefully. Also, please see the attached memo from the Assessor.

**Assessor**

The Assessor's Office agrees with this recommendation and makes every effort to reconcile mapped APNs for all jurisdictional changes to values in the TRAs prior to shifting values. The Assessor's Office does not know why the AB 8 amounts did not reconcile to the assessor's assessed values. Although it is possible for a mistake to occur the assessor's office makes every effort possible to ensure that resulting TRAs identified by the State Board of Equalization are accounted for in the property tax system in a timely manner.

**FINDING 5—  
Unitary and operating  
nonunitary  
apportionment**

The county incorrectly computed the unitary and operating nonunitary apportionment factors in FY 2005-06. Computing and apportioning the excess of 102% of assessed valuation using AB 8 system factors unadjusted for, VLF revenues caused the error. In addition, for FY 2005-06, the County Assessor's Office did not account for pipeline AV in the correct TRA.

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 apply 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 and railroads). 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 unitary and operating nonunitary base year was established and formulas were developed to compute the distribution factors for the fiscal years that followed.

Recommendation

The county must recompute the apportionment factors by adjusting the FY 2004-05 AB 8 for VLF revenues and include pipeline AV in the correct TRA.

County's Response

Monterey County has made the VLF revenue adjustments to the unitary apportionment factors in 2006-07.

**FINDING 6—  
Educational Revenue  
Augmentation Fund  
(ERAF)**

The county computed the ERAF shift growth using gross AB 8 jurisdiction revenues. The jurisdiction revenues should be net of RDA gross increment.

Requirements for the local agency shift of property tax revenues to the ERAF are generally found in Revenue and Taxation Code sections 97.1 through 97.3. Beginning in FY 1992-93, each local agency was generally required to shift an amount of property tax revenues to the ERAF using formulas detailed in the code. The property tax revenues in the ERAF are subsequently allocated to the public schools using factors supplied by the county superintendent of schools.

For FY 1992-93, the ERAF shift amount for cities was generally determined by adding a per capita amount to a percentage of property tax revenues received by each city. The amount for counties was generally determined by adding a flat amount, adjusted for growth, to a per capita amount. The amount for special districts was generally determined by

shifting the lesser of 10% of that district's total annual revenues as shown in the FY 1989-90 edition of the State Controller's Report on Financial Transactions Concerning Special Districts or 40% of the FY 1991-92 property tax revenues received, adjusted for growth. Specified special districts were exempted from the shift.

For FY 1993-94, the ERAF shift for cities and counties was generally determined by:

- Reducing the FY 1992-93 ERAF shift by the FY 1992-93 per capita shift;
- Adjusting the result for growth; and
- Adding the result to a flat amount and a per capita amount determined by the Department of Finance, adjusted for growth.

The FY 1993-94 ERAF shift for special districts, other than fire districts, was generally determined by:

- Multiplying the property tax allocation for FY 1992-93, pre-ERAF, by the Special District Augmentation Fund (SDAF) factor for the district effective on June 15, 1993;
- Adjusting this amount by subtracting the FY 1992-93 shift to the ERAF;
- If the above amount is greater than zero, adjusting this amount for FY 1993-94 growth (zero is used for negative amounts); and
- Adding this amount to the FY 1992-93 ERAF shift, adjusting for growth.

For fire districts, the FY 1993-94 ERAF shift was generally determined by:

- Deducting the FY 1992-93 ERAF shift for the district from the FY 1992-93 property tax allocation;
- Multiplying the result by the SDAF factor for the district effective on June 13, 1993 (net current-year bailout equivalent);
- For a district governed by a board of supervisors, deducting the amount received from the SDAF in FY 1992-93 from the net current-year bailout equivalent; or, for an independent district, deducting the amount received from the SDAF and the difference between the net current-year bailout equivalent and the amount contributed to the SDAF from the net current-year bailout equivalent;
- Adjusting this amount for growth; and
- Adding this amount to the FY 1992-93 ERAF shift, adjusted for growth.

For fiscal years subsequent to FY 1993-94, the amounts determined are adjusted for growth annually to determine the ERAF shift amounts for that year.

### Recommendation

The county must revise the AB 8 system by removing RDA gross increments from participating jurisdictions' prior revenues before calculating the ERAF shift growth. To properly correct the system, the revision should begin with the 1993-94 fiscal year.

### County's Response

Monterey County will adjust the ERAF shift growth and go forward starting in 2007-08.

## **City and County of San Francisco (July 1, 2004, through June 30, 2007)**

### **Follow-up on Prior Audit Findings**

Our prior audit report, issued October 6, 2006, included no findings related to the apportionment and allocation of property tax revenues by the county.

### **FINDING 1— Supplemental property tax**

The county did not apportion supplemental property taxes to the San Francisco Unified School District (SFUSD) in fiscal year (FY) 2004-05 because the information available to the county indicated that the average daily attendance (ADA) was zero for that year. The county reapportioned all supplemental property taxes that would have gone to the district to all other taxing jurisdictions proportionately.

The county subsequently learned that the zero ADA was incorrect and the revenue should have been apportioned to the district. In addition, no statutory provision permits the reallocation of supplemental property taxes in situations of this type.

The legal requirements for supplemental roll property tax apportionment and allocation are found in Revenue and Taxation Code sections 75.60 through 75.71 and 100.2. When there is a change in assessed property value due to changes in ownership or completion of new construction, the property owner is charged a supplemental property tax. This process enables the counties to retroactively tax property for the period when changes in ownership or completion of new construction occurred, rather than at the time the secured roll is developed.

### Recommendation

The county must recover the revenue incorrectly distributed to non-school entities and distribute it to the district.

### City and County's Response

The county concurs with this finding and has allocated the supplemental property taxes to San Francisco Unified School District. Please refer to attached supporting document.

**FINDING 2—  
Unitary and operating  
nonunitary  
apportionment**

The county included the Educational Revenue Augmentation Fund (ERAF) as a taxing entity in the unitary apportionment process. The ERAF is a fund, not a taxing entity, and therefore should not be included in the unitary apportionment process.

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 and railroads). 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 unitary amounts paid to the ERAF for this audit period may be recovered from the ERAF and distributed to the local agencies from which it was diverted.

City and County’s Response

The county agrees with this finding. Adjustments were made to exclude ERAF while the field audit was still in process and will continue to do this in future unitary apportionment.

**San Luis Obispo County (July 1, 2004, through June 30, 2007)**

**Follow-up on Prior  
Audit Findings**

Our prior audit report, issued October 5, 2005, included no findings related to the apportionment and allocation of property tax revenues by the county.

**OBSERVATION**

Except for the possible effects, if any, of the matter discussed below, our audit disclosed that San Luis Obispo County complied with California statutes for the allocation and apportionment of property tax revenues for the period audited.

Prior to fiscal year (FY) 2006-07, counties could not impose a fee, charge, or other levy on a city, nor reduce a city’s allocation of ad valorem property tax revenue, in reimbursement for the services performed by the county under Revenue and Taxation Code sections 97.68 and 97.70. Pursuant to Revenue and Taxation Code section 97.75, beginning with FY 2006-07, a county may impose a fee, charge, or levy

on a city for these services, but the fee, charge, or other levy cannot exceed the actual cost of providing the services.

A legal challenge has arisen regarding the method a county has used to impose the fee for the services provided under Revenue and Taxation Code sections 97.68 and 97.70. San Luis Obispo County has used a different method to impose the fee. At this time, this finding does not warrant a reportable condition, but is only an observation until the legal issues are resolved. After all legal challenges are resolved, this process will be reviewed again to determine if any adjustments or corrections are warranted and the report will be modified accordingly.

## **Santa Cruz County (July 1, 2001, through June 30, 2006)**

### **Follow-up on Prior Audit Findings**

Our prior audit report, issued May 2002, included no findings related to the apportionment and allocation of property tax revenues by the county.

### **OBSERVATION**

Except for the effects, if any, of the matter discussed below, our audit disclosed that the county complied with California statutes for the allocation and apportionment of property tax revenues for the period audited.

Tax Equity Allocation (TEA): In the past, SCO auditors have accepted the County's TEA formula computation. However, the legal challenge in the County has raised the possibility that it may not be in compliance with the Revenue and Taxation Code. At this time, this finding does not warrant a reportable condition, but is only an observation until the legal issues are resolved. After all legal challenges are resolved, this process will be reviewed again to determine if any adjustments or corrections are warranted and the report will be modified accordingly.

## **Stanislaus County (July 1, 2003, through June 30, 2006)**

### **Follow-up on Prior Audit Findings**

The county has satisfactorily resolved the findings noted in our prior audit report, issued September 2005.

### **FINDING— Unitary and operating nonunitary apportionment**

The county complied with California statutes, except that it included the Educational Revenue Augmentation Fund (ERAF) in the unitary and operating nonunitary apportionment process.

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 and railroads). 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 remove the ERAF from the unitary and operating nonunitary process and distribute the revenue to the agencies contributing to the ERAF.

### County's Response

Revenue & Taxation Code Section 100 governs the distribution of unitary and operating nonunitary taxes. This section as evidenced below, defines the distribution of taxes to “taxing jurisdictions”

(3) If the amount of property tax revenue available for allocation to all taxing jurisdictions in the current fiscal year from unitary and operating nonunitary property, exclusive of revenue attributable to qualified property under Section 100.95 and levies for debt service, exceeds 102 percent of the property tax revenue received by all taxing jurisdictions from all unitary and operating nonunitary property in the prior fiscal year, exclusive of revenue attributable to qualified property under Section 100.95 and levies for debt service, **the amount of revenue in excess of 102 percent shall be allocated to all taxing jurisdictions in the county by a ratio determined by dividing each taxing jurisdiction's share of the county's total ad valorem tax levies for the secured roll for the prior year**, exclusive of levies for qualified property under Section 100.95 and levies for debt service, by the county's total ad valorem tax levies for the secured roll for the prior year, exclusive of levies for qualified property under Section 100.95 and levies for debt service.

The underlying foundation for the State Controller's opinion seems to be that ERAF is not a taxing jurisdiction. Unfortunately, in the chapter that governs the distribution of taxes from the unitary and operating nonunitary roll, the term “taxing jurisdiction” is not clearly defined. The general construction for the chapter is found in section 95 of the Revenue and Taxation code. That section (95 (b)) does define the term “Jurisdiction” as “a local agency, school district, community college district, or county superintendent of schools. . .” We also find in section 100 (e) (3) that “Taxing Jurisdiction’ includes a redevelopment agency”. The State Controller has opined that ERAF is not entitled to distribution of unitary and operating nonunitary taxes because linking R&T 100 (e) (3) with R&T 95 (b) eliminates the possibility of ERAF meeting the criteria of being a taxing jurisdiction.

However, R&T 100 also calls for the distribution of unitary and operating nonunitary taxes attributable to any growth over 2% in any given year to be apportioned using the prior year's allocation formula for the secured roll. The allocation of taxes for the Secured Roll is found in R&T 95 et seq. which clearly provides for apportionment of

taxes to ERAF and defines ERAF as a school entity eligible to receive tax distributions R&T 95 (f):

(f) “School entities” means school districts, community college districts, the Educational Revenue Augmentation Fund, and county superintendents of schools.

Given the provision for inclusion of ERAF as part of the secured roll tax allocation formula, it also would be reasonable to conclude that, under the provisions of R&T 100 (c) (3), that ERAF should be a part of the distribution of unitary and operating nonunitary taxes the first year, and each year thereafter, that the assessed valuation of unitary and operating nonunitary properties increase by a magnitude of greater than 2%.

Given these two reasonable, albeit contradictory positions, as to the inclusion of ERAF in unitary and operating nonunitary tax distributions, we need to see what the legislative intent was. R&T 100 was added by Stats. 1997, c.1167. The historical and statutory notes state, “It is the intent of the Legislature in enacting this act only to clarify and reorganize those statutes with respect to the allocation of property tax revenues, and to eliminate portions of those statutes that have been fully implemented or are no longer applicable. ***This act shall not be construed to invalidate or otherwise affect any otherwise proper action taken under the authority of Chapter 6 (commencing with Section 95) of Part 0.5 of Division 1 of the Revenue and Taxation Code*** prior to the operative date of this act, or any requirements of that chapter as the chapter read prior to the operative date of this act.

In our opinion, the intent of the legislature was that the allocation of unitary and operating nonunitary tax revenues attributable to the increase over 2% should strictly follow the allocation practices and procedures for the Secured Roll found in R&T 95 et seq., that includes ERAF as part of the distribution of taxes. In addition, we find it difficult to believe the State intentionally enacted legislation that would negatively impact State revenue by excluding ERAF from the distribution process. We therefore disagree with this finding and will continue with our current practice of including ERAF as part of the distribution of unitary and operating nonunitary taxes.

#### SCO’s Comment

The ERAF is a fund—an accounting entity, not a taxing jurisdiction—and with respect to the allocation and apportionment of unitary and operating nonunitary taxes, the Legislature has not defined the ERAF as a taxing jurisdiction.

The county points out that Revenue and Taxation (R&T) Code section 95(b) defines a jurisdiction as a “local agency, school district, community college district, or county superintendent of schools. . . .” The county further points out that R&T Code section 95(f) includes the ERAF in the definition of school entities. “School entities” means school districts, community college districts, the Educational Revenue Augmentation Fund, and county superintendent of schools.” However, the definition of “jurisdiction” does not include the ERAF but does include all defined school entities *except* the ERAF. Defining the ERAF as a school entity does not make it a jurisdiction.

In addition, the county points out that R&T Code section 100(e)(3) includes a redevelopment agency as a taxing jurisdiction. The county is trying to show that the Legislature, in enacting the section, is including a non-taxing entity in the definition of a taxing jurisdiction. We concur. This demonstrates that the Legislature can include non-taxing entities in the definition of taxing jurisdiction. In this case, it omitted the ERAF from the definition of taxing jurisdiction.

The finding remains as written.

## **Tulare County (July 1, 2003, through June 30, 2006)**

### **Follow-up on Prior Audit Findings**

Our prior audit report, issued August 4, 2004, had no findings related to the apportionment and allocation of property tax revenues by the county.

### **FINDING 1— Incorrect calculation of the AB 8 factors**

The county computed its AB 8 apportionment system in error because it included redevelopment agencies' unitary and operating nonunitary revenues when computing apportionment factors. The error caused an overstatement of each redevelopment agency's revenues and an understatement of revenues for other agencies within the redevelopment projects. The error also impacted other property tax apportionment systems and subsystems.

Requirements for the apportionment and allocation of the annual tax increment (ATI) are found in Revenue and Taxation Code sections 96 through 96.5. The annual increment of property tax, which is the change in assessed value from one year to the next, is allocated to tax rate areas (TRAs) on the basis of each TRA's share of the incremental growth in assessed valuations. The tax increment is then multiplied by the jurisdiction's annual tax increment apportionment factors for each TRA. These factors were developed in the 1979-80 base year and are adjusted for jurisdictional changes. The tax increment is then added to the tax computed for the prior fiscal year to develop the apportionment for the current fiscal year.

#### Recommendation

The county should review the AB 8 process and identify the initial fiscal year in which the error occurred, and then correct the AB 8 factors from that fiscal year forward. In addition, the county should correct all systems impacted by the AB 8 error.

#### County's Response

The recommended changes have been completed.

**FINDING 2—  
Redevelopment agencies  
included in supplemental  
property tax**

The county included redevelopment agencies in the supplemental property tax apportionment process.

The legal requirements for supplemental roll property tax apportionment and allocation are found in Revenue and Taxation Code sections 75.60 through 75.71 and 100.2. When there is a change in assessed property value due to changes in ownership or completion of new construction, the property owner is charged a supplemental property tax. This process enables the counties to retroactively tax property for the period when changes in ownership or completion of new construction occurred, rather than at the time the secured roll is developed.

Recommendation

The county should exclude redevelopment projects from the supplemental property tax apportionment process, and should adjust accordingly the apportionment factors for other agencies.

County's Response

The recommended changes have been completed.

**FINDING 3—  
Supplemental property  
tax—administrative  
costs not documented**

The county did not document supplemental property tax administrative costs before collecting the allowable fee.

Revenue and Taxation Code section 75.60 allows a county to charge an administrative fee for supplemental property tax collections. This fee is not to exceed 5% of the supplemental property taxes collected.

Recommendation

The county should document supplemental property tax administrative costs before collecting the allowable fee.

County's Response

Supporting documentation for supplemental property tax administrative costs are on file in a manner that has passed all previous audits by the State Controller. We are implementing improved documentation and procedures for these costs as recommended.

**FINDING 4—  
ERAF included in unitary  
and operating nonunitary  
apportionment**

The county included the Educational Revenue Augmentation Fund (ERAF) in the unitary and operating nonunitary apportionment process when unitary and operating nonunitary assessed value grew by more than 2% over the preceding year. The ERAF is not a taxing jurisdiction and is not eligible to be included in the unitary and operating nonunitary apportionment process.

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 apply 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 and railroads). 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 unitary and operating nonunitary base year was established and formulas were developed to compute the distribution factors for the fiscal years that followed.

#### Recommendation

The county should exclude the ERAF from the unitary and operating nonunitary apportionment process and adjust apportionment factors accordingly.

#### County’s Response

This issue is an ongoing debate statewide as the law is inconsistent. In May of 2007 the State Auditor’s Association recommended all County Auditors make no changes and stay consistent in following the Property Tax Manager’s Reference Manual. We will follow this recommendation until the issue is resolved by the State Legislature and there are clear, consistent codes and guidelines.

#### SCO’s Comment

The ERAF is a fund—not a taxing jurisdiction—and should not be included in the unitary and operating nonunitary process. The finding remains as written.

## **Ventura County (July 1, 2003, through June 30, 2006)**

### **Follow-up on Prior Audit Findings**

The county has satisfactorily resolved the findings noted in our prior audit report, issued in July 2005.

### **FINDING— Supplemental property tax**

Ventura County excluded the Educational Revenue Augmentation Fund (ERAF) from Supplemental Apportionments.

The legal requirements for supplemental roll property tax apportionment and allocation are found in Revenue and Taxation Code sections 75.60 through 75.71 and 100.2. When there is a change in assessed property value due to changes in ownership or completion of new construction, the property owner is charged a supplemental property tax. This process enables the counties to retroactively tax property for the period when changes in ownership or completion of new construction occurred, rather than at the time the secured roll is developed.

### Recommendation

The county must include the ERAF in future supplemental apportionments. Additionally, the county must pay \$9,203,208 into the ERAF for FY 2003-04 through FY 2005-06.

### County's Response

As directed by your letter, which we received December 20, 2007, we are responding to the audit finding that asserts our County is improperly excluding the Educational Revenue Augmentation Fund (ERAF) from Supplemental Roll apportionments. In addition, although it is not included as an audit finding, we are addressing the audit's assertion that ERAF should be excluded from the Unitary Roll apportionment process.

We disagree with the finding that the County is improperly excluding ERAF from the Supplemental Roll apportionments because the finding is not supported by law or any authoritative pronouncement. During the exit conference, the auditor made it clear that this position was not based on Revenue and Taxation (R&T) code or any other applicable law, but that he was basing his finding solely upon an unpublished State Attorney General's opinion letter, a copy of which was not provided to use for our review.

We further disagree with the finding because the audit report is attempting to apply the principles for apportioning the Equalized Roll (Secured, Unsecured and State Utility Rolls), which is governed by R&T code 95, et seq., to the apportionment of the Supplemental Roll, which is governed by R&T code 75, et seq. R&T codes 75 through 75.80, as updated by R&T code 100.2 to include tax years after 1985-86, clearly identify the Supplemental Roll as a roll that is separate from the Equalized Roll. In R&T code 75.70, ERAF is not referenced as a "school entity" that is to receive Supplemental Roll apportionments. According to the code, "all elementary, high school, and unified school districts within the county," are to participate in the Supplemental Roll apportionments. R&T code 75.70 further specified that the allocation of property tax revenues to these entities is to occur "without respect to the allocation of property tax revenues pursuant to Chapter 6 (commencing with Section 95)," which governs the apportionment of the Equalized Roll and does include ERAF as a "school entity," as defined by R&T code 95(f) [school districts, community college districts, the Educational Revenue Augmentation Fund, and county superintendents of schools].

Given R&T code 75.80 identified the specific entities that participate in the Supplemental Roll apportionments, and the code does not reference school entities as defined under R&T code 95(f), which does include ERAF as a participating school entity, the County of Ventura is correct in its exclusion of ERAF from Supplemental Roll apportionments.

Two additional items should be noted regarding the Supplemental ERAF apportionment finding: 1) In previous audits, two other State Controller auditors agreed that we are in compliance with applicable law by excluding ERAF from Supplemental Roll apportionments. 2) Other than to reference R&T code 96(c)(3), which limits the cumulative amount of the proposed adjustment, the audit report does not provide specifics on how the auditor developed the amounts of the desired ERAF adjustment for the three years under review. Since we

are not able to verify the calculations, we cannot comment on their validity.

During the same exit conference where the Supplemental ERAF finding was discussed, the auditor raised the issue of excluding ERAF from the Unitary Roll apportionment process. He referenced the same, unpublished State Attorney's General's opinion letter as the basis for his opinion that ERAF should be excluded from the Unitary Roll. Our application of law to include all taxing jurisdictions, including ERAF, in the Unitary Roll apportionment for the three years under review is correct and is fully supported by clarification to R&T code 100.95(a)(3)(A)(i) for the 2007-08 fiscal year. R&T code 100.95(a)(3)(A)(i) states:

“School entities, as defined in subdivision (f) of section 95 [school districts, community college districts, the Educational Revenue Augmentation Fund, and county superintendents of schools], shall be allocated an amount equivalent to the same percentage the school entities received in the prior fiscal year from the property tax revenues paid by the utility in the county in which the qualified property is located.”

Since the statement in the audit report related to ERAF in the Unitary Roll is not a finding, and specific Revenue and Taxation code supports our current methodology for apportioning the Unitary Roll, we will not make any modifications to our processes at this time.

#### SCO's Comment

Revenue and Taxation (R&T) Code section 75.70(c) provides that supplemental property tax allocations to counties, cities, and special districts are to be calculated on the basis of each entity's property tax apportionment factor determined “pursuant to section 97.5” (now section 96.2) (i.e., in accordance with section 96.2).

Supplemental property tax revenues are not included in the computation of property tax apportionment factors. However, the applicable law makes it clear that the allocation of such revenues is to be made on the basis of, and in accordance with, the apportionment factors.

After the supplemental property tax laws were enacted, section 97.5 (now section 96.2) was amended by Chapter 448, Statutes of 1984, adding as subdivision (f) the identical provision that is now in subdivision (c) of section 96.1 (i.e., supplemental tax revenues are not to be included for purposes of the section). But subdivision (f) was in effect for less than two months (July 16 to September 10, 1984). It was deleted from section 97.5 by Chapter 946, Statutes of 1984, which substituted the following as subdivision (h) of section 97.5:

(h) Supplemental property tax revenues for 1985-86 and each year thereafter, generated by Sections 75 to 75.80, inclusive, shall be apportioned using the property tax apportionment factors for the current year.

Subdivision (h) remained in section 97.5 until reorganization of the property tax allocation statutes (Chapter 1167, Statutes of 1994). Former section 97.5 became section 96.2, and the above quoted subdivision (h)

became section 100.2. The primary purpose of Chapter 1167 was to “clarify and reorganize” the property tax allocation code provisions. The Legislature did not intend any substantive change in transferring subdivision (h) to section 100.2. This provision was intended to have the same application it had over the previous ten years. The supplemental tax revenues are to be allocated by application of the current year’s apportionment factor.

However, the pertinent ERAF sections (section 97, et seq.) specifically provide that “Notwithstanding any other provision of this chapter, the computations and allocations made by each county pursuant to section 96.1 or its predecessor section . . . shall be modified. . . .” This supersedes the pre-ERAF apportionment factor formula.

Section 96.1 is modified by law. There is no unmodified section 96.1, nor any statute that provides for allocation of property tax revenues based on a pre-modified section 96.1 apportionment factor. Section 75.70(c) specifies that supplemental revenues are to be distributed using apportionment factors “pursuant” to section 96.2—that is, factors developed on the basis of a modified section 96.1.

In this regard, sections 97.2(d)(5), 98.2(e)(3), and 97.3(d)(5) specify that amounts allocated from the ERAF “shall be deemed property tax revenue allocated to the Educational Revenue Augmentation Fund in the prior fiscal year.” Additionally, section 95(f) defines “school entities” as including the ERAF. As a result of these sections, the ERAF is, in effect, treated the same as a school district with its own property tax apportionment factor. This is consistent with and supports the above interpretation that apportionment factors must be determined for all entities on the basis of a modified section 96.1—that is, after deduction of the ERAF shifts moneys.

It should also be noted that Chapter D-6 of the *California Property Tax Managers’ Reference Manual* includes the ERAF as an entity to receive supplemental property taxes.

The county has also addressed the exclusion of the ERAF from the unitary and operating nonunitary apportionment process.

The ERAF is a fund—an accounting entity, not a taxing jurisdiction—and with respect to the allocation and apportionment of unitary and operating nonunitary taxes, the Legislature has not defined it as a taxing jurisdiction.

R&T Code section 95(b) defines a jurisdiction as a “local agency, school district, community college district, or county superintendent of schools. . . .” R&T Code section 95(f) includes the ERAF in the definition of school entities. It states “‘School entities’ means school districts, community college districts, the Educational Revenue Augmentation Fund, and county superintendent of schools.” It is clear that the definition of jurisdiction does not include the ERAF but does include all defined school entities except the ERAF. Defining the ERAF as a school entity does not make it a jurisdiction.

R&T Code section 100(e)(3) includes a redevelopment agency as a taxing jurisdiction, demonstrating that the Legislature knows how to include non-taxing entities in the definition of taxing jurisdiction if it so desires. In this case, it omitted the ERAF from the definition of taxing jurisdiction.

The county has stated that its application of law “to include all taxing jurisdictions, including ERAF, in the Unitary Roll apportionment . . . is correct and is fully supported [sic] by clarification to R&T code 100.95(a)(3)(A)(i) for the 2007-08 fiscal year.” The county then quotes the section as included in its response above.

However, the county did not note that R&T Code section 100.95 is concerned with certain “qualified property” and not the unitary and operating nonunitary property of R&T Code section 100. R&T Code section 100.95(c)(1) states:

“Qualified property” means all plant and associated equipment, including substation facilities and fee-owned land and easements, placed in service by the public utility on or after January 1, 2007, and related to the following:

- (A) Electrical substation facilities that meet either of the following conditions:
  - (i) The high-side voltage of the facility’s transformer is 50,000 volts or more.
  - (ii) The substation facilities are operated at 50,000 volts or more.
- (B) Electric generation facilities that have a nameplate generating capacity of 50 megawatts or more.
- (C) Electrical transmission line facilities of 200,000 volts or more.

The finding remains as written. In addition, the county should exclude the ERAF from the unitary and operating nonunitary apportionment process.

## **Yuba County (July 1, 2001, through June 30, 2006)**

### **Follow-up on Prior Audit Findings**

The county has satisfactorily resolved the findings noted in our prior audit report, issued August 1, 2002.

### **FINDING 1— Supplemental property tax**

The county has included redevelopment agencies in the factors used to apportion supplemental property taxes.

The legal requirements for supplemental roll property tax apportionment and allocation are found in Revenue and Taxation Code sections 75.60 through 75.71 and 100.2. When there is a change in assessed property value due to changes in ownership or completion of new construction, the property owner is charged a supplemental property tax. This process enables the counties to retroactively tax property for the period when changes in ownership or completion of new construction occurred, rather than at the time the secured roll is developed.

Recommendation

Redevelopment agencies must be removed from the supplemental apportionment factor process. Redevelopment agencies receive all supplemental taxes that are generated within their boundaries.

County's Response

We agree with this finding and have with the helpful oversight of Mr. Rose corrected our methodology in apportioning of supplemental property taxes.

**FINDING 2—  
Unitary and operating  
nonunitary  
apportionment**

The county has included the Educational Revenue Argumentation Fund (ERAF) as a taxing jurisdiction within the unitary and operating nonunitary apportionment process.

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 and railroads). 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 remove the ERAF from the unitary and operating nonunitary apportionment process and spread the revenue proportionately to contributing agencies.

County's Response

We disagree with this finding and will continue to follow the State of California Auditors Association approved methodology of apportionment of unitary and operating nonunitary property taxes by including ERAF in our computations.

SCO's Comment

The ERAF is a fund—an accounting entity, not a taxing entity. Unitary and operating nonunitary revenues are allocated to taxing entities. The finding remains as written.

*Copies of the audit reports referred to in this report may be obtained by contacting:*

**State Controller's Office  
Division of Audits  
Post Office Box 942850  
Sacramento, CA 94250-5874**

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