



Local Government Aid 101

This guide describes Minnesota's Local Government Aid (LGA) program. The first official LGA program was created in 1971 and provided funds to counties on a per capita basis for allocation to cities in proportion to their property tax levy. LGA has undergone many changes since to arrive at the system used today. The most recent major changes were enacted in 2008 and will be in effect for payments made in 2009 and thereafter. LGA is distributed using a complex formula that compares a city's spending needs with its ability to raise revenue (unmet need). The 2008 reform included the addition of a jobs base aid and modified the small cities base aid.

Funding History

Prior to 2003, the total LGA appropriation increased annually for inflation. This increase ranged from 2.5 to 5 percent. In addition to enacting significant changes to the program, the Minnesota Legislature reduced funding for LGA by 25 percent in 2003. While some of this funding was restored in 2005 and 2008, total certified LGA for 2009 was approximately 10 percent below the 2003 funding level. The total LGA distribution is shown below for 2000 through 2008.

Year	Certified LGA	Actual LGA
2000	394,846,199	394,846,199
2001	411,514,841	411,514,841
2002	565,338,952	565,338,952
2003	586,848,950	464,941,977
2004	437,466,461	437,466,461
2005	436,558,200	436,558,200
2006	484,558,200	484,558,200
2007	484,558,200	484,558,200
2008	484,148,487	430,634,157

The 2009 appropriation was reduced due to the governor's unallotments, ratified by the Legislature. The 2010 appropriation was reduced in two parts - \$102 million in the governor's unallotments and \$7.8 million in additional reductions by the 2010 Legislature. The 2010 Legislature also reduced the 2011 LGA certification from \$558 million to \$527 million. The 2011 appropriation was further reduced by the 2011 Legislature.

Year	Certified LGA	Actual LGA
2009	526,148,487	481,521,933
2010	536,671,457	426,438,012
2011	527,100,646	425,345,348
2012	425,238,384	

Prior to the 2003 reforms cities received a grandfather distribution each year that ensured that each city received at least as much LGA as in 1993. While the grandfather distribution was eliminated in 2003, approximately \$26 million is still reserved for aid base for regional centers and cities that have faced unique circumstances. From 2006 to 2008, cities under 5,000 in population received

base aid equal to six dollars per capita. Between 2003 and 2008, the total amount of LGA received by a city is the sum of any aid base and formula aid.

The formula for 2009 through 2011 keeps the need minus ability to pay calculation used since 2003, modifies the small city base aid and adds a jobs base aid.

Formula Basics

A city's share of the LGA appropriation is determined by a complex formula. Each city's expenditure need is measured based on several statistical variables. These variables or factors attempt to identify characteristics that cause differences in the amount cities need to spend to provide the same level of service. Calculated need is then compared to the city's ability to pay. A city's LGA distribution is the sum of its unmet need plus its jobs base aid and small city base aid and any city aid base.

For 2009, all data used in the calculation will be based on the data used in calculating aids payable in 2008. For aids payable in 2010 and subsequent years the data will be the most recent available as of January 1.

Variables

Prior to 2003, one formula was used to estimate expenditure need for all cities. As a result of the 2003 changes, separate formulas are used to determine need for cities above and below 2,500. The formula for cities under 2,500 continues to use the variables that were used for all cities prior to 2003. These variables are:

- pre-1940 housing percentage;
- population decline over the past ten years;

- commercial/industrial property market value percentage; and
- population

The new formula for cities over 2,500 in population, enacted in 2003, includes the pre-1940 housing percentage and population decline factors. It also includes four additional variables:

- traffic accidents per capita (three year average);
- average household size (not including institutionalized populations);
- metro or non-metro location; and
- adjusted net tax capacity (ANTC) per capita (control variable)

More detailed information on each variable can be obtained by calling the League.

Calculating Unmet Need

To calculate a city's expenditure need, the values for each variable are multiplied by fixed coefficients. These coefficients were determined by a statistical process called multiple regression. The coefficients weigh the variables according to their relative importance in explaining differences in city spending need. The sum of these products is a per capita dollar expenditure need. The minimum need per capita of a city greater than 2,500 population is \$285. Multiplying the per capita need by the population gives the total expenditure need, which is then compared to an individual city's ability to pay.

Ability to pay is defined as a city's capacity to raise revenue via property taxes. This is calculated by applying the statewide average city tax rate based on

the prior year's levy to the city's tax base.

The difference between a city's total expenditure need and its ability to pay is its unmet need. Unmet need is adjusted so that the total of all distributions equals the current appropriation. A city's formula aid is the sum of its jobs base aid, small city base aid and unmet need. For aids payable in 2010 and subsequent years a city's formula aid will be the sum of its jobs and small city aid bases and the average of its unmet need for the most recent two years.

Aid Bases

Jobs and small city base aid are part of a city's formula aid. City aid base, regional center aid and aid given to cities facing unique circumstances, is added to a city's formula aid but is subject to maximum and minimum adjustments.

Small city aid base is now equal to \$8.50 per capita. For aids payable in 2010 and subsequent years, the small city aid base is multiplied by the ratio of appropriation. Cities over 5,000 in population do not receive any small city aid base.

Jobs aid base is intended to account for overburden to a city. Job aid base is equal to \$25.20 multiplied by the city's population and by the number of jobs per capita in the city. The \$25.20 will be adjusted annually based on the Implicit Price Deflator. The jobs base aid for a city that receives regional center aid is reduced by the lesser of 36 percent of its regional center aid or \$1.0 million. The maximum jobs base aid a city may receive is \$4,725,000. Cities under 5,000 do not receive any jobs base aid.

Like the small city base aid, jobs base aid will be adjusted by the ratio of appropriation for aids payable in 2010 and subsequent years. The number of jobs per capita in a city is determined by dividing the average annual number of employees in the city by the city's population for the same calendar year. The average number of employees in a city is obtained from the Quarterly Census of Employment and Wages. Cities have the opportunity to challenge employee estimates by filing an objection with the Department of Employment and Economic Data by June 20, 2008.

Adjustments

A city's distribution is the sum of its formula aid and its city aid base, if any. This payment is further adjusted to fall within minimum and maximum amounts. Minimum and maximum rules were designed to phase in the new formula by limiting the amount a city's LGA can change in a single year.

For aids payable in 2009, a city's total aid cannot exceed 35 percent of its net levy for the prior year (2007) plus its total aid distribution in 2008. For aids payable in 2010 and subsequent years, a city's LGA distribution cannot increase by more than 10 percent of its net levy for the previous year plus the total amount of aid received in the prior year.

Aid minimums vary based on population. For aids payable in 2009 only, a small city (under 2,500 population) cannot receive less than its 2008 distribution. If a city's entire 2008 payment was small city base aid, its 2009 minimum is zero. For aids payable in subsequent years, a small city cannot receive less than its certified aid for the

prior year minus the lesser of \$10 per capita or 5 percent of its 2003 certified aid amount.

For aids payable in 2009 and subsequent years, a large city (population 2,500 and above) cannot receive less than its certified aid for the prior year minus the lesser of \$10 per capita or 10 percent of its prior year net levy.

No city's total aid loss can exceed \$300,000 if the total appropriation is the same or larger than the year previous. Aid loss may also exceed this maximum when a city's net tax capacity is adjusted due to decertification of a tax increment financing district.

Timing

The Department of Revenue notifies cities of their LGA amounts for the following year by July 31st. Cities receive aid in two equal payments in July and December.

Policy Issues

Several of the 2003 changes resulted in a much more volatile program. The elimination of both the grandfather provision and the automatic inflationary increase in the LGA appropriation meant that some cities experienced actual decreases from year to year instead of progressively smaller increases. The elimination of the caps on aid increases for Minneapolis, St. Paul and Duluth meant that their distributions could consume a larger (and less predictable)

portion of the allocation, decreasing aid available to other cities.

The mix of factors in the 2003 formula also added to the volatility. The formula for large cities no longer includes two traditionally stable variables – population and commercial/industrial market value percentage – and does include a potentially highly variable factor – automobile accidents per capita.

The 2008 changes are intended to eliminate some of this volatility. For example in 2010 and thereafter a city's formula aid will include the average need for the previous two years.

The efficacy of certain formula factors as indicators of need is often questioned in reform efforts. For example, is the percentage of pre-1940 housing units the best measure of infrastructure age? Also, this factor can be drastically changed due to natural disasters or other unforeseen events. The use of traffic accident data has been questioned because of potential unevenness in reporting accidents.

The Legislature included a provision in the 2008 bill requiring a study of LGA that will consider these questions. In 2008, the chairs held only one meeting. In late 2011, new chairs called a meeting to get the effort going again. The group must make recommendations to the Legislature by the end of 2012.

Resources

League of Minnesota Cities

<http://www.lmc.org/page/1/property-tax-state-funding-fiscal-issues.jsp>