

SAN BERNARDINO COUNTY

Audit Report

PROPERTY TAX APPORTIONMENT AND ALLOCATION SYSTEM

July 1, 2004, through June 30, 2006



JOHN CHIANG
California State Controller

January 2007



JOHN CHIANG
California State Controller

January 26, 2007

The Honorable Larry Walker
Auditor/Controller-Recorder
San Bernardino County
222 West Hospitality Lane, 4th Floor
San Bernardino, CA 92415-0018

Dear Mr. Walker:

The State Controller's Office audited the methods employed by San Bernardino County to apportion and allocate property tax revenues for the period of July 1, 2004, through June 30, 2006. The audit was conducted pursuant to the requirements of *Government Code* Section 12468.

Our audit disclosed that the county complied with California statutes, except that its property tax system computed new annual tax increment factors for all jurisdictions in jurisdictional change tax rate areas.

If you have any questions, please contact Jerry McClain, Chief, Special Audits Bureau, at (916) 323-1573.

Sincerely,

Original signed by

JEFFREY V. BROWNFIELD
Chief, Division of Audits

JVB/vb:ams

cc: Peggy Collins, Chief Consultant
 Joint Legislative Budget Committee
Peter Detwiler, Consultant
 Senate Local Government Committee
Elvia Dias, Assistant
 Senate Local Government Committee
Dixie Martineau-Petty, Secretary
 Assembly Local Government Committee
Martin Helmke, Consultant
 Senate Revenue and Taxation Committee
Kimberly Bott, Chief Consultant
 Assembly Revenue and Taxation Committee
Diana L. Ducay, Chief
 Office of State Audits and Evaluations
 Department of Finance
Catherine Smith, Executive Director
 California Special Districts Association

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Audit Report

Summary

The State Controller's Office (SCO) audited the methods employed by San Bernardino County to apportion and allocate property tax revenues for the period of July 1, 2004, through June 30, 2006. The last day of fieldwork was July 24, 2006.

Our audit disclosed that the county complied with California statutes for the allocation and apportionment of property tax revenues, except that its property tax system computed new annual tax increment (ATI) factors for all jurisdictions in jurisdictional change tax rate areas (TRAs).

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 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.

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 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 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 constitute sufficient “permanence” or have other intrinsic qualities to guarantee payment of taxes levied against it.
- *State-Assessed Roll*—This roll contains public utility and railroad 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, legislation (SB 418) was enacted in 1985 that requires 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 systems for apportioning and allocating property tax revenues used by the county auditor and the subsystems used by the tax collector and the assessor.

We performed the following procedures.

- Performed tests to determine whether there had been any incorrect apportionment and allocation of property tax.
- 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 redevelopment agency (RDA) reports prepared by the county and verified the computations used to develop the project base amount and the tax increment distributed to the RDA.
- 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 reports and computations prepared by the county to determine any increases in property tax revenues due cities having low or non-existent property tax amounts.

We performed our audit according to *Government Auditing Standards*, issued by the Comptroller General of the United States, and covered the period of July 1, 2004, through June 30, 2006. However, we did not audit the county's financial statements. 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.

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 disclosed that, except for the item discussed in the Finding and Recommendation section of this report, San Bernardino County complied with California statutes for the apportionment and allocation of property tax revenues for the period of July 1, 2004, through June 30, 2006. The county should correct the item discussed in the Finding and Recommendation section.

Follow-up on Prior Audit Findings

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

Views of Responsible Officials

We issued a draft audit report on November 3, 2006. Larry Walker, Auditor-Controller-Recorder, responded by letter dated December 22, 2006 (Attachment). He agreed with the audit results.

Restricted Use

This report is solely for the information and use of San Bernardino 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.

Original signed by

JEFFREY V. BROWNFIELD
Chief, Division of Audits

Finding and Recommendation

FINDING— Jurisdictional changes

The county's property tax system recomputed new annual tax increment (ATI) factors for all jurisdictions in jurisdictional changes tax rate areas (TRAs).

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

We recommend that the county properly transfer the ATI factors only for changed jurisdictions in the new TRAs and set up the property tax system so that the ATI factors can be manually input into the property tax system for jurisdictional changes.

**Attachment—
County’s Response to
Draft Audit Report**

AUDITOR/CONTROLLER-RECORDER COUNTY CLERK



COUNTY OF SAN BERNARDINO

AUDITOR/CONTROLLER • 222 West Hospitality Lane, Fourth Floor
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LARRY WALKER
Auditor/Controller-Recorder
County Clerk

ELIZABETH A. STARBUCK
Assistant Auditor/Controller-Recorder
Assistant County Clerk

December 22, 2006

Mr. Jerry McClain, Chief
Special Audits Bureau
State Controller's Office
Division of Audits
P.O. Box 942850
Sacramento, CA 94250-5874

RE: San Bernardino County

Dear Mr. McClain:

The following is our comment to the property tax audit recommendation in the draft audit report of San Bernardino County for the period from July 1, 2004 through June 30, 2006. We appreciate the opportunity to respond to the finding and recommendation before the issuance of the report.

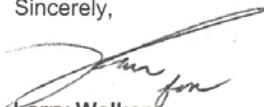
Finding: The County's property tax system recomputed the annual tax increment (ATI) factors for all jurisdictions in jurisdictional changes tax rate areas (TRAs).

Recommendation: The County should properly transfer the ATI factors only for changed jurisdictions in the new TRAs and set up the system so that the ATI factors can be manually input into the property tax system for jurisdictional changes.

Response: We agree with the State Controller's Office (SCO) finding. In the process of modifying our system to correct the findings from your prior audit, we did not anticipate that the ATI factors in new TRAs would be recomputed. Our system now has the capability to accommodate this recommendation and will be followed in the future.

If you have any questions about our response, please call Bob Wright at (909) 386-8829.

Sincerely,


Larry Walker
Auditor/Controller-Recorder

LDW:HMO:dlp

**State Controller's Office
Division of Audits
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Sacramento, California 94250-5874**

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