

# STATE OF CALIFORNIA

Report to the California State Legislature

## PROPERTY TAX APPORTIONMENTS

*Calendar Year 2011*



**JOHN CHIANG**  
California State Controller

February 2012



**JOHN CHIANG**  
California State Controller

February 28, 2012

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

Re: Property Tax Apportionments Report to the Legislature for Calendar Year 2011

I am pleased to present the Property Tax Apportionments report for calendar year 2011. 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 2011 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 2011 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. The method has 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 2011, the SCO completed audits of eight counties' property tax apportionment and allocation systems, processes, and records. The eight counties are Alpine, Colusa, Inyo, Nevada, Sacramento, San Joaquin, Shasta, and Solano counties.

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 seven of the eight counties have successfully resolved the prior audit findings and that one of the eight counties had no prior audit findings.

Therefore, except for the findings and recommendations noted in this report, the processes used by the eight counties audited during 2011 appear to comply with the requirements for the apportionment and allocation of property tax revenues.

Our audit report findings are broadly classified as follows:

#### Prior Audits

- Findings noted in prior audits have been satisfactorily resolved by the counties.

#### Current Audits

- One county included the airplane assessed value levy in the RDA tax increment adjustment.
- Seven counties included the ERAF, a non-taxing jurisdiction, in the unitary and operating nonunitary apportionment calculations.
- Three counties miscalculated the annual tax increment amounts and did not carry forward some of the base revenues from the prior year, causing the current year's revenues, growth percentages, and AB 8 apportionment factors computations to be incorrect.
- For one county, the errors in the AB 8 system caused the factors and allocations in the supplemental property tax system to be incorrect beginning with FY 2003-04.
- For one county, the errors in the AB 8 system and the failure to carry forward some of the agencies' ERAF shift amounts from the prior year caused ERAF shift amounts for all fiscal years to be incorrect.
- For one county, the FY 2005-06 base revenue ERAF shift did not carry forward to FY 2006-07.

We noted two pending legal issues that could have an impact on many counties:

- The first issue 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 issue 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 eight audits of county property tax apportionments and allocations completed by the State Controller's Office (SCO) in calendar year 2011. The following counties were audited: Alpine, Colusa, Inyo, Nevada, Sacramento, San Joaquin, Shasta, and Solano counties. 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, the eight audited counties complied with the requirements for the apportionment and allocation of property tax revenues.

## 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 (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 revenue 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 Government 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. 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 (according to Government Code sections 12418–12419.5). The specific remedy employed by the SCO depends on the facts and circumstances of each situation.

The SCO developed and implemented a comprehensive audit program to carry out the mandated duties. The comprehensive audit program 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 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
- The payment by ERAF was made in compliance with Revenue and Taxation Code section 97.68, commonly known as the "Triple Flip," and section 97.70, commonly known as the "VLF Swap."

## Pending Litigation

### Property Tax Administration Fees

A dispute has arisen between the counties and the cities regarding the application of Revenue and Taxation Code section 95.3 relating to the computation of Property Tax Administration Fees (PTAF). The counties generally contend that distribution factors for purposes of distributing PTAF to taxing agencies should be computed including amounts received by cities under Revenue and Taxation Code section 97.68, commonly known as the "Triple Flip," and section 97.70, commonly known as the "VLF Swap." The cities generally believe that the Triple Flip and the VLF (Vehicle License Fee) Swap should be excluded from the computation.

We are aware of two legal actions that have been filed on this issue.

In the first action, 47 cities (petitioners) in Los Angeles County filed suit against the county (respondent). In the summary of facts included in the decision, a retired judge acting as referee, noted:

The financial consequences of RESPONDENTS' method of calculating the PTAF for PETITIONERS are that PETITIONERS' PTAF fees were, collectively, over \$4.8 million in fiscal year 2006-07 and \$5.3 million in fiscal year 2007-08, more than such fees would have been had the Triple Flip and the VLF Swap additional property tax revenues not been included in PETITIONERS' property tax share used for apportioning PTAF, [sic] the County's actual cost of incremental tax allocation/distribution duties required by the Triple Flip and VLF Swap was approximately \$35,000 per year.

On June 2, 2009, the referee determined that the above-described method used by Los Angeles County was correct.

In the second action, filed in Fresno County, seven cities (petitioners) filed suit against the county (respondent). In this action, the court ruled that the method used by Fresno County was not in accordance with statute. This is the same method approved by the referee in Los Angeles County. In relevant part, the court ruled:

Under the County's methodology, each city's allocation of property tax revenue is reduced by the amount of PTAF. In the first sentence of section 97.75, the Legislature prohibited counties from reducing the allocation in reimbursement for the services performed under the two swaps. But when the Legislature said what the counties can do to get reimbursed in the second sentence, it did not say that counties could reduce a city's property tax revenue allocation. But that is exactly the effect of the County's approach. . . .

Pursuant to section 97.75, Respondents are permitted to charge no more than their actual incremental costs in providing the services specified in Rev. & Tax Code §§ 97.68 and 97.70.

Currently, the SCO is not expressing an opinion on the computation of the PTAF until such time as appeals (if any) are resolved.

### Tax Equity Allocation Computations

Some cities historically received little or no property tax allocations from the taxes generated in their jurisdictional boundaries. Legislation was subsequently enacted to provide 7% of the property tax revenue, generated within the boundary of the qualifying city, phased in over a seven-year period. Some counties perform the tax equity allocation (TEA) calculation annually. Other counties have brought the TEA cities into the AB 8 process at 7% and do not perform the calculation annually. In the past, the SCO has accepted either methodology.

A dispute has arisen between a city and a county concerning the proper method of computing the minimum 7% share, commonly known as “tax equity allocation” or “TEA payment.” Among the items of contention is whether or not the TEA city’s ERAF shift, pursuant to Revenue and Taxation Code section 97.3, is restored through the TEA payment process, thus effectively making the TEA city exempt from the second shift. The first ERAF shift, under Revenue and Taxation Code section 97.2, requires that the TEA calculations be done “so that those computations do not result in the restoration of any reduction required pursuant to this section.” Revenue and Taxation Code section 97.3 does not include similar language.

Currently, the SCO is not expressing an opinion on the TEA process in any county with a TEA city until the legal issues are resolved.

### **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 2011 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

Findings noted in prior audits have been satisfactorily resolved by the counties.

## 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.)

We noted three counties that continued to have base year revenue and factor computation errors that have not been corrected.

## 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.

No errors were noted in this area.

## 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 had errors in its AB 8 system that caused the factors and allocations in the supplemental property tax system to be incorrect beginning with FY 2003-04.

**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 the counties adopt a method of identifying the actual administrative costs associated with the supplemental roll, they are allowed to charge an administrative fee for supplemental property tax collections. This fee is not to exceed 5% of the supplemental taxes collected.

No errors were noted in this area.

**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 included the airplane assessed value levy in the redevelopment agency tax increment adjustment process. The Educational Revenue Augmentation Fund received pass-through payments from the redevelopment agency.

**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 FY 1988-89.

Seven counties included the ERAF as a taxing jurisdiction in unitary and operating nonunitary apportionment calculations.

**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 (PTAF). 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 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 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 other levy on a city for these services, but the fee, charge, or other levy shall 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, we will review the PTAF process again to determine if any adjustments are warranted and will modify reports accordingly; the counties will also be allowed to modify their method of imposing the fee. Currently, the SCO is not expressing an opinion on the computation of the PTAF until all legal issues are resolved.

## **Educational Revenue Augmentation Fund**

The legal requirements for the local agency shift of property tax revenues to the Education Revenue Augmentation Fund (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 Assembly Bill (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 SCO 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 AB 1589, Chapter 290, Statutes of 1997. Subsequently, the Legislature enacted AB 417 (Chapter 464, Statutes of 1999), restoring the exemption to fire districts.

We noted that, in two counties, the errors in the AB 8 system and the failure to carry forward the correct ERAF shift amounts (with growth) from the prior year caused the ERAF shift amounts for some agencies to be incorrect.

Furthermore, in another county, the FY 2005-06 base revenue ERAF shift did not carry forward to FY 2006-07.

**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 issue is noted as an observation until the legal issues are addressed. After all legal challenges are resolved, the SCO will review the no- or low-property tax revenue procedures again to determine if any adjustments or corrections are warranted, and we will modify any reports accordingly.

Currently, the SCO is not expressing an opinion on the TEA process in any county with a TEA city until the legal issues are resolved.

**Sales and Use Tax/Vehicle License Fee Adjustment**

The Revenue and Taxation Code requires allocation of ad valorem property tax revenue by ERAF to Sales and Use Tax and Vehicle License Fee adjustment amount under code sections 97.68 and 97.70. If there is not enough ad valorem property tax revenue in ERAF, the difference shall be reduced from all school districts and community college district that are not excess tax school entities.

No errors were noted in this area.

# 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 State Controller's Office (SCO) in calendar year 2011. 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.

## Alpine County (July 1, 2004, through June 30, 2008)

### Follow-up on Prior Audit Findings

The county has satisfactorily resolved the findings noted in our prior audit report, issued November 2004.

### Conclusion

Our audit disclosed that the county complied with California statutes for the allocation and apportionment of property tax revenues for period audited.

## Colusa County (July 1, 2003, through June 30, 2009)

### Follow-up on Prior Audit Findings

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

### FINDING 1— Calculation and distribution of ATI

The county miscalculated the annual tax increment amounts, and did not carry forward some of the base revenues from the prior year, causing the current year's revenues, growth percentages, and Assembly Bill (AB) 8 apportionment factors computations to be incorrect. As a result, all agencies received incorrect tax allocations.

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

During the audit fieldwork, the county re-computed the AB 8 system and made the proper adjustments to the tax allocations. The county then provided copies of the corrected AB 8 documents to the SCO auditors. We will review the tax allocations again during the next audit to ensure that the county implemented the correction for FY 2009-10 and each fiscal year thereafter.

County's Response

I accept the findings with the knowledge that all necessary revisions have been accomplished and audited by your staff.

**FINDING 2—  
Supplemental  
property tax**

The errors in the AB 8 system caused the factors and allocations in the supplemental property tax system to be incorrect beginning with FY 2003-04.

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

During the audit fieldwork, the county corrected the supplemental property tax apportionment factors and allocation of revenues. The county then provided copies of the corrected supplemental property tax documents to the SCO auditors. We will review the supplemental property tax apportionment factors again during the next audit to ensure that the county implemented the correction for FY 2009-10 and each fiscal year thereafter.

County's Response

I accept the findings with the knowledge that all necessary revisions have been accomplished and audited by your staff.

**FINDING 3—  
Unitary and operating  
nonunitary  
apportionment**

The county did not properly compute the unitary and operating nonunitary property taxes, including the regulated railway revenues.

1. The unitary and operating non-unitary property tax apportionment factors and allocations were not computed correctly. In addition, the ERAF was included in the unitary and operating non-unitary tax apportionment process;
2. The unitary railroad base revenues, and tax apportionment factors and allocations were not computed correctly. In addition, the ERAF was excluded in the tax 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

During the audit fieldwork, the county corrected all noted errors in the system and made the appropriate adjustments to the affected agencies. The county provided copies of the corrected unitary and regulated railway property tax documents to the SCO auditors. We will review the unitary and operating nonunitary allocations and the regulated railway allocations again during the next audit to ensure that the county implemented the correction for FY 2009-10 and each fiscal year thereafter.

The county should not include the ERAF in future unitary and operating non-unitary tax apportionment computations, as the ERAF does not qualify as a taxing jurisdiction under Revenue and Taxation Code section 100. Thus, the ERAF is not eligible to share and its amount should be distributed proportionately among all taxing jurisdictions that contributed to the fund.

#### County’s Response

Regarding the inclusion of the ERAF in the unitary and operating non-unitary tax apportionment process, I understand there is a legal opinion issued by the State Controller’s Office to support the exclusion of ERAF in unitary and operating non-unity tax apportionment process. I am happy to make that correction, upon receipt of the State Controller’s legal opinion. In the meantime, I am inclined to follow the Property Tax Guidelines for the ERAF calculations. The guidelines were developed by State Controller’s staff and County Auditor-Controller’s representatives, based on legislation, to ensure all counties consistently follow the same property tax allocation methods throughout the State.

#### SCO’s Comment

Our finding and recommendation remain unchanged.

The ERAF is a fund—an accounting entity, not a taxing jurisdiction. Revenue and Taxation Code section 100 requires that taxes from unitary and operating nonunitary property be allocated to taxing jurisdictions.

The county states that it is inclined to follow the Property Tax Guidelines for the ERAF calculations as outlined in the California Property Tax Managers' Reference Manual. While we recognize the guidelines prepared by the County Property Tax Managers' Association as a guide, it is important to note that we audit to applicable statutes. Furthermore, it must be noted that the SCO did not participate in the development of the Reference Manual and has also not approved it.

**FINDING 4—  
Property tax  
administrative costs**

The errors in the AB 8 system, identified in Finding 1, caused the factors and allocations in the property tax administrative costs system to be incorrect.

Requirements for the reimbursement of county property tax administrative costs are found in Revenue and Taxation Code section 95.3. County property tax administrative costs are incurred by the assessor, the tax collector, the assessment appeals board, and the auditor. The county is allowed, depending on the fiscal year and any corresponding exclusions, to be reimbursed by local agencies and public schools for these administrative costs.

Recommendation

During the audit field work, the county corrected the property tax administrative cost factors and allocations. The county then provided copies of the corrected property tax administrative cost documents to the SCO auditors. We will review the property tax administrative cost factors again during the next audit to ensure that the county implements the correction for FY 2009-10 and each fiscal year thereafter.

County's Response

I accept the findings with the knowledge that all necessary revisions have been accomplished and audited by your staff.

**FINDING 5—  
Educational Revenue  
Augmentation Fund  
(ERAF)**

The errors in the AB 8 system, identified in Finding 1, and the failure to carry forward some of the agencies' ERAF shift amounts from the prior year caused the ERAF shift amounts for all fiscal years to be incorrect.

Requirements for the local agency shift of property tax revenues to the ERAF are primarily found in Revenue and Taxation Code sections 97.1 through 97.3. Beginning in FY 1992-93, most local agencies were 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 determined by adding a per capita amount to a percentage of property tax revenues received by each city. The amount for counties was 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

During the audit fieldwork, the county corrected the ERAF factors and allocations. The county then provided copies of the corrected ERAF shift documents to the SCO auditors. We will review the ERAF shift amounts again during the next audit to ensure that the county implements the correction for FY 2009-10 and each fiscal year thereafter.

#### County's Response

I accept the findings with the knowledge that all necessary revisions have been accomplished and audited by your staff.

## **Inyo County (July 1, 2003, through June 30, 2010)**

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

The county has satisfactorily resolved the findings noted in our prior audit report, issued on April 16, 2004.

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

The county included the Educational Revenue Augmentation Fund (ERAF) in the unitary and operating nonunitary tax apportionment computation during this audit period.

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 not include the ERAF in future unitary and operating nonunitary tax apportionment computations, as the ERAF does not qualify as a “taxing jurisdiction” under the Revenue and Taxation Code section 100. Thus, the ERAF is not eligible to share and its amount should be distributed proportionately among all taxing jurisdictions that contributed to the fund.

### County’s Response

Consistent with the majority of counties in the State, Inyo County included ERAF in the unitary and operating nonunitary apportionments in accordance with unitary and nonunitary allocation guidelines. The State Auditor’s Association recommended that County Auditors make no changes in their allocation methodology and stay consistent in following the Property Tax Manager’s Reference Manual. Until the legislature classifies this issue, we do not intend to change our position.

### SCO’s Comment

Our finding and recommendation remain unchanged.

The ERAF is a fund—an accounting entity, not a taxing jurisdiction. Revenue and Taxation Code section 100 requires that taxes from unitary and operating nonunitary property be allocated to taxing jurisdictions.

The county’s statement that “The State Auditor’s Association recommended that County Auditors make no changes in their allocation methodology and stay consistent in following the Property Tax Manager’s Reference Manual” is not relevant. We audit to applicable statutes.

As the ERAF is not a taxing jurisdiction, it is not eligible to receive unitary and operating nonunitary taxes.

## **Nevada County (July 1, 2002, through June 30, 2010)**

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

Findings noted in our prior audit, issued December 2003, have been satisfactorily resolved by the county, with the exception of the base revenue adjustments between the City of Grass Valley and the Consolidated Fire District. The county inadvertently removed \$3,499 from Ophir Hill Fire District and transferred this base to the City of Grass Valley.

During the audit fieldwork, the county corrected the noted error and made the appropriate transfer to reflect the correct exchange of property tax revenues according to the resolutions. No further action is required.

**FINDING 1—  
Calculation and  
distribution of ATI**

In fiscal year (FY) 2007-08 and FY 2009-10, the county did not include the base year annexation adjustment amounts in the growth percentage calculation, thereby causing errors in the Educational Revenue Augmentation Fund (ERAF) shift amounts, Assembly Bill (AB) 8 revenues, and AB 8 apportionment factors for some agencies.

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 (TRA) 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

During the audit fieldwork, the county re-computed the AB 8 system and made the proper adjustments to the base year amounts and growth percentages. The county then provided the SCO with copies of the corrected AB 8 documents. We will review the tax allocations again during the next audit to ensure that the county implemented the correction for FY 2010-11 and each fiscal year thereafter.

County's Response

The County does concur with this finding and will implement the correction.

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

The unitary and operating non-unitary property tax apportionment factors and allocations have not been computed correctly since FY 2002-03. In addition, the ERAF was included in the tax 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

During the audit fieldwork, the county corrected the unitary and operating non-unitary property tax apportionment factors and made the appropriate adjustments to the affected agencies. The county then provided the SCO with copies of the corrected unitary property tax documents. We will review the unitary and operating non-unitary allocations again during the next audit to ensure that the county implemented the correction for FY 2010-11 and each fiscal year thereafter.

The county should not include the ERAF in future unitary and operating non-unitary tax apportionment computations, as the ERAF does not qualify as a taxing jurisdiction under Revenue and Taxation Code section 100. Thus, the ERAF is not eligible to share and its amount should be distributed proportionately among all taxing jurisdictions that contributed to the fund.

#### County's Response

The County does concur that the unitary and operating non-unitary apportionment factors and allocations were not computed correctly since 2002-03. This correction will be implemented.

The County respectively disagrees with the finding that the Educational Revenue Augmentation Fund (ERAF) should be excluded from the unitary and non-unitary tax apportionment computations. This finding is not consistent with the results of our prior tax audit for the period of July 1, 1997 through June 30, 2002. In our prior audit, the ERAF computation was included in the same manner and a finding noted that it had been under allocated by \$91,755. We have consistently followed the methodology of the computation as outlined in the Tax Manager's Reference Manual as approved by the State Association of County Auditors. We consider this methodology to be in accordance with the R&T Code section 100.

#### SCO's Comment

Our finding and recommendation relating to the inclusion of the ERAF in the unitary and operating nonunitary apportionment remain unchanged.

The ERAF is a fund—an accounting entity—not a taxing jurisdiction. Revenue and Taxation Code section 100 requires that taxes from unitary and operating property be allocated to taxing jurisdictions. As the ERAF is not a taxing jurisdiction, it is not eligible to receive unitary and operating nonunitary taxes.

The county states that the Finding is not consistent with the prior SCO audit from July 1, 1997, through June 30, 2002. We acknowledge that the county's methodology was found to be in compliance in previous audits, because in our audit reports issued prior to FY 2004-05, we stated that the ERAF should receive unitary and operating nonunitary revenues. However, at the request of another county, the SCO revisited the issue and determined that because the ERAF was not a taxing jurisdiction, it was not eligible to receive unitary and operating nonunitary revenues.

Additionally, the county also stated that it will continue to follow the guidelines from the Tax Managers Reference Manual to allocate unitary and operating nonunitary tax to the ERAF. While we acknowledge the fact that the Tax Managers' Reference Manual is a guide, we audit to applicable statutes.

**FINDING 3—  
Educational Revenue  
Augmentation Fund  
(ERAF)**

The errors in the AB 8 system, identified in Finding 1, and the failure to carry forward the correct ERAF shift amounts (with growth) from the prior year, caused the ERAF shift amounts for some agencies to be incorrect since FY 2003-04.

Requirements for the local agency shift of property tax revenues to the ERAF are primarily found in Revenue and Taxation Code sections 97.1 through 97.3. Beginning in FY 1992-93, most local agencies were 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 determined by adding a per capita amount to a percentage of property tax revenues received by each city. The amount for counties was 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

During the audit fieldwork, the county corrected the growth percentages and ERAF shift amounts. The county then provided the SCO with copies of the corrected ERAF shift documents. We will review the ERAF shift amounts again during the next audit to ensure that the county implemented the correction for FY 2010-11 and each fiscal year thereafter.

#### County's Response

The County does concur with the finding and will implement the corrections.

## Sacramento County (July 1, 2006, through June 30, 2010)

### Follow-up on Prior Audit Findings

Our prior audit report, issued May 23, 2007, included no findings related to the apportionment and allocation of property tax revenues by the county.

### FINDING— ERAF included in unitary and operating nonunitary tax apportionment computation

The county included the Educational Revenue Augmentation Fund (ERAF) in the unitary and operating nonunitary tax apportionment computation during this audit period.

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 not include the ERAF in the future unitary and operating nonunitary tax apportionment computations, as the ERAF does not qualify as a “taxing jurisdiction” under Revenue and Taxation Code section 100. Thus, the ERAF is not eligible to share and its amount should be distributed proportionately among all taxing jurisdictions that contributed to the fund.

### County’s Response

ERAF does qualify as a “taxing jurisdiction” under the R & T code section 100 because ERAF, as a jurisdiction, received allocation of the County’s total ad valorem tax levies for the secured roll for the prior year (R & T code sections 96.1, 96.2, and 96.5(g)). Therefore, ERAF is a taxing jurisdiction for the purpose of allocating unitary and nonunitary tax revenues under the R & T code section 100(c) (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.”

Furthermore, by receiving its allocation under R & T code section 100(c)(3), ERAF continues to receive allocation of tax from the unitary and operating nonunitary property in proportion to all qualified taxing jurisdictions per R & T code sections 100(c)(1) and 100(c)(2).

Therefore, we will continue to follow the guidelines from the State Auditor Controller Association to allocate unitary and operating nonunitary tax to ERAF.

### SCO's Comment

Our finding and recommendation remain unchanged.

The ERAF is a fund—an accounting entity, not a taxing jurisdiction. Revenue and Taxation Code section 100 requires that taxes from unitary and operating nonunitary property be allocated to taxing jurisdictions. As the ERAF is not a taxing jurisdiction, it is not eligible to receive unitary and operating nonunitary taxes.

Revenue and Taxation Code section 100(c) states:

The property tax revenue derived from the assessed value assigned to the countywide tax rate area pursuant to subdivision (a) and pursuant to paragraph (2) of subdivision (a) of section 100.1 by the use of the tax rate determined in paragraph (1) of subdivision (b) shall be allocated as follows:

- (1) For the 1988-89 fiscal year and each fiscal year thereafter, each taxing jurisdiction shall be allocated an amount of property tax revenue. . . .

Revenue and Taxation Code section 95(a) defines a local agency as a “city, county, and special district.” In addition, section 95(b) defines a jurisdiction as a “local agency, school district, community college district or county superintendent of schools.”

The county contends that ERAF is a taxing jurisdiction for the purpose of allocating unitary and nonunitary tax revenues under the Revenue and Taxation Code section 100(c)(3). We find no statutory support for this viewpoint. In fact, Revenue and Taxation Code section 100(e) specifically includes a redevelopment agency as a “taxing jurisdiction.” By including redevelopment agencies as taxing jurisdictions, the Legislature demonstrates that it can include a non-taxing jurisdiction in the definition of taxing jurisdictions, if it so desires. In this case, the Legislature opted to include redevelopment agencies and not the ERAF.

The county states that it will continue to follow the guidelines from the State Property Tax Managers' manual to allocate unitary and operating nonunitary tax to ERAF. While we recognize the guidelines prepared by the County Property Tax Managers' Association as a guide, it is important to note that we audit to applicable statutes.

## San Joaquin County (July 1, 2005, through June 30, 2010)

### Follow-up on Prior Audit Findings

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

### FINDING— ERAF included in unitary and operating nonunitary apportionment

The county included the Educational Revenue Augmentation Fund (ERAF) in the unitary and operating non-unitary property tax apportionment process during this audit period.

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 fiscal year 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 not include the ERAF in future unitary and operating non-unitary tax apportionment computations, as the ERAF does not qualify as a "taxing jurisdiction" under Revenue and Taxation Code section 100. Thus, the ERAF is not eligible to share and its amount should be distributed proportionately among all taxing jurisdictions that contributed to the fund.

### County's Response

We disagree with the audit finding on the inclusion of ERAF in the unitary and operating non-unitary property tax apportionment computations. Our methodology was found to be in compliance in previous audits. We intend to be consistent and will continue to follow methodologies and guidelines approved by the California State Association of County Auditors.

SCO's Comment

The ERAF is a fund—an account entity—not a taxing jurisdiction.

The county states “our methodology was found to be in compliance in previous audits.” The county further noted that it will continue to follow methodologies and guidelines approved by the California State Association of County Auditors.

The State Controller's Office audit objective is to determine whether the county complied with the Revenue and Taxation requirements. As stated in the finding, we determined that the county did not comply with Revenue and Taxation Code section 100, because it included the ERAF in the unitary and operating non-unitary property tax apportionment process. Since the ERAF is not a taxing jurisdiction, it is not eligible to receive unitary and operating non-unitary property tax apportionments. Therefore, the county's disagreement with the finding because it was not disclosed in our prior audit, and its assertion of following the methodologies and guidelines approved by the California State Association of Auditors does not mean that the county was in compliance with the Revenue and Taxation Code section 100.

Our finding and recommendation remain unchanged.

**Shasta County (July 1, 2005, through June 30, 2010)****Follow-up on Prior Audit Findings**

The county has satisfactorily resolved the findings noted in our prior audit report, issued July 14, 2006.

**FINDING 1—  
Calculation and  
distribution of ATI**

During the current audit period, fiscal year (FY) 2005-06 through FY 2009-10, numerous base revenue adjustments were not computed correctly.

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 (TRA) 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

We recommend that the county correct the base revenue for all entities.

County’s Response

We acknowledge the necessity for accuracy in all property tax calculations. Staff will review calculations and make adjustments as appropriate.

**FINDING 2—  
Redevelopment  
agencies**

The county included the airplane assessed value levy in the redevelopment agency tax increment adjustment process.

The Educational Revenue Augmentation Fund (ERAF) received pass-through payments from the redevelopment agency.

Requirements for the apportionment and allocation of property taxes 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 should remove the airplane assessed value levy from the redevelopment agency annual tax increment for purposes of adjusting the various property tax allocation systems.

The ERAF is not a taxing entity; therefore, it is not eligible to receive AB 1290 pass-through payments.

County’s Response

We agree that the airplane assessed value levy should not be included in the redevelopment agency tax increment adjustment process and have removed it as recommended.

For Shasta County, the practice of the Educational Revenue Augmentation Fund (ERAF) receiving pass-through payments did not arise from reasoning that ERAF was a taxing entity, instead that pass-through monies were AB8 revenue and therefore subject to the ERAF shift.

**FINDING 3—  
ERAF included in  
unitary and operating  
nonunitary  
apportionment**

The county included the ERAF in the unitary and operating nonunitary tax apportionment computations for all years during this audit period.

The regulated railroad allocation system adjusted the school districts’ base year amounts before carrying forward that base into the subsequent fiscal year. In addition, the base revenues for FY 2008-09 did not carry forward in FY 2009-10.

The regulated railroad assessed valuation adjustment for the Midtown Redevelopment Agency was incorrect.

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

For all future unitary and operating nonunitary tax apportionment computations, the ERAF should not be included since it does not qualify as a “taxing jurisdiction” under Revenue and Taxation Code section 100. Thus, the ERAF is not eligible to share in the unitary and operating nonunitary computation and its amounts should be distributed proportionately among all taxing jurisdictions that contributed to the fund.

The regulated railway base revenues must carry forward to subsequent fiscal years before any adjustments are made. The regulated railway assessed valuation amount from the State Board of Equalization must be used to adjust the redevelopment agency base value.

#### County’s Response

Whether or not ERAF should be included in the unitary apportionment is an ongoing issue across the state caused by inconsistency in Revenue and Taxation law. Shasta County has included ERAF in the allocation of unitary revenue beginning in 1995 and since that time two audits by the State Controller’s Office appear to have supported this methodology without a finding. While we understand that the position of the SCO has changed on this matter since those audits, we are concerned with changing methodology based solely on that fact. Tax law has not changed nor have the guidelines in the California Property Tax Managers’ Reference Manual. Therefore until clear, consistent direction is given we will take this recommendation under advisement.

We have corrected the regulated railroad calculation as recommended.

#### SCO’s Comment

Our finding and recommendation remain unchanged.

The ERAF is a fund—an accounting entity, not a taxing jurisdiction. Revenue and Taxation Code section 100 requires that taxes from unitary and operating nonunitary property be allocated to taxing jurisdictions. The county’s assertion that the guidelines in the California Property Tax Managers’ Reference Manual have not changed is not relevant. We audit to applicable statutes.

As the ERAF is not a taxing jurisdiction, it is not eligible to receive unitary and operating nonunitary taxes.

**FINDING 4—  
Educational Revenue  
Augmentation Fund  
(ERAF)**

The FY 2005-06 base revenue ERAF shift for the Fire Protection Service Area 1 and Anderson Fire District did not carry forward to FY 2006-07.

The Halcumb Cemetery District and Western Shasta RCD property tax levy allocation was less than their ERAF shift. As a result, the two districts allocation factors were negative.

Requirements for the local agency shift of property tax revenues to the ERAF are primarily found in Revenue and Taxation Code sections 97.1 through 97.3. Beginning in FY 1992-93, most local agencies were 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 determined by adding a per capita amount to a percentage of property tax revenues received by each city. The amount for counties was 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 California 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 bail-out equivalent; or, for an independent district, deducting the amount received from the SDAF and the difference between the net current-year bail-out equivalent and the amount contributed to the SDAF from the net current-year bail-out 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 ERAF shift base revenues must carry forward in like amount into the next fiscal year.

The base revenues for all districts must be corrected in the AB 8 system to prevent negative property tax allocation to districts.

#### County's Response

We agree that the ERAF shift base revenues must carry forward in like amount into the next fiscal year. We will make the correction to the calculation for 2006-07 and forward for Fire Protection Services Area 1 and Anderson Fire District.

Prior Shasta County property tax audits completed by the State Controller's Office have addressed these negative allocation factors; no finding issued. At the exit conference for the previous audit (for the time period of July 1, 2000 to June 30, 2005) the following observation was included:

“It was noted during the review that there is a school district (Indian Springs) that has no AB8 revenue, though there is Value in the TRA(s) in which the school resides. However, it was also noted that this school has enough revenue from their Unitary property tax allocation to be a basic aid school. It is assumed that this anomaly occurred when the Unitary value was separated from the local Utility roll and though the computations may have appeared correct at the time, it should not have resulted that a jurisdiction should have no revenue in the AB8 process even though there is positive value in their TRA(s). There are also two local special districts (Halcumb Cemetery and Western Shasta RCD) whose AB8 revenue is reduced to zero after ERAF adjustments, possibly also due to inflated Unitary revenue amounts that were included in the original ERAF computations.

This issue is noted here simply to make the county aware that though the two systems (AB8/Unitary) currently seem to offset one another in this matter, if there should ever be a substantial change in the way either system is computed, some consideration may have to be made for districts such as those noted above.”

Instead of noting the issue as above, the current audit recommends correcting base revenues for all districts to eliminate negative property tax allocation factors.

Staff will review all referenced legislation. Consideration shall include but not be limited to; current audit interpretation of the appropriateness of negative allocation factors.

## **Solano County (July 1, 2006, through June 30, 2010)**

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

Our prior audit report, issued September 29, 2006, included no findings related to the apportionment and allocation of property tax revenues by the county.

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

The county included the Educational Revenue Augmentation Fund (ERAF) in the unitary and operating nonunitary tax apportionment during this audit 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 fiscal year (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 not include the ERAF in future unitary and operating nonunitary tax apportionment computations, as the ERAF does not qualify as a “taxing jurisdiction” under Revenue and Taxation Code section 100. Thus, the ERAF is not eligible to share and its amount should be distributed proportionately among all taxing jurisdictions that contributed to the fund.

#### County’s Response

We agree with your interpretation that ERAF should not be included in unitary and operating non-unitary apportionment. However, the procedure we used included ERAF in the apportionment and was based on a methodology adopted by the State Association of County Auditors (SACA) as outlined in the *California Property Tax Managers’ Reference Manual*. SACA is currently in the process of taking another look at the process in order to bring this issue to a final resolution.

In the meantime, we will continue with the current practice to include ERAF in our apportionment of unitary and operating non-unitary roll.

*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>**