STATE OF CALIFORNIA

Report to the California State Legislature

PROPERTY TAX APPORTIONMENTS

Calendar Year 2006

JOHN CHIANG
California State Controller

July 2007

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California State Controller

July 25, 2007

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

Re: Property Tax Apportionments Report to the Legislature for Calendar Year 2006

I am pleased to present the Property Tax Apportionments report for calendar year 2006. 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 2006 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

Attachment

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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 2006 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 Gov. Code. §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 2006, the SCO completed audits of 17 counties' property tax apportionment and allocation systems, processes, and records. The 17 counties include Alameda, Contra Costa, Del Norte, Kern, Los Angeles, Madera, Merced, Orange, San Francisco, San Joaquin, Santa Barbara, Shasta, Siskiyou, Solano, Sonoma, Trinity, and Tuolumne.

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 all 17 counties have successfully resolved the prior audit findings. In addition, we had no reportable audit findings or conditions in nine of the 17 counties audited during 2006.

Therefore, except for the findings and recommendations noted in this report, all 17 counties audited during 2006 complied with the requirements for the apportionment and allocation of property tax revenues.

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

- Five counties incorrectly allocated property taxes, resulting in some jurisdictions within the county receiving too much property tax revenues at the expense of other jurisdictions in the county. For example, one county did not properly compute growth in assessed valuation and used incorrect bond rates in its calculation. Another county made revenue computation errors as a result of using incorrect assessed values.

- Four counties incorrectly imposed administrative charges against some or all of the jurisdictions within the county. For example, one county charged its agencies for costs of administering the supplemental property tax program but could not produce any documentation to support the validity of such charges. Another county calculated its administrative charges by using data from an incorrect year.

- One county did not properly carry forward the prior year balance from the Educational Revenue Augmentation Fund, thereby improperly increasing the State's cost in support of schools and community colleges.

In their responses, the counties agreed with our findings and 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 17 audits of county property tax apportionments and allocations completed by the State Controller's Office (SCO) in calendar year 2006. The following counties were audited: Alameda, Contra Costa, Del Norte, Kern, Los Angeles, Madera, Merced, Orange, San Francisco, San Joaquin, Santa Barbara, Shasta, Siskiyou, Solano, Sonoma, Trinity, and Tuolumne. 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 audited counties complied with the requirements for the apportionment and allocation of property tax revenues.

Nine of the counties audited—Alameda, Contra Costa, Kern, Los Angeles, Orange, Siskiyou, Solano, Sonoma, and Trinity—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 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 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 § 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., Ed. Code § 42237.7 et seq., and Gov. Code § 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., Gov. Code § 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 2006 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.

We noted no findings for this area.

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. 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.)

One county did not properly include all new TRA factors for all jurisdictions in all new TRAs.

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.

We noted findings for two counties in this area.

One county failed to properly complete the exchange of tax increment factors for an annexation by a city.

One county had assessed value and increment factor errors in some of their jurisdictional exchanges.

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.

We noted no findings for this area.

Supplemental Property Tax Administrative Fees

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.

One county couldn't provide current documentation of supplemental property tax administrative costs.

Redevelopment Agencies

The legal requirements for the apportionment and allocation of property tax to redevelopment agencies 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.

We noted no findings for this area.

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.

We noted findings for two counties in this area.

One county had revenue computation errors because they used incorrect assessed values.

One county did not properly compute growth when assessed valuation increased by more than 2% over the prior year. They also used incorrect bond rates.

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.

We noted findings for three counties in this area.

One county did not include unitary revenue in the computation of administrative cost allocation factors.

One county computed the administrative cost reimbursement allocation for one year using costs from an incorrect year.

One county did not properly include ERAF III contributions in the computation of administrative cost allocation factors for FY 2004-05.

Educational Revenue Augmentation Fund

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 of particular interest 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 § 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 § 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. 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, Statues of 1997. Subsequently, the Legislature enacted AB 417 (Chapter 464, Statutes of 1999), restoring the exemption to fire districts.

One county did not properly carry forward prior year ERAF amounts throughout the audit period.

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.

We noted no findings in this area.

Senate Bill 1096 and Assembly Bill 2115 Reviews

During 2006, we also reviewed the counties' second year implementation of the requirements of SB 1096 (Chapter 211, Statutes of 2004), as amended by AB 2115 (Chapter 610, Statutes of 2004). Although we noted findings, we found that the counties' implementation generally complied with those requirements.

A small number of counties made errors in computing property tax administration charges, supplemental property tax apportionment factors, or unitary computations when unitary assessed values grew by more than 2% over the preceding year.

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 2006. 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.

Alameda County (July 1, 2002, through June 30, 2005)

Follow-up on Prior Audit Findings

The county has satisfactorily resolved the findings noted in our prior audit report, issued July 23, 2003.

Conclusion

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

Contra Costa County (July 1, 2002, through June 30, 2005)

Follow-up on Prior Audit Findings

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

Conclusion

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

Del Norte County (July 1, 2000, through June 30, 2005)

Follow-up on Prior Audit Findings

The county has satisfactorily resolved the findings noted in our prior audit report, issued November 1, 2001.

FINDING 1—Jurisdictional changes

The county failed to properly complete the exchange of tax increment factors between the county and the City of Crescent City for an annexation to the city.

The legal requirements for jurisdictional changes are stated 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, local government agencies are required to negotiate any exchange of base year property tax revenue and annual tax increment. After the jurisdictional change, the local agency whose responsibility increased receives additional annual tax increment, and the base property tax revenues are adjusted according to the negotiated agreements.

Recommendation

The county computed the correct increment factors and corresponding revenue amounts for the city and county during this audit and inserted the correct amounts into their AB 8 processing system. If the corrected amounts are carried forward into the next AB 8 processing cycle (fiscal year [FY] 2005-06), no further adjustment will be necessary to correct this item.

County's Response

> In response to finding 1, the County has corrected AB8 factors were corrected for 2004/2005 and the adjustment was made in the final tax allocation. The corrected AB8 factors have been carried over to the 2005/2006 roll.

FINDING 2—Educational Revenue Augmentation Fund (ERAF)

The county carried forward the incorrect ERAF contribution amounts in FY 2001-02 and 2002-03, resulting in a net understatement of ERAF contributions for FY 2001-02 through 2004-05 (Schedule 1).

Requirements for the local agency shift of property tax revenues to the ERAF are stated in Revenue and Taxation Code sections 97.1 through 97.3. Beginning in 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 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, the county computed corrected ERAF contribution amounts for all affected agencies for FY 2001-02 through 2004-05 and determined the net over/underpayments made for the audit period. If the county properly carries forward the corrected amounts to the FY 2005-06 process and makes appropriate revenue adjustments to all affected agencies and the ERAF, no further adjustments will be necessary to correct this finding.

County's Response

> In response to finding 2, the County has computed the correct ERAF contribution amounts for fiscal year 2001/2002 through 2004/2005. The county has carried over the corrected amounts to the fiscal year 2005/2006 calculations. Revenue adjustments have been made in the fiscal year 2005/2006 tax allocations and will be adjusted in fiscal year 2006/2007 and completed in 2007/2008.

SCO's Comment

The county's response indicates an intention to repay its ERAF over a three-year period. The county should contact the SCO to request a formal agreement to repay the amount owed.

Kern County (July 1, 2001, through June 30, 2005)

Follow-up on Prior Audit Findings

The county has satisfactorily resolved findings noted in our prior audit report, issued February 26, 2003.

Conclusion

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

Los Angeles County (July 1, 2003, through June 30, 2005)

Follow-up on Prior Audit Findings

Our prior audit report, issued December 2003, included no findings related to the apportionment and allocation of property tax revenues by the county.

Conclusion

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

Madera County (July 1, 2000, through June 30, 2005)

Follow-up on Prior Audit Findings

The county has satisfactorily resolved the findings noted in our prior audit report, issued August 11, 2001.

FINDING—Property tax administrative costs

Madera County did not document the costs of assessing, billing, collecting, and apportioning the local property taxes for the AB 8 and unitary process for fiscal year 2004-05. The county did not properly compute the costs for FY 2004-05; instead, it used previously used costs for the fiscal year.

Requirements for the reimbursement of county property tax administrative costs are listed 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 may, depending on the fiscal year and any corresponding exclusions, be reimbursed by local agencies and public schools for these administrative costs.

Recommendation

We recommend that the county calculate the administrative cost fee every year as stated by statutes.

County's Response

> There is only one finding in the subject audit report and, while it is substantially correct, the way it is worded is, I believe, misleading. The finding is that "Madera County did not document the costs of assessing, billing, collecting, and apportioning the local property taxes for the AB 8 and unitary process for fiscal year 2004-05. The county did not properly compute the costs for FY 2004-05; instead, it used previously used costs for the fiscal year."

> Every year since 1994-95, Madera County has hired the firm of David M. Griffith (now Maximus, Inc.), to calculate Property Tax Administration Fees using the costs incurred in the Assessor, Tax Collector, Auditor-Controller and Assessment Appeals Board cost centers in the most current completed fiscal year. In fiscal year 2004-05, the report was not completed by the time the April 10, 2005 property tax collections were apportioned. Historically, we have always deducted the Property Tax Administration Fees from the apportionment of the April 10th collections. So as not to delay the apportionment of the April 10, 2005 collections, I decided to use the Property Tax Administration Fees calculated by Maximus, Inc. for the prior year, 2003-04 as an approximation of the 2004-05 fees. These estimated fees were apportioned to the entities receiving taxes using the 2004-05 AB 8 factors. I estimated that the actual fees for 2004-05, when available, would exceed the 03-04 fees used as an estimate as costs had increased each year since 1994-95. I would like the subject audit report to show that the Property Tax Administration Fees charged in fiscal year 2004-05 were properly computed fees. In my opinion, the circumstance appropriate for comment in the report, is that the fees charged in 04-05 were those properly computed for the 03-04 fiscal year.
>
> I agree with the recommendation that the Property Tax Administrative Fees should be recalculated each year using the most current cost data and have returned to that practice for fiscal year 05-06. If you have any questions or need additional information, please contact me.

SCO's Comment

Although the methodology used by the county to calculate the property tax administration costs for FY 2004-05 is correct, Mr. DeWall admits that the county charged property tax administration costs for FY 2004-05 using FY 2003-04 costs. Therefore, the finding remains as written.

Merced County (July 1, 2000, through June 30, 2005)

Follow-up on Prior Audit Findings

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

FINDING 1—Calculation and distribution of ATI

In fiscal year (FY) 2004-05, the county did not use all of the tax rate area (TRA) factors (new TRAs) when computing increments for a few jurisdictions.

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

The county has input the newly created TRAs in FY 2005-06 and is in the process of fixing the base for FY 2004-05. No further action is required. The county should establish and implement procedures to ensure that all TRAs are included in the computation of tax increment.

FINDING 2— Unitary and operating nonunitary apportionment

In FY 2004-05, the county did not properly compute growth for the unitary and operating non-unitary property tax system when the assessed valuation exceeded 2% over the previous year. The county did not compute greater than 102% factors using the prior year AB 8 formula for the revenue increase in excess of 2%.

Revenue and Taxation Code section 100 contains the requirements for the apportionment and allocation of unitary and operating nonunitary property taxes.

Unitary properties are those properties to 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 recomputed the greater than 102% factors by using the prior year AB 8 formula for the revenue increase in excess of 2%. No further action is required.

FINDING 3 — Property tax administrative costs

The county did not use unitary revenue amounts in its computation of the prorated share of costs for FY 2002-03 and FY 2003-04.

Revenue and Taxation Code section 95.3 contains the requirements for the reimbursement of county property tax administrative costs. 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

For future years, the county should include unitary revenue amount in its computation of the prorated share of administration costs.

Orange County (July 1, 2002, through June 30, 2005)

Follow-up on Prior Audit Findings

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

Conclusion

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

San Francisco City and County (July 1, 2001, through June 30, 2004)

Follow-up on Prior Audit Findings

The city and county has satisfactorily resolved findings noted in our prior audit report, issued July 11, 2003.

FINDING—Unitary and operating nonunitary apportionment

The unitary and operating nonunitary assessed value in excess of 102% for fiscal year FY 2002-03 was allocated using FY 2002-03 AB 8 apportionment factors. In addition, the bond rate used in the unitary and operating nonunitary system is the same bond rate used for secured property tax.

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 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."

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 City and County of San Francisco corrected both issues as of September 14, 2005. The city and county should establish procedures to ensure that the proper apportionment factors and bond rates are used in the unitary and operating nonunitary system.

City and County's Response

With regard to the apportionment factors:

> The County agrees with your finding and corrected the apportionment factors to allocate unitary and operating non-unitary monies calculated in excess of 102% for FY 2002-03 by the prior year AB 8 apportionment factors, effective Sept. 14, 2005.

With regard to the bond rate:

> The County concurs with your finding and report recommendation.

San Joaquin County (July 1, 2001, through June 30, 2005)

Follow-up on Prior Audit Findings

Our prior audit report, issued December 31, 2002, had no findings related to the county's apportionment and allocation of property tax revenues.

FINDING—Supplemental property tax-administrative costs

The county failed to document the cost of the supplemental tax process to support the administrative amount collected.

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 develop procedures and document sufficient supplemental costs to justify the amount(s) of administrative cost collections.

County's Response

> In connection with the State Controller's Office audit of San Joaquin County's property tax apportionment and allocation system for the period of July 1, 2001, through June 30, 2005, for the purposes of determining the county's compliance with the California *Revenue and Taxation Code* and applicable rules and regulations, please be advised that County of San Joaquin has procedures and documentation now to justify the amount of administrative cost collection for the supplemental cost.

Santa Barbara County (July 1, 2002, through June 30, 2005)

Follow-up on Prior Audit Findings

The county satisfactorily resolved the findings noted in our prior audit report, issued June 25, 2003.

FINDING—Jurisdictional changes

The county incorrectly computed jurisdictional changes as follows.

1. The final assessed values for jurisdictional changes in the Auditor-Controller's automated property tax system did not reconcile with those in the County Assessor's automated system.

2. The county used an incorrect assessed value to compute jurisdictional change for tax rate area (TRA) 08-001.

3. The county used an incorrect existing TRA factor to compute jurisdictional change in a resulting TRA 01-038.

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 increased receives additional annual tax increment, and the base property tax revenues are adjusted according to the negotiated agreements.

Recommendation

The county should examine all jurisdictional changes that occurred between fiscal year (FY) 2002-03 and FY 2004-05, reconcile any differences, and adjust the assessed values as necessary.

County's Response

> We understand the importance of jurisdictional changes and will review our processes to ensure these issues are appropriately examined, that any necessary corrections are made, and that identified improvements are included in the implementation of our new property Tax systems currently in development. The identified errors for Items 2 and 3 were corrected during the course of the audit.

Shasta County (July 1, 2000, through June 30, 2005)

Follow-up on Prior Audit Findings

Our prior audit report, issued August 29, 2001, had no findings related to the apportionment and allocation of property tax revenues by the county.

FINDING—Property tax administrative costs

The county did not remove ERAF III contributions from the county's and cities' revenue for the administrative cost share computation for fiscal year 2004-05.

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

The county has computed adjusted administrative cost share factors for the county and cities for fiscal year 2004-05. If the amounts are adjusted as presented in the correcting schedule provided to the SCO, no

additional adjustment will be necessary. We will review this issue during our next audit of the county to ensure that adjustments were made correctly.

Siskiyou County (July 1, 2001, through June 30, 2006)

Follow-up on Prior Audit Findings

The county satisfactorily resolved the findings noted in our prior audit report, issued April 4, 2003.

Conclusion

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

Solano County (July 1, 2002, through June 30, 2006)

Follow-up on Prior Audit Findings

Our prior audit report, issued December 31, 2002, had no findings related to the apportionment and allocation of property tax revenues by the county.

Conclusion

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

Sonoma County (July 1, 2002, through June 30, 2005)

Follow-up on Prior Audit Findings

Our prior audit report, issued July 18, 2003, had no findings related to the apportionment and allocation of property tax revenues by the county.

Conclusion

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

Trinity County (July 1, 2000, through June 30, 2005)

Follow-up on Prior Audit Findings

The county has satisfactorily resolved the findings noted in our prior audit report, issued May 2001.

Conclusion

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

Tuolumne County (July 1, 1999, through June 30, 2004)

Follow-up on Prior Audit Findings

The county satisfactorily resolved findings noted in our prior audit report, issued April 30, 2001.

FINDING 1—Unitary and operating nonunitary apportionment

The county's unitary revenue amounts were incorrect in the last two years of this audit period. The prior year values were not properly carried forward and the assessed value was overstated, including utility value that was also included on the local secured roll in the AB 8 process.

Revenue and Taxation Code section 100 provides the requirements for the apportionment and allocation of unitary and operating nonunitary property taxes.

Unitary properties are those properties to 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). 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 computed corrected unitary revenue amounts for all affected taxing entities through the start of FY 2004-05 during the audit. If the corrected revenue amounts are used for the FY 2004-05 tax process, no further corrections will be necessary. The SCO will confirm the corrections during our next audit.

FINDING 2 — Property tax administrative costs

The county's computation of administrative costs for the last four years of the audit was incorrect. The county added offsets to costs such as fees and supplemental tax administration collections, rather than subtracting them. These errors resulted in an overstatement of charges to all local agencies for these years; schools and ERAF were not charged.

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

Recommendation

The county computed corrected administrative costs for all local agencies during the audit. A proposed adjustment to the costs for FY 2004-05, if implemented, would correct the prior-year errors, and no further correction will be necessary. The SCO will confirm the corrections during our next audit.

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

State Controller's Office
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http://www.sco.ca.gov

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