ERAF Background Provided by Santa Clara County

During the early 1990s, the state experienced an economic recession and budget shortfalls. To help balance the budget, the state permanently redirected almost one-fifth of statewide property tax revenue from cities, counties, and special districts to schools and community colleges. The redirected property tax revenue is deposited into an account in the county treasury known as Educational Revenue Augmentation Fund (ERAF). Initially, the operation of these accounts was relatively straightforward—all the property tax revenue was distributed to schools and colleges within the county to offset revenue they would otherwise receive from the state General Fund. By increasing property tax revenue to schools, the ERAF shifts reduced the amount of General Fund needed to meet the Proposition 98 guarantee. Basic aid districts did not receive any allocations from ERAF because they received no General Fund revenue the state could offset.

Five counties in California – Santa Clara, Marin, Napa, San Francisco, and San Mateo have more than enough funding in ERAF to offset all the General Fund its schools would receive from the state. Some of these funds are used for special education programs and the remainder are allocated to other agencies in the county, including the county government, cities, and special districts. The ERAF funds allocated to noneducation agencies through this process are known as excess ERAF. An agency's share of excess ERAF is proportional to the share of its property tax revenue originally shifted into ERAF. The agencies receiving excess ERAF may use it for any local purpose.

In February 2019, the Excess ERAF counties learned that there were some inconsistencies in the methodologies they were employing to determine their ERAF calculations. For more than a year, the counties have been engaged in conversations with their respective county offices of education as well as among themselves with the goal of identifying a reliable, consistent, and mutually-understood methodology that could be used by all counties, the State Controller, and other state agencies when calculating ERAF entitlements to school districts. Subsequently, in January 2020, conversations transpired between the local county offices of education, the Department of Education (CDE), the State Department of Finance (DOF), and the Legislative Analyst's Office (LAO) without any engagement with the auditor-controllers.

On March 6, 2020, the LAO issued a report titled "Excess ERAF: A Review of the Calculations Affecting School Funding" ("LAO Report"). The LAO Report contains several major misrepresentations, does not explain how or why the counties' ERAF calculations fail to comply with the law, and makes the unfounded accusation that County auditor-controllers are trying to maximize revenues to certain entities resulting from a purported lack of State oversight over the ERAF process. The report also does not mention that the State Controller's Office (SCO) conducts regular audits of the counties' property tax distributions and has never found any problems with regard to the counties' ERAF distributions, and has never concluded that the counties have acted in bad faith in calculating school district ERAF entitlement amounts.

A provision in the Education Omnibus Trailer Bill with May Revision Amendments would amend Revenue and Taxation Code section 97.2 to add a new subsection (d)(2)(B) to impose civil penalties and provide the Department of Finance with a punitive mechanism against the counties.

The State Controller's Office (SCO) is the State agency granted the authority to oversee the county auditor-controllers, through its duties from the State Constitution, statutory authority, and its historical role and expertise in auditing and issuing guidance regarding property taxes. By usurping the duties and responsibilities of the SCO, and delegating that role to the Department of Finance (DOF), this legislation deprives the voters of their right to elect an independent official to oversee the tax collection and distribution of State and local revenue for thousands of governmental entities.

The proposed changes are an attempt to shift funds to assist the State budget and are done in a manner that would punish the counties retroactively, suggesting that the Counties purposely disregarded clear guidance to the contrary. Such guidance was never provided, and, in fact, the counties were attempting to obtain the legal basis for the DOF's position until those efforts were interrupted by the COVID-19 pandemic.