

# **SANTA BARBARA COUNTY**

Audit Report

## **PROPERTY TAX APPORTIONMENT AND ALLOCATION SYSTEM**

*July 1, 2005, through June 30, 2009*



**JOHN CHIANG**  
California State Controller

August 2010



**JOHN CHIANG**  
**California State Controller**

August 25, 2010

The Honorable Robert Geis, CPA, CPFO  
Auditor-Controller  
Santa Barbara County  
105 East Anapamu Street, Room 303  
Santa Barbara, CA 93102

Dear Mr. Geis:

The State Controller's Office audited the methods employed by Santa Barbara County to apportion and allocate property tax revenues for the period of July 1, 2005, through June 30, 2009. 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 it:

- Included the Educational Revenue Augmentation Fund (ERAF) in the unitary and operating nonunitary tax apportionment; and
- Deposited a portion of pass-through payments from the City of Goleta Redevelopment Agency into the ERAF and made interest payments to the Sales and Use Tax Compensation Fund and the Vehicle License Fee Property Tax Compensation Fund from the ERAF.

If you have any questions, please contact Steven Mar, Chief, Local Government Audits Bureau, at (916) 324-7226.

Sincerely,

*Original signed by*

**JEFFREY V. BROWNFIELD**  
Chief, Division of Audits

JVB/vb

cc: Janet Wolf, Chairwoman  
Board of Supervisors, Santa Barbara 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

# Contents

## **Audit Report**

<b>Summary</b> .....	1
<b>Background</b> .....	2
<b>Objective, Scope, and Methodology</b> .....	3
<b>Conclusion</b> .....	4
<b>Follow-Up on Prior Audit Findings</b> .....	5
<b>Views of Responsible Official</b> .....	5
<b>Restricted Use</b> .....	6
<b>Findings and Recommendations</b> .....	7
<b>Attachment—County’s Response to Draft Audit Report</b>	

# Audit Report

## Summary

The State Controller's Office (SCO) audited the methods employed by Santa Barbara County to apportion and allocate property tax revenues for the period of July 1, 2005, through June 30, 2009.

Our audit disclosed that the county complied with California statutes for the allocation and apportionment of property tax revenues, except that it:

- Included the Educational Revenue Augmentation Fund (ERAF) in the unitary and operating nonunitary tax apportionment; and
- Deposited a portion of pass-through payments from the City of Goleta Redevelopment Agency into the ERAF and made interest payments to the Sales and Use Tax Compensation Fund and the Vehicle License Fee Property Tax Compensation Fund from the ERAF.

Additionally, we noted the following observation.

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

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 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 in Los Angeles County filed suit against the county. On June 2, 2009, the court referee determined that the method used by Los Angeles County was correct.
- In the second action, filed in Fresno County, seven cities filed suit against the county. 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.

The SCO will make a determination on the computation of the PTAF at such time as appeals (if any) are resolved.

## 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 have 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:

- 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 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.

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, 2005, through June 30, 2009. 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 items discussed in the Findings and Recommendations section of this report, Santa Barbara County complied with California statutes for the apportionment and allocation of property tax revenues for the period of July 1, 2005, through June 30, 2009. The county should correct the items discussed in the Findings and Recommendations section.

Additionally, we noted the following observation.

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 the services performed by the county under Revenue and Taxation Code sections 97.68 and 97.70. Pursuant to Revenue and Taxation Code section 97.75, for FY 2006-07 and thereafter, a county may impose a fee, charge, or other levy on a city for these services, but the fee, charge, or other levy cannot exceed the actual cost of providing the services.

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 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 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 in Los Angeles County filed suit against the county. On June 2, 2009, the court referee determined that the method used by Los Angeles County was correct.
- In the second action, filed in Fresno County, seven cities filed suit against the county. 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.

The SCO will make a determination on the computation of the PTAF at such time as appeals (if any) are resolved.

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

The county has satisfactorily resolved the findings noted in our prior audit report, issued October 31, 2006.

### **Views of Responsible Officials**

We issued a draft audit report on May 27, 2010. Robert W. Geis, Auditor-Controller, responded by letter dated June 17, 2010. The county disagreed with Finding 1. With regards to Finding 2, the county disagreed with our recommendation to not deposit pass-through payments from any RDA in the ERAF and concurred that interest earned on SUT/VLF transfers while in the ERAF should remain in the ERAF. The county's response is attached.

**Restricted Use**

This report is solely for the information and use of Santa Barbara 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

August 25, 2010

# Findings and Recommendations

## **FINDING 1— ERAF included in unitary and operating nonunitary**

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 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 realize the current position of the SCO is that the ERAF is not to receive Unitary apportionments. We also note that this position is contrary to the SCO’s previous position published in the February 2001 audit report to Marin County in which the SCO required that county to include the ERAF in the Unitary apportionment.

We understand that the basis for the SCO’s current position is that the ERAF is not a taxing jurisdiction. However, the courts were asked in 1994 whether the ERAF was allowed to receive annual tax increments as the ERAF was not defined as a taxing jurisdiction. The courts opined in *San Miguel Consolidated Fire Protection Dist. v. Davis* 25 Cal.App.4<sup>th</sup> 134 (1994) that since school districts (which are defined as jurisdictions) are beneficiaries of the ERAF monies that it was proper to allocate annual tax increments to the ERAF.

“FN 19. Petitioners also contend annual tax increments may only be allocated to “jurisdictions”—a term which petitioners contend does not encompass the Educational Revenue Augmentation Funds Section 95, subdivision (b), includes cities, counties, special districts, school districts, community college districts, and county superintendents of schools within the definition of “jurisdiction.” The beneficiaries of the Educational Revenue Augmentation Funds are school districts, county offices of education, and community college districts. (§97.03, subd. (d)(1).) Annual tax increments are initially allocated to the special districts, which are specifically included within the “jurisdiction” definition, and a percentage is then subsequently reallocated by the county auditors to the Educational Revenue Augmentation Funds for the benefit of the school districts. We find no statutory prohibition to this procedure.”

We believe this court decision has merit in the analysis of this issue, but as we requested but were denied copies of the SCO legal analysis on their position, we are unable to learn how this point was addressed. Accordingly, until this court decision has been addressed and in addition to the other arguments presented by other counties in their audit report responses, we believe that our current method which is described in the *Property Tax Managers’ Reference Manual* published by the County Auditor’s Association of California is correct and allowed by law. We will implement any changes to our process should the *Property Tax Managers’ Reference Manual* be revised in the future.

#### 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, Revenue and Taxation Code section 95(b) defines a jurisdiction as a “local agency, school district, community college district, or county superintendent of schools. A jurisdiction as defined in this subdivision is a ‘district’ for purposes of Section 1 of Article XIII A of the California Constitution.” Furthermore, Revenue and Taxation Code section 100(e)(3) includes a redevelopment

agency as a taxing jurisdiction. This section demonstrates that the Legislature knows how to include non-taxing entities in the definition of taxing jurisdiction if it so desires. In this case, the Legislature omitted the ERAF from the definition of taxing jurisdiction.

In its response to the finding, the county includes, and places reliance on, footnote 19 from *San Miguel Consolidated Fire Protection District v. Davis* 25 Cal. App. 4<sup>th</sup> 134 (1994). The county states that the court opined in the case “that since school districts (which are defined as jurisdictions) are beneficiaries of the ERAF monies that it was proper to allocate annual tax increments to the ERAF.”

The court stated in the above footnote: “. . . Annual tax increments are initially allocated to the special districts, which are specifically included within the ‘jurisdiction’ definition, and a percentage is then subsequently reallocated [emphasis added] by the county auditors to the Educational Revenue Augmentation Fund for the benefit of the school districts.” We find no statutory prohibition to this procedure.

We acknowledge that, 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.

Finally, the Property Tax Manager’s Reference Manual is a guide, not a statute. We perform audits according to applicable statutes. 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.

**FINDING 2—  
Educational Revenue  
Augmentation Fund**

A portion of the mandatory pass-through payments made by the City of Goleta Redevelopment Agency were deposited by the county in the ERAF, a non-affected taxing entity.

In addition to making required payments to the Sales and Use Tax Compensation Fund (SUT) and Vehicle License Fee Property Tax Compensation Fund (VLF), the county made interest payments to these funds from the ERAF.

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

The county should not deposit in the ERAF pass-through payments from any redevelopment agency, as the ERAF does not meet the definition of an affected taxing entity.

Additionally, the county should not make payments in excess of the required amounts to the SUT and VLF funds.

#### County's Response

##### ERAF Deposits for Pass-through Payments

We believe this finding is directed incorrectly to the Auditor-Controller rather than to the RDA that submitted the pass-through payment, as the RDAs themselves not this office are responsible for the calculation of any statutory RDA pass-through payments.

As previously reported to the SCO under the AB1389 reporting process, our office noted that RDAs within the county were treating the ERAF differently for purposes of pass-through payment calculations, with one RDA making pass-through payments to the ERAF and the other reallocating the ERAF's share proportionally to the other affected taxing entities. As part of the AB1389 process we asked the SCO whether this was appropriate and were told that the SCO did not have an answer on how to address the ERAF share, that this was also noted at other counties and that to report it as an observation rather than a finding due to the uncertainty of the correct treatment. During the audit we were also told that SCO did not have an answer as to the correct treatment of the ERAF's share other than the ERAF was not to receive a pass-through payment.

We also note that the *Los Angeles Unified School District v. County of Los Angeles* 181 Cal. App. 4<sup>th</sup> 414 (2010) case may impact the distribution of statutory pass-through payments in many counties. Accordingly, we believe that this comment should be redirected to the RDAs once the SCO can provide guidance on how to treat the ERAF's share taking into consideration the impacts of the *Los Angeles Unified School District v. County of Los Angeles* case noted above.

##### Interest payments to SUT and VLF fund

We concur that interest [sic] earned on the SUT and VLF transfers while in the ERAF should be retained in the ERAF and not distributed to the SUT and VLF. Corrections to our process were made during the course of the audit.

SCO's Comment

Our finding and recommendation remain unchanged.

We concur that the redevelopment agency is responsible for making the statutory pass-through payments. However, it is the county's responsibility to ensure the proper accounting for and distribution of funds received by the ERAF. The ERAF is a fund, not an affected taxing agency. The county noted in its response that some redevelopment agencies in the county were treating the pass-through payments differently. The county should have returned the ERAF pass-through payment to the redevelopment agency to be held in trust or should have held the money in trust in the county treasury until the matter is resolved.

The county quoted *Los Angeles Unified School District v. County of Los Angeles* 181 Cal. App. 4<sup>th</sup> 414 (2010). However, this case does not appear to address whether the ERAF is to receive a share of the pass-through payments. The court held that the redevelopment agency must, with noted exceptions, include as property taxes received the amount of the ERAF the local education agency received when it is computing pass-through shares. This increases the share of pass-through revenue the local education agency receives while decreasing the pass-through for all other affected taxing agencies.

As the ERAF does not meet the definition of an affected taxing agency, the county should not deposit in the ERAF pass-through payments from any redevelopment agency.

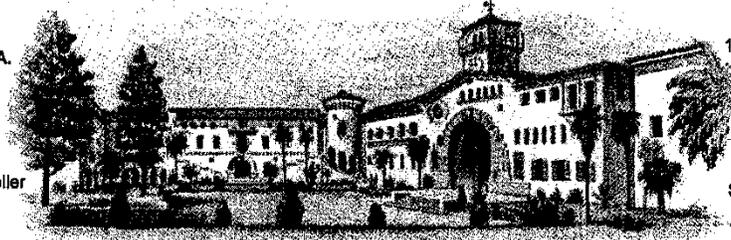
**Attachment—  
County’s Response to  
Draft Audit Report**

---

# COUNTY OF SANTA BARBARA

Robert W. Gels, C.P.A.  
Auditor-Controller

Theo Fallati, C.P.A.  
Assistant Auditor-Controller



Administration Building  
105 E. Anapamu Street, Rm. 303  
Santa Barbara, CA 93101  
(805) 568-2100

Mailing Address:  
P.O. Box 39  
Santa Barbara, CA 93102-0039  
Fax (805) 568-2016

## Office of the Auditor-Controller

VIA FACSIMILE and USPS

June 17, 2010

Steven Mar  
Chief, Local Government Audits Bureau  
California State Controller Office  
Division of Audits  
P. O. Box 942850  
Sacramento, CA 94250-5874

Dear Mr. Mar:

We have reviewed the draft report of the audit of the Property Tax Apportionment and Allocation System of Santa Barbara County for the period July 1, 2005 through June 30, 2009 and have the following responses:

### **Finding 1 – Unitary and Operating Nonunitary Apportionment**

We realize the current position of the SCO is that the ERAF is not to receive Unitary apportionments. We also note that this position is contrary to the SCO's previous position published in the February 2001 audit report to Marin County in which the SCO required that county to include the ERAF in the Unitary apportionment.

We understand that the basis for the SCO's current position is that the ERAF is not a taxing jurisdiction. However, the courts were asked in 1994 whether the ERAF was allowed to receive annual tax increments as the ERAF was not defined as a taxing jurisdiction. The courts opined in *San Miguel Consolidated Fire Protection Dist. v. Davis* 25 Cal.App.4th 134 (1994) that since school districts (which are defined as jurisdictions) are beneficiaries of the ERAF monies that it was proper to allocate annual tax increments to the ERAF.

"FN 19. Petitioners also contend annual tax increments may only be allocated to "jurisdictions"-a term which petitioners contend does not encompass the Educational Revenue Augmentation Funds. Section 95, subdivision (b), includes cities, counties, special districts, school districts, community college districts, and county superintendents of schools within the definition of "jurisdiction." The beneficiaries of the Educational Revenue Augmentation Funds are school districts, county offices of education, and community college districts. (§ 97.03, subd. (d)(1).) Annual tax increments are initially allocated to the special districts, which are specifically included within the "jurisdiction" definition, and a percentage is then subsequently reallocated by the county auditors to the Educational Revenue Augmentation Funds for the benefit of the school districts. We find no statutory prohibition to this procedure."

We believe this court decision has merit in the analysis of this issue, but as we requested but were denied copies of the SCO legal analysis on their position, we are unable to learn how this point was addressed. Accordingly, until this court decision has been addressed and in addition to the other arguments presented by other counties in their audit report responses, we believe that our current method which is described in the *Property Tax Managers' Reference Manual* published by the County Auditor's Association of California is correct and allowed by law. We will implement any changes to our process should the *Property Tax Managers' Reference Manual* be revised in the future.

## **Finding 2 – Education Revenue Augmentation Fund**

### **ERAF Deposits for Pass-through Payments**

We believe this finding is directed incorrectly to the Auditor-Controller rather than to the RDA that submitted the pass-through payment, as the RDAs themselves not this office are responsible for the calculation of any statutory RDA pass-through payments.

As previously reported to the SCO under the AB1389 reporting process, our office noted that RDAs within the county were treating the ERAF differently for purposes of pass-through payment calculations, with one RDA making pass-through payments to the ERAF and the other reallocating the ERAF's share proportionally to the other affected taxing entities. As part of the AB1389 process we asked the SCO whether this was appropriate and were told that the SCO did not have an answer on how to address the ERAF share, that this was also noted at other counties and that to report it as an observation rather than a finding due to the uncertainty of the correct treatment. During the audit we were also told that SCO did not have an answer as to the correct treatment of the ERAF's share other than the ERAF was not to receive a pass-through payment.

We also note that the *Los Angeles Unified School District v. County of Los Angeles* 181 Cal. App. 4<sup>th</sup> 414 (2010) case may impact the distribution of statutory pass-through payments in many counties. Accordingly, we believe that this comment should be redirected to the RDAs once the SCO can provide guidance on how to treat the ERAF's share taking into consideration the impacts of the *Los Angeles Unified School District v. Los Angeles County* case noted above.

Interest payments to SUT and VLF fund

We concur that interest earned on the SUT and VLF transfers while in the ERAF should be retained in the ERAF and not distributed to the SUT and VLF. Corrections to our process were made during the course of the audit.

We appreciate the opportunity to address the proposed findings as well as the value provided to the public by the SCO's audit of the property tax apportionments.

Sincerely,

A handwritten signature in black ink, appearing to read "Robert W. Geis". The signature is fluid and cursive, with a large initial "R" and "G".

Robert W. Geis, C.P.A.

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

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