

PART VI

FINANCE, BUDGETING AND DEBT

CHAPTER 21: MUNICIPAL BUDGETING

Chapter 21: Municipal budgeting.....	3
I. Public versus private budgeting.....	3
II. Budgeting basics and funds.....	4
III. Municipal budget is a plan	5
A. Budget cycle	5
IV. Budget as a communication tool	7
A. Explain city financial conditions in budget documents.....	8
B. Tie budgeting to goals in budget documents.....	8
C. Foster citizen involvement in budget process.....	8
D. Link citizen input to budget decisions.....	9
E. Use the budget to communicate the value of government.....	9
V. Budget structures	9
VI. Revenues.....	10
A. Tax revenue	10
B. Franchise fees	11
C. License and permit revenue.....	11
D. Intergovernmental revenue	12
E. Charges for services	14
F. Public safety revenue.....	14
G. Culture and recreation	14
H. Enterprise funds.....	14
I. Penalty charges.....	14
J. Special assessment revenue	14
K. Miscellaneous revenues.....	15
L. Other revenue	15
VII. Expenditures	15
A. General government	15
B. Public safety	16
C. Culture-recreation.....	16
D. Conservation of natural resources	16
E. Debt service.....	16
F. Miscellaneous expenditures.....	17
VIII. Capital improvements.....	17

IX. Other regulations impacting municipal budgets17

 A. GASB 17

 B. State auditor reports..... 18

 C. Truth in taxation 18

X. Plan B cities18

XI. Standard plan cities.....18

XII. Charter cities.....19

XIII. Conclusion 19

Chapter 21: Municipal budgeting

City budgets are not just financial documents. Done thoroughly, they reflect city plans, policies and goals regarding services and sound resource management. Simply adopting last year's budget is not acting in the city's best interest. Instead, consider goals, what programs and services citizens want in the city and then look to sustaining or allocating funding for those goals. The budget document is an important communication tool revealing a city's plan for the coming year. Cities are under great pressure to streamline operations and meet strict financial standards at the same time. In the current economy, with dropping market values and loss of local government aid, sustainability is an overarching concern for cities. Budgeting is the vehicle to sustain cities in this extremely difficult economy.

I. Public versus private budgeting

[Minn. Stat. § 412.221.](#)

A city is a municipal corporation but budgeting in the public sector is very different than it is in the private sector. The table below illustrates some of the major differences in terms of scope, law, and process.

CITIES	PRIVATE OR NON-GOVERNMENTAL ORGANIZATIONS (NGOS)
Provide services and programs for the entire community.	Provide services to a discreet set of customers.
Budgets focus on public safety and well-being of the community as a whole.	Private companies allocate money to meet shareholders or owners expectations for profit.
Must fund a wide variety of activities from safe roads and clean water to economic development.	Focus spending on narrowly defined programs or services.
Subject to a significant number of state and federal mandates or laws that legally require cities to provide certain services but do not provide funding for them. For example, federal law requires cities to manage storm water but does not fund the costs of those requirements.	Not subject to such extensive and numerous legally binding mandates that require both provision and levels of service.
Must not borrow money from a bank but issue debt in the form of general obligation bonds to build public infrastructure such as roads and bridges.	Obtain funds by borrowing money to build or improve their business or buildings.
Use taxing authority to raise funds to provide services and programs often at or below cost.	Charge for services or programs at a cost that includes a profit.
Prepare budgets in public and include the public in the process and in the final product. Minn. Stat. § 471.6965.	Prepare budgets in private with no public participation.
Information on budget decisions, city revenue and expenditures is public data, done in public.	Detailed budget decisions and information on private companies is not public and done in private.

CITIES	PRIVATE OR NON-GOVERNMENTAL ORGANIZATIONS (NGOS)
City councils must make budgeting decisions by consensus.	Non-governmental organizations often vest decision-making authority in one person.
Competing interests are a given when cities prepare budgets.	Fewer competing interests - making a profit and/or being competitive is typically the focus.
Must budget for services in good and bad markets based on community needs, goals and objectives.	Make budget decisions based on competition with other businesses and on market conditions.
Subject to stringent and comprehensive financial controls and public reporting to prevent mismanagement and misuse of public funds.	Not subject to accounting and financial controls or public scrutiny of funds and spending activities.

II. Budgeting basics and funds

[Minn. Stat. § 6.745.](#)

[Minn. Stat. § 471.6965.](#)

See Sections X-XII, *Plan B cities, Standard plan cities, Charter cities.*

[Minn. Stat. § 471.696.](#)
[Handbook, Chapter 26.](#)

Budgeting is basically planning and prioritizing goals for the coming year based on experiences in the past year or years. All cities are required to prepare and adopt an annual budget. By law in Minnesota, the fiscal year of a city and all of its funds must be the calendar year. Thus, for cities, a budget is one year of estimated money coming in, or revenue and expenditures or money going out. Note: Cities organized under Plan B form of government, and cities with home rule charters, special laws, local ordinances or unique circumstances may have additional or special budgeting requirements and considerations.

A city budget is a comprehensive financial plan for one year. It is a snapshot in time of city activities and services supported by discreet city funds for the coming year. In governmental accounting terms a “fund” is a sum of money set aside for a specific purpose -- not necessarily a separate bank account -- but tracked on paper separately. The three basic city fund types are:

Governmental funds ----used to finance most governmental services and based on tax revenues, special assessments or issuing debt. The cities general fund, debt service funds (to pay off bonds), and capital project funds are examples of governmental funds.

Proprietary funds ---financing for governmental activities operating like a private business, for example, water and sewer utilities, electrical utilities or municipal liquor stores. Service charges usually provide most of these funds.

Fiduciary funds ----trust and agency funds used to account for assets a city holds in a trustee capacity or as an agent, for example, pension funds. Fiduciary funds cannot be used to support the city’s own programs.

See Sections VI and VII, *Revenues and Expenditures.*

See the state auditor’s [Uniform Chart of Accounts.](#)

The Office of the State Auditor (OSA) provides the Uniform Chart of Accounts to facilitate the preparation of uniform annual financial statements. The outline of accounts may also serve as a useful checklist when preparing city budgets. Every city should consult this chart when preparing the annual budget and maintaining financial records. The OSA recommends the adoption of the uniform account numbering system for all cities, including cities under 2,500 in population, whenever practical.

Government Finance Officers Association: See p. 5-6 for all Minnesota recipients of the [Distinguished Budget Award 2007](#) (Annual Report for Fiscal Periods Beginning 2006).

Preparing city budgets involves policy decisions about the use of money and it helps cities make important decisions - tying funding to specific goals set by the council. During the budgeting process, city council members and staff look back to what programs and services worked the previous year and they look forward to what city activities may be changed, dropped or increased in the coming year.

III. Municipal budget is a plan

To make a useful municipal budget, examine all city services and programs, for example, fire fighting services, police protection services, water and sewer services, holding elections, park and recreation programs, park maintenance, snowplowing, and any other city funded activity. Include personnel costs, office supplies, computers, software, building and maintenance supplies fuel costs and any other equipment. These are the current expenditures. Next look at money coming in, or revenue, from all sources. As explained in more detail below, property taxes are the largest source of revenue for cities. In order to balance the budget, total estimated revenues must be equal to or exceed total estimated expenditures. The budget sets out a council's yearly plan to maintain, change, add or drop services and activities.

See state auditor's Statement of Position: [Fund Balances for Local Governments](#)
[City Fund Balances 101](#).

Planning a city budget includes a fund balance, or unrestricted money available to cover unexpected costs. The state auditor recommends but does not require that cities keep a minimum of five months' operating costs on hand and accessible to cover such unanticipated costs. Some city councils believe that higher fund balances provide more protection against unforeseen emergencies.

See Section VIII, *Capital Improvements*.

Cities often budget and plan separately for capital improvements because the process covers more than one year. Capital improvements includes planning for replacing, repairing and maintaining infrastructure such as streets, sidewalks, water and sewer systems, transportation, buildings and parks. Planning for future infrastructure costs is essential. Without it, cities run the risk of costly emergency repairs to local infrastructure.

A. Budget cycle

See [Budget Process](#), City of Hopkins. Winner of both GFOA Budget Award and Certificate of Achievement in Financial reporting Program Award.

The process of annual budget preparation occurs within the framework of the state property tax system. Property taxes are generally the primary revenue source for Minnesota cities. Each fall, cities submit their property tax levies for the following year to the county auditor. Counties are responsible for property tax administration; the state Department of Revenue provides assistance and oversight.

See Section VI, *Revenues*.

Minnesota cities also participate in revenue sharing and property-tax-relief programs known as local government aid (LGA) and market value homestead credit (MVHC). LGA supplements property tax revenue; MVHC reimburses property tax revenue taken by a state homestead credit.

See Section IX.C, *Truth-in-Taxation*.

Cities must prepare and adopt proposed budgets and proposed property tax levies each year. Cities over 500 in population with more than nominal proposed property tax increases are required to provide notice of the proposed budget adoption and to hold public hearings on the proposed budget and property tax levy. The "truth-in-taxation" (TNT) process is described later in this chapter.

Minn. Stat. § 477A.014.

Minn. Stat. § 275.74, subd. 1.

Minn. Stat. § 275.065, subd. 1(a).

Minn. Stat. § 275.065, subd. 6.

Minn. Stat. § 275.07.

Cities generally prepare budgets in the summer with the following due dates:

On or before Aug. 1: The Department of Revenue notifies cities of state aid amounts.

On or before Sept. 1: The Department of Revenue notifies cities of the applicable levy limit, if any.

On or before Sept. 15: Cities must adopt their proposed budget and certify their proposed levy to the county auditor. Note: Once cities certify a *proposed* levy in September they may decrease the amount when they certify a *final* levy in December -- but may not increase it.

Between Nov. 29 and Dec. 20: The TNT public comment hearings, if required, must occur.

On or before five working days after December 20 in each year: Cities must adopt a final tax levy and certify that final property tax levy to the county auditor.

Minn. Stat. § 477A.015.

Minn. Stat. § 273.1384, subd. 4.

See also, *Dates for City Budgets 101: State aid and Credit Programs Property Tax System*.

Cities generally receive various property tax revenues and state aid as follows:

The first in June and the second in December: The county treasurer distributes property tax revenues to cities in two payments.

On or around July 20 and Dec. 26 each year: The state distributes LGA payments to cities in two equal installments.

On Oct. 31 and on Dec. 26: Cities receive half of their MVHC reimbursement (if any) on each of these dates.

City budgeting never stops. While city councils and staff are preparing new annual city budgets, they are also tracking and reviewing the current year's revenues and expenditures. As cities implement a new year's budget, they are also auditing and reporting on the past year's expenditures. Preparation, approval, implementation, and audit review comprise the ongoing budget cycle.

1. Budget preparation

"City Solutions," *Minnesota Cities* (Nov.-Dec. 2008 p. 8)

Cities begin budget preparations in May or June, examining current economic trends, as well as all revenue sources and expenditures and proposing increases or decreases accordingly. City staff collects budget information and present it to the council at meetings, where interested citizens may participate. The goal of budget preparation is to balance all revenues and expenditures, prioritize capital improvements, and appropriately manage outstanding debt.

2. Budget approval

Minn. Stat. § 275.07, subd. 1.

See Section VI, A 2. *Setting the property tax levy within limits*.

By law in Minnesota, the fiscal year of a city and all of its funds is the calendar year. By December of each year cities determine their financial condition showing a freeze frame in time of all money flowing in and out of the city, outstanding city debt and financing for needed capital improvements. Cities adopt a new budget late in December to begin in January of the coming year.

3. Budget implementation

See state auditor's Statement of Position: [Internal Controls](#).

See state auditor's Statement of Position: [Petty Cash \(Imprest\) Funds](#).

See state auditor's Statement of Position: [Credit Card Use and Policies](#).

City councils must monitor the current budget, directing how staff accounts for expenditures and revenues. One important step is for council to adopt a policy on internal controls, meaning that the council sets the rules to prevent misuse of public money. For example, if at all possible, the same person should not be taking in money and paying it out. This 'segregation of duties' is part of a policy on internal control and budget implementation crucial to appropriate use of public funds. Policies on the use of petty cash (known as imprest funds in financial jargon) and a policy on credit card use also helps protect cities from loss or misuse of public funds.

4. Budget audits

[Minn. Stat. § 471.697, subd. 1. Minn. Stat. § 412.591, subd. 2. Minn. Stat. § 412.02, subd. 3. Handbook, Chapter 26](#)

City councils must audit budgets, depending on the size and structure of the city. At a minimum, a city with a population of 2,500 or less and a combined clerk/treasurer must have an annual audit for 2010 if its annual revenue is greater than \$178,000. A city with a combined clerk/treasurer and annual revenue of \$178,000 or less must have an audit once every five years and the person doing the auditing will select the year to be audited. A city with a population over 2,500 must have an annual audit performed.

5. Budget amendments

City budgets are not set in stone. Many cities must revise their original budgets over the course of the year for a variety of reasons. Amending the budget is not illegal nor is it necessarily undesirable. Typically, city councils simply note the reason for amending the city budget (the city receives a grant, a piece of equipment fails, etc.) and adopt the amendment in a resolution.

[Minn. Stat. § 412.731.](#)

See Section X: *Plan B cities*.

However, in Minnesota's 16 Plan B cities, resolutions reducing amounts in the budget or authorizing transfers from unencumbered balances must pass by a four-fifths vote of all the members of the council.

[Preface and summary of GASB Statement No. 34](#)

[2008 City of Farmington, CAFR. Winner of the GFOA Budget Award for 10 years.](#)

For cities over 2500 in population, the Governmental Accounting Standards Board (GASB) requires that cities include the original budget and budget amendments in budget reports, such as the comprehensive annual financial report (CAFR).

IV. Budget as a communication tool

[City of Cottage Grove, Where Do My Tax Dollars Go?](#)

[City of Burnsville, 2010 Budget – Understanding Your TNT Statement.](#)

City council members, as policy makers, must understand budget documents. And making a city budget understandable to citizens is not easy. The scope and complexity of city budgeting also makes citizen participation difficult; citizens may focus on one area and advocate for budget cuts or expenditures that are not fiscally prudent. Using the budget process and product to communicate, showing what services resident tax dollars fund is one way to make budgeting meaningful for council members and residents.

A. Explain city financial conditions in budget documents

City of Richfield, [Comprehensive Annual Financial Report \(CAFR\) 2008: Factors Affecting Financial Condition](#), p. 4. Winner of both GFOA Budget Award and Certificate of Achievement in Financial reporting Program Award.

City of Mankato, [2010 Preliminary Budget: Budget Challenges](#).

Citizens have a sense of the current economy, but many people may not understand how the recession impacts city budgets. City council members also need to look at the city budget in light of state and federal economic conditions. In the budget documents, explain which of these state and local challenges affects your city:

- Falling or stalling real estate markets which lower market value estimates and thus tax revenues.
- The current low interest on bonds allowing refinancing and paying off old bonds thus saving on interest payments.
- The cuts in aid from the state (local government aid and market value homestead credit).
- Low interest rates on city investments.
- Rapidly increasing unpaid water and sewer charges.
- Foreclosures.
- High unemployment.
- Abandoned or vacant properties.

City budget documents build on the past year and project into the coming year. Communicating an accurate picture of the city's financial condition helps citizens and council develop strategies to sustain the city.

B. Tie budgeting to goals in budget documents

White Bear Lake [2009 Annual Budget](#), Winner of both GFOA Budget Award and Certificate of Achievement in Financial reporting Program Award.

Citizens support goals not just expenditures. For example, all cities share the critical responsibility to hold elections. One city sets a goal in the annual budget to “continue providing efficient and friendly non-partisan voter registration, absentee, and election Day services” and tracks everything related to that goal in the annual budget document. Citizens are therefore able to understand and support the city's expenditures related to elections.

C. Foster citizen involvement in budget process

City of Northfield, [Minn. Stat. § 275.065, subd. 1e](#).

City of Minnetonka.

City of Hopkins, [City Budget Process](#). Winner of both GFOA Budget Award and Certificate of Achievement in Financial reporting Program Award.

City of Worthington, [Budget Information](#). Winner of the GFOA Distinguished Budget Presentation Award.

Many cities use citizen surveys to determine city priorities and guide budget decisions about the level of city services provided. Given the extreme stress on city budgets in the current economy and the expenses of a city-wide survey, a number of cities seek citizen input on the city budget simply by providing a way to submit ideas, questions or comments about the budget through the city website. Cities may also seek citizen input from targeted discussion groups, advisory boards and public meetings during the development of the budget. Even though allowing citizen participation is required in cities with population over 500 (by the truth in taxation law) it occurs late in the budget cycle. Cities may wish to publicize the budget process or calendar to encourage citizen participation earlier in the year.

D. Link citizen input to budget decisions

White Bear Lake 2009 Annual Budget, Winner of both GFOA Budget Award and Certificate of Achievement in Financial reporting Program Award.

Once a city engages citizens in the budgeting process, include that participation and comments in the budget documents. For example, if many citizens comment on the need to revitalize certain commercial or residential areas of the city, include the comments and actions that the city council takes on that issue in the budget document, even if it is a preliminary plan to investigate revenue related to revitalization. Citizens must see how their involvement impacts the city's budget process and plan.

E. Use the budget to communicate the value of government

Tax Value Illustration from Lenexa, Kansas

City of Cottage Grove, [Where Do My Tax Dollars Go?](#)

Easy to understand information on what programs and services a city tax dollar supports helps citizen understand the value of government and city budgets. City budgets necessarily focus on the overall cost of a service, for example, police protection. But looking at city budgets from the opposite end---how much tax revenue comes into the city from each home and all the services those dollars support----shows a more accurate picture of the value of city services to residents.

City Expenditures chart

Over the years, statistics show that cities in Minnesota consistently spend more on public safety and public works than in any other category. Use the city budget to show citizens that their tax dollars support public safety and safe water.

V. Budget structures

See [Additional Information on Budget Structures](#)

Most cities approach budgeting using a particular format. The most common budget techniques cities use include the following formats:

Line item budgets: the simplest budgeting structure showing each expenditure on a separate line.

Program budgets: presents budgeting information around particular programs instead of simple line item expenditures.

Performance budgets: rather than just expenditures, includes service goals and objectives, and measures outcomes related to expenditures.

Zero-based budgets: starts with funding city services at a minimum level and working up from there to a level of funding that councils agree is appropriate for each city service.

Many city budgets contain a mix of these formats. The format is simply a way to present information on expenditures so that city councils may decide which services the city will fund, and at what level, for the coming year.

LMC City Pro Financial Planning Tool
Fund Balance Policy.
Financial Management Policy.

The League's *City Pro Financial Planning Tool* may be helpful when preparing city budgets. The League and its Small Cities Financial Viability Task Force partnered with Springsted Incorporated's financial advisors to develop this affordable, easy-to-use tool. City staff enters current budgets and financial data, and City Pro projects up to 10 years of future revenues, expenditures, costs of capital improvements, and fund balances. City Pro calculates the tax rate necessary to support projected needs, giving city staff and elected officials a sound basis for long-range planning and decision making regarding future service delivery capacity. The League's staff also worked with Ehlers and Associates to develop five sample financial documents two of them relating to city budgets.

City Revenues chart

Minn. Stat. § 410.32 and
Minn. Stat. § 412.301.

Minn. Stat. § 297A.99, subd. 1.

City of Hopkins 2009 Revenue Summary Graph. Winner of both GFOA Budget Award and Certificate of Achievement in Financial reporting Program Award.

VI. Revenues

City budgets start with a picture of revenue (money coming in). Minnesota law greatly restricts the available types of local revenue sources. Unlike some other states, local governments in Minnesota may not impose an income tax. In addition, without specific legislative authority, cities may not impose a local sales tax and those that have been granted are usually for specially designated purposes. (Currently, a city may not advertise, promote, expend funds or hold a referendum to support imposing a local option sales tax.)

Understanding where city funds come from is the first step in developing a budget plan. Of course for many cities unallotment and levy limits, discussed later, pose serious challenges to the reliability of city revenue streams. Based on the state auditor's uniform chart of accounts, revenue for most cities includes money from the following 13 categories.

A. Tax revenue

Minn. Stat. ch. 275; Minn. Stat. § 282.08Minn. Stat. § 216B.025; Minn. Stat. § 276.131; Minn. Stat. § 349.213 Minn. Stat. § 469.190.

Tax revenue includes current property taxes; delinquent property taxes; apportionments from tax forfeit sales; franchise and public utility taxes; and city sales, gambling, and local lodging taxes, if any. Cities in Minnesota receive a variety of shared tax revenue, or general state aid, from the state. Amounts for each city are typically available from the Minnesota Department of Revenue on or before Aug. 1 of each year.

1. Property tax revenue

Property Tax 101.

See [Additional Information on Sources of Revenue](#).

Excerpts from the state auditor's *Accounting Manual for Small Cities and Towns in Minnesota*. See also, state auditor's [Uniform Chart of Accounts](#)

The property tax is the primary revenue source for cities and it applies to all taxable property within cities' boundaries. The Minnesota property tax system is complicated, including classifications of property based on the use of the property. Over time, the system has become more complex and difficult for taxpayers to understand. Unfortunately, local officials must frequently explain how the system works and take the blame for the complicated features of the system. Local officials, however, can only control local levy decisions and must focus on that for budgeting purposes.

2. Setting the property tax levy within levy limits

Minn. Stat. § 477A.011.
Minn. Stat. ch. 275.
Minn. Stat. § 275.70, subd. 5.
How to Estimate Your 2010
Levy Limit.

Handbook, Chapter 22.

Each year, cities certify a property tax levy, within current levy limits, for the following year in dollars, not at a specific rate. The council should set a tax levy high enough to provide money for the following purposes during the upcoming budget year:

- Payment of all estimated expenditures, including an allowance for a reserve and the amount necessary to make all city contributions to the Public Employees' Retirement Association (PERA).
- Current expenditure liabilities the city cannot pay in the present year for lack of current funds or that the city will pay through short-term borrowing.
- Repayment of all tax anticipation certificates the city issued during present and past years.
- An amount in anticipation of the reduction or loss of state aids, federal revenues, or other undependable sources of revenue.
- For the payment of interest and repayment of principal on bond issues before the bonds are delivered. (Bonds issued previously are already funded by a portion of the city levy.)

3. Gambling taxes and funds

Minn. Stat. § 349.213, subd. 3.

Cities may impose up to a 3 percent local gambling tax on licensed gambling organizations in order to cover the cost of regulating lawful gambling. A city may not use these tax revenues for any other purpose.

Minn. Stat. § 349.213, subd. 1(a).

Cities may also require organizations conducting lawful gambling to contribute 10 percent of their net profits derived from lawful gambling to a city-administered fund to be disbursed for lawful purposes. Note: state law defines lawful purpose. Such funds cannot be used for the benefit of a pension or retirement fund.

See LMC information memo
Lawful Gambling.

For further discussion of lawful gambling expenditures and regulation, see LMC information memo, *Lawful Gambling*.

B. Franchise fees

Minn. Stat. § 216B.36.
47. U.S.C.A. § 542.
"Minnesota City and Town
Accounting and Financial
Reporting Standards Uniform
Chart of Accounts" Office of
the State Auditor, Oct. 2004.

Cities are authorized to impose a franchise fee on utility services, such as gas, electric, and cable television. Franchise fees for gas and electric utilities are subject to negotiation. Cable franchise fees are limited to no more than 5 percent of the cable operator's gross revenues over a 12-month period. The revenues from franchise fees can be useful in offsetting a city's costs to regulate these businesses and maintain and protect the public right-of-way. The state auditor classifies franchise fees as other taxes.

C. License and permit revenue

See [Additional Information on Sources of Revenue](#).

Another source of revenue for cities come from license and permit fees. Cities should be conservative when estimating these amounts as they can vary considerably from year to year. Municipal licensing should not be viewed as a significant source of revenue. In Minnesota, license fees must approximate the direct and indirect costs in issuing the license and policing the licensed activities.

D. Intergovernmental revenue

Dates for City Budgets 101:
State aid and Credit Programs
Property Tax System.

Local Government Aid 101.
History of Local Government
Aid to Cities.

10 LGA Key Points .

Minn. Stat. § 477A.014. “Local
Government Aid (LGA) and
Annexations, Boundary
Changes, or Changes in Form
of Government,” Minnesota
Department of Revenue.

Minn. Stat. § 273.1384.
Market Value Homestead
Credit 101.

2009/2010 LGA and MVHC
Unallotment FAQ.

LMC information memo,
Budget Guide for Cities.

1. Local government aid

For some cities, local government aid (LGA) from the state is a significant source of income. The goal of LGA is to equalize cities’ ability to provide an average level of services at reasonable property tax rates. A complex formula determines how much LGA each city receives. The Minnesota Department of Revenue certifies how much LGA each city receives by Aug. 1 of each year. Cities receive two annual LGA payments—one in mid-July and the other at the end of December.

The commissioner of the Department of Revenue notifies each city of its LGA distribution during the first week of August. Cities have 60 days to appeal the calculation or factors used in the computation. Special considerations apply for cities dealing with annexation or a change in the form of city government.

2. Market value homestead credit

In 2001, the MVHC program replaced the homestead and agricultural credit aid. Please note: MVHC is a part of each city’s certified levy. MVHC is a credit that the state figures into each city’s certified levy, *so do not budget to receive MVHC dollars above your total certified levy.*

3. Unallotment or reduction of LGA and MVHC

Gov. Pawlenty announced unallotment, or reductions, of LGA and MVHC reimbursement in June 2009. Cities exempt from unallotment in 2009 and 2010 are those that are below 1,000 in population and with a below average tax base per capita (measured by adjusted net tax capacity per capita compared to the statewide average for all cities). For cities subject to unallotment in both years, some of the cut will come out of the July check (October for MVHC) and the balance will come out of the December check. The 2009 cuts will be equally split between the two payments (July and December for LGA, October and December for MVHC reimbursement). Cuts take effect, for the most part, in 2010 to give cities more time to make budget adjustments. Roughly one-third of the overall cut occurs in 2009 while the remaining two-thirds occur in 2010.

4. General state aid

Cities in Minnesota receive a variety of shared revenues from the state. Amounts for each city are typically available from the Minnesota Department of Revenue on or before Aug. 1 of each year. Each of these programs has a separate policy goal, and, taken in combination, the programs and their impact on city finances can be confusing. The following sections describe these programs and their interaction with the city budget-setting process.

a. Fire and police state aid

Minn. Stat. §§ 69.011-.031.
Minn. Stat. § 424A.08. Minn.
Stat. § 69.021, subd 4(c).
Minn. Stat. § 471.699. Minn.
Stat. § 69.021, subd. 5.

For example, see 2009
information on fire and police
state aid [Minnesota
Department of Revenue](#).

The state must pay the police and fire aid by Oct. 1 so the money usually goes out just before that deadline. However, cities must file the appropriate forms by March 15 each year to receive this money. The state auditor can delay the Oct. 1 payment date if a city fails to submit legally required financial reports.

According to the Minnesota Department of Revenue, *if the forms are not received by March 15 the Department of Revenue will send a final reminder stating that the forms have not been received and that the fire or police department could forfeit part or all of its aid for the year if the forms are not received within 10 days. The amount of aid forfeited is equal to the amount of yearly aid multiplied by 5 percent for each week or fraction of a week that the form is late.* Please note that the police state aid form must be signed and dated by the city clerk. If the form is not signed and dated, the form will be returned. Please also note that the fire state aid form must be signed and dated by both the municipal clerk (or secretary of an independent nonprofit firefighting corporation) and the fire chief. If the form does not contain both signatures, the form will be returned.

Funding for these programs comes from the state general fund, based on taxes paid to the state by most insurers writing homeowners, fire, and commercial non-liability policies. The state apportions the money to qualifying cities for fire and police pensions. If all of the police officers in the city police department are members of the PERA Police and Fire Fund), the state peace officer aid must be applied toward the city's employer contribution to the Police and Fire Fund of PERA. If there is no firefighters' relief association and the city is not a member of the statewide volunteer firefighter retirement plan (SVFRP), then the fire aid must be used to maintain the fire department.

Minn. Stat. § 424A.02, subd.
3a. Minn. Stat. § 424A.02,
subd. 10.

City councils preparing budgets should know that there is a penalty for paying relief association benefits in excess of the statutory limits. This penalty includes the loss of fire state aid. Also, volunteer firefighter relief associations must file a copy of revised bylaws with the state auditor when they are amended. Failure to do so could mean a loss of state aid until such documents have been filed.

b. County state aid for trunk highways and municipal state aid

Minn. Stat. § 162.09. See
[Additional Information on
Sources of Revenue](#).

The Minnesota Constitution requires that state gasoline taxes and motor vehicle registration fees provide funding for certain city, county, and state roads. These revenues are distributed through the highway user distribution fund. This fund is distributed by the Minnesota Department of Transportation for state trunk highways and for certain county and city roads through the county state aid highway and municipal state aid programs. Twenty-nine percent of the fund is dedicated for certain county roads and highways. Nine percent goes to cities with populations over 5,000. The remaining 62 percent is dedicated to the state trunk highway system.

c. Highway user tax distribution fund

Minn. Stat. § 161.081, subd. 1.
See [Additional Information
on Sources of Revenue](#)

Minnesota law, pursuant to article 14, section five of the state Constitution, requires 5 percent of the net highway user tax distribution fund be set aside for use on municipal and state roads.

E. Charges for services

See [Additional Information on Sources of Revenue](#).

Cities may also receive revenues from election filing fees, sales of maps and ordinances, assessment searches, court fees, police patrol and fire service fees, street and sidewalk repair, parking fees, refuse collection, water and sewer charges, inspection fees, and service charges such as those made by libraries, museums, and recreation facilities.

F. Public safety revenue

Contact the [POST Board](#) for further information at (651) 643-3060.

2009 Minn. Laws ch. 83, art. 1. See [Additional Information on Sources of Revenue](#).

The state reimburses cities for some police officer training costs. The reimbursement amount available for training and per officer depends on the number of eligible officers and is not determined until all of the applications have been received. Large changes in the total number of police officers in the state could affect the total amount available. The final amounts will be determined and checks should be mailed to cities by mid-September. For fiscal year 2010-2011, the Legislature appropriates \$2,859,000 to reimburse local governments for peace officer training costs.

G. Culture and recreation

Cities may generate income from cultural or recreational activities. This may include money from park rentals or revenue from city sponsored programs such as swimming classes, city festivals and city parades.

H. Enterprise funds

“[Minnesota City and Town Accounting and Financial Reporting Standards Uniform Chart of Accounts](#)” Office of the State Auditor, Oct. 2004.

Enterprise funds come from city operations run in a manner similar to private businesses. Examples include water and sewer operations, municipal liquor stores and electric utilities. These services are typically funded by charging those who use the service. According to the state auditor, cities are required to report sewer operations as enterprise funds.

I. Penalty charges

City revenue also comes from penalties and fines such as court fines, confiscated deposits, and collections on bonds or surety held for enforcement or security purposes. Though such revenue occurs, accounting for it in the city budget does not mean that cities plan on issuing a set number of penalties or fines.

J. Special assessment revenue

“[Special Assessments](#)” *House Information Brief*, Sept. 2008.

Special assessments are a charge imposed on properties for a particular improvement that benefits the owners of those selected properties. The payments may continue coming in to the city for years and may be tied to bond payments for local infrastructure improvements such as improved water and sewer structures.

K. Miscellaneous revenues

According to the state auditor, miscellaneous revenues do not come from taxes, licenses and permits, intergovernmental revenues, charges for services, or fines and forfeits. Examples of miscellaneous revenues includes money from interest on investments, including such investments as savings accounts, certificates of deposit, money market funds and treasury bonds and bills net increase (decrease) in the fair value of investments rents and royalties such as revenues from rental of city/town properties (excluding city hall and community hall rent, parking lot fees, and auditorium use fees which are classified elsewhere) and contributions and donations from private agencies or persons.

L. Other revenue

An example of other revenue in this fund is cash received from insurance companies or individuals to compensate the city for the loss of general fixed assets due to theft, accident or natural disaster. Also included in this fund are interfund transfers (legally authorized transfers between revenue funds to expenditure funds. Examples include transfers from the general fund to a capital projects fund for authorized construction and transfers from an enterprise fund to the general fund to finance general fund expenditures. This fund also tracks money from the sale of general obligation bonds issued by the city.

[City Expenditures chart](#)

[City of Hopkins 2009 Expenditures Summary Graph](#). Winner of both GFOA Budget Award and Certificate of Achievement in Financial reporting Program Award. Excerpt from state auditor's *Accounting Manual for Small Cities and Towns in Minnesota*.

VII. Expenditures

Cities must estimate their expected costs for the upcoming fiscal year and budget accordingly. Common expenses across all categories of expenditures include salaries and other employment costs, equipment, supplies, materials, maintenance, repairs, training, and fuel costs. Many cities will have some activity in most of these seven categories and the first two categories (general government and public safety) make up the majority of city expenditures.

A. General government

See, state auditor's [Uniform Chart of Accounts](#). State auditor's [2007 Minnesota City Finances Report: Glossary](#).

Expenditures under this category include general costs for the administration and finance of city government. Costs include those associated with the council activities, such as publishing ordinances, and meetings. This category includes clerk costs for holding general and special elections. Legal costs fit into this category as do salaries, wages, and related employee benefits such as employer contributions to retirement systems, insurance, sick leave and similar benefits.

[Minn. Stat. § 415.11](#).

City councils may now temporarily reduce their own salaries for one year. New law, effective in May 2009, allows a city council to enact an ordinance to take effect immediately. The law provides an automatic readjustment back up to the previous salary unless a city's ordinance specifies a different time.

B. Public safety

Minn. Stat. § 626.8458.
Minn. Stat. § 626.8462.

The basic costs of public safety include police protection, fire protection, ambulance service, emergency preparedness, and some protective inspections. Cities should be sure to budget for public safety training costs. Training costs include statutorily required training, such as police-pursuit training and training requirements for part-time police officer licensure.

Minn. Stat. § 69.77, subd. 7.
"Municipal Contributions to Volunteer Fire Relief Associations" state auditor's office, March 2009.

The city must provide for at least the minimum obligation to the fire relief association in the annual municipal budget. The main sources of revenue for relief associations are municipal contributions, fire state aid, and investment earnings. Municipal contributions can be made voluntarily by a local community or may be required, based on the relief association's financial situation. State law requires a municipality to pay a minimum annual contribution to the special fund of its affiliated relief association, unless the special fund is fully funded or fire state aid is sufficient to cover the municipal obligation. Decreased earnings on investments generally mean higher required municipal contributions, which can create challenges for a municipality's budget.

C. Culture-recreation

Document all expenditures for city organized cultural and recreational activities. Examples include city expenditures for libraries, lifeguards, community centers, senior citizen centers, park supervision, park lighting and trails.

D. Conservation of natural resources

This category covers all expenditures for the conservation and development of natural resources, for example shade tree programs and the staff time taken to provide such programs.

E. Debt service

Minn. Stat. § 470.71. Report of Outstanding Indebtedness (Excel spreadsheet format or Adobe Acrobat form) Minn. Stat. § 475.755; Minn. Stat. § 475.754; Minn. Stat. § 412.310; Minn. Stat. § 410.32 (charter cities).

Cities have no authority to borrow money from banks or financial institutions. Instead, cities issue debt, or bonds, to finance public infrastructure improvements. *Each year, councils and staff must keep track of the amount of debt issued, and payments of bond principal, interest and all associated costs.* Cities must also document costs of issuing bonds and payments to fiscal agents working with a city on bonds in this category.

Minn. Stat. § 475.755.

Another type of expenditure cities may budget for is the use of certificates of indebtedness. If the income of a city is reasonably expected to be reduced below the amount anticipated in its budget when the final property tax levy was certified, and those receipts are insufficient to meet the expenses incurred or to be incurred during the fiscal year, a city can issue certificates of indebtedness to mature within two years or less from the end of that fiscal year. The maximum amount the certificates may be issued for in a fiscal year is the expected reduction and the costs of issuance.

The certificates must be repaid by a levy, which according to the Department of Revenue, is not subject to or included in a city's levy limit. If these certificates are used to compensate for unallotment or loss of other state aid, the same amount cannot be again recouped under a separate special levy.

F. Miscellaneous expenditures

Miscellaneous expenditures are those which do not fit in the other categories. Examples of miscellaneous expenditures may include costs to maintain a cemetery, costs to settle legal claims against the city and costs related to enterprises like water and sewer that do not fit anywhere else.

VIII. Capital improvements

Minn. Stat. § 412.221.
“Financing Infrastructure
Projects,” *Minnesota Cities*
(Aug. 2009, p. 6).

City of Faribault, *Capital
Improvement Plan 2009-
2010*.

Budgeting for city infrastructure (roads, bridges, buildings etc.) covers more than one year so many cities separate these costs from yearly budgeting. Planning for future infrastructure costs is essential. A capital budgeting plan, sometimes referred to as a capital improvement plan or CIP, typically lists five or six years of major capital improvements, their order of priority, and a way to pay for them. A plan allows a city to save money for these projects. Priorities in the capital budget program remain tentative, and the council reviews them annually. Although capital improvement budgeting may appear cumbersome and unwieldy to small cities, this is actually not the case. A capital budget plan provides protection to small cities, avoiding unforeseen infrastructure failures and expensive emergency repairs.

IX. Other regulations impacting municipal budgets

A number of state and federal regulations require certain types of reports and technical accounting strategies related to city budgets and city budgeting practices.

A. GASB

Governmental Accounting
Standards Board. *Summaries
of GASB Statements. State
auditor’s GASB 34 and Other
Governmental Accounting:
Effective Dates*.

The Governmental Accounting Standards Board (GASB) issues statements (so far 47 of them) that establish standards for accounting and financial reporting—or generally accepted accounting principles (GAAP)—for state and local governments throughout the United States. In Minnesota, pursuant to state law, the state auditor enforces the accounting standards for cities. Specifically, the state auditor requires and enforces compliance with GAAP for cities with populations of 2,500 and higher.

Minn. Stat. § 477A.017, subd.
2. See state auditor’s
“Financial Reporting for
Small Cities.”

However, state law does not require that cities with populations under 2500 report GAAP financial statements. (These cities may prepare GAAP statements as a good business practice or because of some contractual requirement, but are not required to do so by state statute). The state auditor provides a discussion on compliance with GASB 34 in small cities in the document, “Financial Reporting for Small Cities.” This guidance should be used with the help of financial service providers to be best prepared to meet financial reporting requirements.

See [OSA](#); [GASB](#) and [GFOA](#).

GASB 34 is lengthy and is not discussed in detail in this chapter. For further information on GASB 34, contact GASB, the Minnesota Office of the State Auditor, or the Government Finance Officers Association (GFOA).

B. State auditor reports

Handbook, Chapter 26. “City of Roseville, MN 2008 Summary Budget Statement 2008 Budget.” Winner of both GFOA Budget Award and Certificate of Achievement in Financial reporting Program Award.

State law requires that cities *file* budget information with the state auditor’s office and also requires that cities *publish* budget information each year. A number of other financial reports and forms must be filed with the state auditor as explained in detail in Chapter 26 of the League’s *Handbook for Minnesota Cities*.

C. Truth in taxation

Minn. Stat. § 275.065, subd. 1.

Citizen engagement in the budget making process is required by state law. The 2009 Legislature made significant changes to the truth-in-taxation requirements, essentially abolishing the old scheme of published notices, multiple public hearings, and meetings. While apparently not the intent of the legislation, the amended language contains no exception for smaller cities or cities with levy increases less than or at the inflation price deflator (IPD). The law seems to require that all cities follow this new process, but the Minnesota Department of Revenue views this as contrary to legislative intent and it will not be enforcing the law with respect to cities under 500. However, according to the Minnesota Department of Revenue, the exception for being at or below the IPD is gone. So if a city increases its levy by 0.83 percent or less that city is still subject to the new TNT process.

Additional Information on TNT Hearings 2009.

Pursuant to the Department of Revenue’s written interpretation of the new law, councils must include information on the budget and levy process in meeting minutes. Citizens must be allowed to speak (before a final budget and levy is determined) at one meeting dealing with budgets and levies. This meeting must occur after Nov. 24, 2009 and must not be held before 6 p.m. Cities may, but are not required to, determine a final budget and levy at this public comment meeting. This law takes effect now, in 2009, for taxes payable 2010 and thereafter.

X. Plan B cities

Minn. Stat. §§ 412.701 – 412.731.

Minn. Stat. § 412.651, subd. 7.

See Handbook, Chapter 1.

Cities with the Plan B form of government must follow unique budgeting requirements in state law. In these cities, the city manager is responsible for the city budget and sets out the required budgeting structure. State law addresses citizen participation in budgeting, requires that the manager read the budget aloud and respond to council questions. As noted previously, once a Plan B city adopts a final budget, budget amendments require approval by a four-fifths vote of all members of the council. Consult the city attorney when voting on budget amendments in a Plan B city to ensure compliance with the law.

XI. Standard plan cities

In Standard Plan cities, the council might use either of two procedures when developing city budgets. Council might delegate the task of coordinating departmental budget requests to a council committee and it may make either this committee or an administrative officer responsible for budget execution. Or the council may also give the responsibility for both budget preparation and execution to the clerk, deputy clerk or other official responsible for the supervision of all city activities

XII. Charter cities

Councils in charter cities must review any special requirements related to city budgets and work with staff and the city attorney to ensure that the requirements in charter and law are met. A number of city charters make the city manager responsible for city budgeting but the council must still play a role in budget planning and approval.

XIII. Conclusion

City of Hopkins [City Budget](#).
Winner of both GFOA
Budget Award and Certificate
of Achievement in Financial
reporting Program Award.

Accurate and complete budgeting is crucial to a city. It provides sound legal, financial and ethical basis for city operations. Done correctly, budgets show the revenues and expenditures necessary to provide the services and programs desired by the community. It reflects the goals, objectives, and priorities the current council identifies, based on input from previous council decisions, the residents and taxpayers.