EL DORADO COUNTY

Audit Report

PROPERTY TAX APPORTIONMENT AND ALLOCATION SYSTEM

July 1, 2006, through June 30, 2013

BETTY T. YEE
California State Controller

March 2015

BETTY T. YEE
California State Controller

March 26, 2015

The Honorable Joe Harn
Auditor-Controller
El Dorado County
360 Fair Lane
Placerville, CA 95667

Dear Mr. Harn:

The State Controller's Office audited the methods employed by El Dorado County to apportion and allocate property tax revenues for the period of July 1, 2006, through June 30, 2013. The audit was conducted pursuant to the requirements of Government Code section 12468.

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

However, we observed that the county computed total net administrative costs and included Vehicle License Fee/Sales and Use Tax (VLF/SUT) up to fiscal year 2011-12. The VLF/SUT is not to be included in the administrative cost computation. As a result, the administrative pro-rata share of costs was overstated, substantially increasing the amount of proportionate costs to cities. The county removed the VLF/SUT from the administrative cost calculation for FY 2013-14 forward. We noted that the county has not resolved the disputed amounts with one of the cities. The county must complete the refund or agreement of the overcharge to the city.

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

Sincerely,

JEFFREY V. BROWNFIELD, CPA
Chief, Division of Audits

JVB/gc

cc: Sally Zutter, Accounting Division Manager
El Dorado County
Jody Martin, Principal Consultant
Joint Legislative Budget Committee
Peter Detwiler, Staff Director
Senate Local Government Committee
Elvia Dias, Committee Assistant
Senate Local Government Committee
Dixie Martineau-Petty, Secretary
Assembly Local Government Committee
Gayle Miller, Staff Director
Senate Revenue and Taxation Committee
Oksana Jaffe, Chief Consultant
Assembly Revenue and Taxation Committee
Neil McCormick, Executive Director
California Special Districts Association
Richard J. Chivaro, Chief Counsel
State Controller's Office
Brian K Veerkamp, Chair
Board of Supervisors, El Dorado County

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Summary

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The issue will be kept open for follow-up in the subsequent audit.

Background

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

One key law was Assembly Bill (AB) 8, Chapter 282, Statutes of 1979, which established the method of allocating property taxes for fiscal year (FY) 1979-80 (base year) and subsequent fiscal years. The methodology is commonly referred to as the AB 8 process or the AB 8 system.

The property tax revenues that local government agencies receive each fiscal year are based on the amount received in the prior year, plus a share of the property tax growth within their boundaries. Property tax revenues are then apportioned and allocated to local agencies and schools using prescribed formulas and methods defined in the Revenue and Taxation Code.

The AB 8 base process involved numerous steps, including the transfer of revenues from schools to local agencies (AB 8 shift) and the development of the tax rate area annual tax increment apportionment factors (ATI factors), which determine the amount of property tax revenues to be allocated to each jurisdiction.

The total amount to be allocated to each jurisdiction is then divided by the total amount to be allocated to all entities to determine the AB 8 apportionment factor (percentage share) for each entity for the year. The AB 8 factors are computed each year for all entities, using the revenue amounts established in the prior year. These amounts are adjusted for growth annually, using ATI factors.

Subsequent legislation removed revenues generated by unitary and nonunitary properties, regulated railway companies, and qualified electric properties from the AB 8 process. These revenues are now allocated and apportioned under separate processes.

Other legislation established an Educational Revenue Augmentation Fund (ERAF) in each county. Most local government agencies are required to transfer a portion of their property tax revenues to the fund. The fund is subsequently allocated and apportioned to schools by the county auditor according to instructions received from the county superintendent of schools or the State Chancellor of Community Colleges.

Revenues generated by the different types of property tax are apportioned and allocated to local agencies and schools using prescribed formulas and methods, as defined in the Revenue and Taxation Code. Taxable property includes land, improvements, and other properties that are accounted for on the property tax rolls maintained primarily by the county assessor. Tax rolls contain an entry for each parcel of land, including the parcel number, the owner's name, and the value. Following are the types of property tax rolls:

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

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

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

- *Supplemental Roll*—This roll contains property that has been reassessed due to a change in ownership or the completion of new construction, where the resulting change in assessed value is not reflected in other tax rolls.

To mitigate problems associated with the apportionment and allocation of property taxes, Senate Bill 418 was enacted in 1985 requiring the State Controller to audit the counties' apportionment and allocation methods and report the results to the California State Legislature.

Objective, Scope, and Methodology

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

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

We performed the following procedures:

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

We conducted this performance audit under the authority of Government Code sections 12468 and 12410. We did not audit the county's financial statements. We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. The audit covered the period of July 1, 2006, through June 30, 2013. Our audit scope was limited to:

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

A property tax bill contains the property tax levied at a 1% tax rate pursuant to the requirement of Proposition 13. A bill may also contain special taxes, debt services levies on voter-approved debt, fees, and assessments levied by the county or a city. The scope of our audit is concerned with the distribution of the 1% tax levy. Special taxes, debt service levies on voter-approved debt, fees, and assessments levied by the county or a city are beyond the scope of our audit and were not reviewed or audited.

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

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

Conclusion

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

However, we observed that the county computed total net administrative costs and included Vehicle License Fee/Sales and Use Tax (VLF/SUT) up to fiscal year 2011-12. The VLF/SUT is not to be included in the administrative cost computation. As a result, the administrative pro-rata share of costs was overstated, substantially increasing the amount of proportionate costs to cities. The county removed the VLF/SUT from the administrative cost calculation for FY 2013-14 forward. We noted that the county has not resolved the disputed amounts with one of the cities. The county must complete the refund or agreement of the overcharge to the city.

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Follow-up on Prior Audit Findings

The county has satisfactorily resolved the findings noted in our prior audit report, issued January 2008.

Views of Responsible Officials

We issued a draft audit report on August 25, 2014. Sally Zutter, Accounting Division Manager, responded by telephone on October 24, 2014, agreeing with the audit results.

Restricted Use

This report is solely for the information and use of the county, the California Legislature, and the SCO; it is not intended to be and should not be used by anyone other than these specified parties. This restriction is not intended to limit distribution of this report, which is a matter of public record.

JEFFREY V. BROWNFIELD, CPA
Chief, Division of Audits

March 26, 2015

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