State of the Cities 2013: City Fiscal Conditions

Introduction

This marks the tenth consecutive year that the League of Minnesota Cities has asked member city officials to report on the kinds of fiscal challenges faced in their cities and to describe the strategies used to address those challenges (see the League's website for the 2013 survey instrument). A total of 405 cities participated in the survey for a response rate of 49 percent. It is important to remember that survey results must be considered as a snapshot of conditions at a specific point in time. Cities responded to the 2013 survey from November 8, 2012 through January 16, 2013.

This year city officials responded to the four questions that have been asked every year as well as to several new questions on a variety of topics. This report will discuss the responses to these four base questions, comparing them with data from prior years. A separate report will describe responses to questions on volunteers in cities. This second report will include several case studies of cities using volunteers to deliver services.

For the first time since 2006, more than half of cities report an increased ability to meet needs in 2012

Highlights of this section

- The share of cities that reported an increased ability to meet needs rose for the third year in a row, from 30 percent in 2011 to 51 percent in 2012.
- Looking to 2013, 52 percent of cities predict more favorable conditions.

The share of cities that reported being better able to meet financial needs during the past year grew 20 percentage points, from 30 percent in 2011 to 51 percent in 2012[1] (see Chart A[2]). This is the third time since 2006 that this figure has increased, and the first time since 2006 that this share is over 50 percent. The share reporting an easier time meeting needs is now just slightly below the share that did so in 2006 (53 percent). Looking to next year, a slightly larger share of cities, 52 percent, predicts better times in 2013. While the mix of cities responding to the survey changes

[1] The measure of "better" or "less able" is a relative comparison between a city's fiscal condition in the current year and in the prior year. In other words, a response of "better able" does not imply that a city's financial circumstances are good, only that they improved over the previous year. Cities are not asked how well they're able to meet needs in any given year.
[2] The share of cities reporting an increased ability to meet needs and the share reporting a decreased ability may not sum to 100 percent. Cities are not required to answer all questions on the survey. Cities often leave no response if they are unsure of how to answer or if the question does not apply to their city. Many cities that leave the question regarding ability to meet fiscal needs blank do so because they feel that there is no change in this ability between years.

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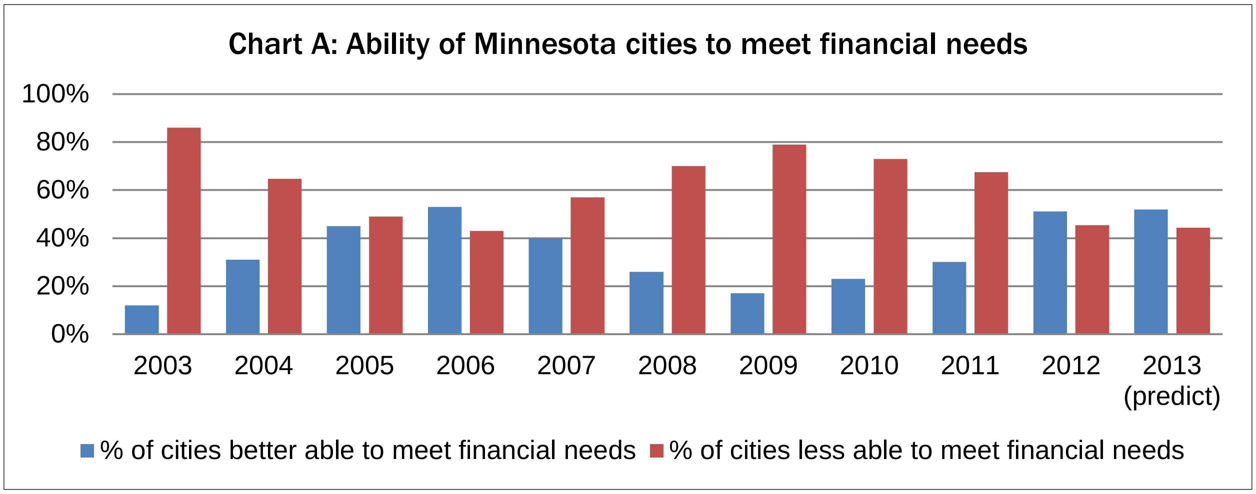
each year and must be considered when comparing responses from multiple years, 49 cities have responded to the survey in all 10 years. Data from this group show a similar trend with 59 percent reporting improved conditions in 2012, and 61 percent predicting more favorable circumstances in 2013.



The proportion of cities reporting an improvement in conditions increased annually between 2003 and 2006, when roughly half of cities reported being better able to meet needs. Over the next few years this share declined, until just 17 percent of cities reported more favorable conditions in 2009. This share edged upward in both 2010 and 2011, and jumped considerably this year to right above 50 percent. It is important to remember that "better able" does not mean that conditions are good, just that they're more favorable when compared to the prior year. Also, cities have been working to adapt to the "new normal" for several years now. Cities may be better able to meet needs with fewer resources. Given resource constraints, some cities may now be doing less than they used to do. Cities may now be accustomed to confronting problems that arose during the recession. What once may have been a challenge may now be part of the new normal. Actions taken over the last several years may have improved their ability to meet needs now.

Years of cuts to local government aid (LGA), some occurring after cities have already budgeted for the year, have led some cities to plan on using any aid received for one-time purchases. For example, one city planned to use its LGA for a street project that could be delayed if aid was not received. Of course, not all cities are able to do so. The instability in LGA distributions certainly influences a city's ability to meet needs. Aid reductions for 2012 were announced prior to being certified, giving more time to plan for less revenue. Thus, a city's expected aid amount equaled the amount actually received. Similarly, the 2012 tax bill included provisions that reduced the 2013 LGA distributions. Cities with populations over 5,000 will receive their 2012 amount while smaller cities will receive the greater of their 2012 amount or their 2013 formula amount.

A recent survey of Minnesota citizens shows a similar trend in terms of improving outlook. A poll conducted in 2011 showed 45 percent of respondents believed that Minnesota was headed in the right direction. In 2012 this share jumped to 65 percent.[3]

Likewise, a recent survey conducted by the National League of Cities (NLC) suggests that city officials nationwide may have adjusted their assessment and expectations of meeting fiscal conditions to reflect the new normal.[4] The survey, conducted in the spring of 2012, shows that 57 percent of city officials were better able to meet needs in 2012 than in 2011. In 2011, 43 percent reported more favorable conditions than in 2010.

Trends by size follow pattern of cities overall

Highlights of this section

- The increase in the proportion reporting more favorable conditions from 2011 to 2012 was substantial among all sizes of cities. This increase was greatest among mid-sized cities, and smallest for cities with populations over 10,000.
- When looking to the future, cities in the three smallest size categories showed a decrease while the others showed an increase or no change in the share predicting an improved ability to meet needs in 2013.

Just as the share of cities overall reporting an improved ability to meet needs in 2012 grew, it also grew across all population size categories (see Chart B). This trend was observed last year as well. The share of cities reporting more favorable conditions is now the largest since 2006 for all size categories. Cities with populations between 3,001 and 10,000 saw the greatest change in the share reporting an easier time meeting needs in 2012 (68 percent compared with just 28 percent in 2011). Cities with populations between 1,301 and 3,000 also saw a large jump in this share, increasing from 25 percent in 2011 to 51 percent in 2012. In each of the three largest size categories, more than half of cities report improved conditions in 2012.

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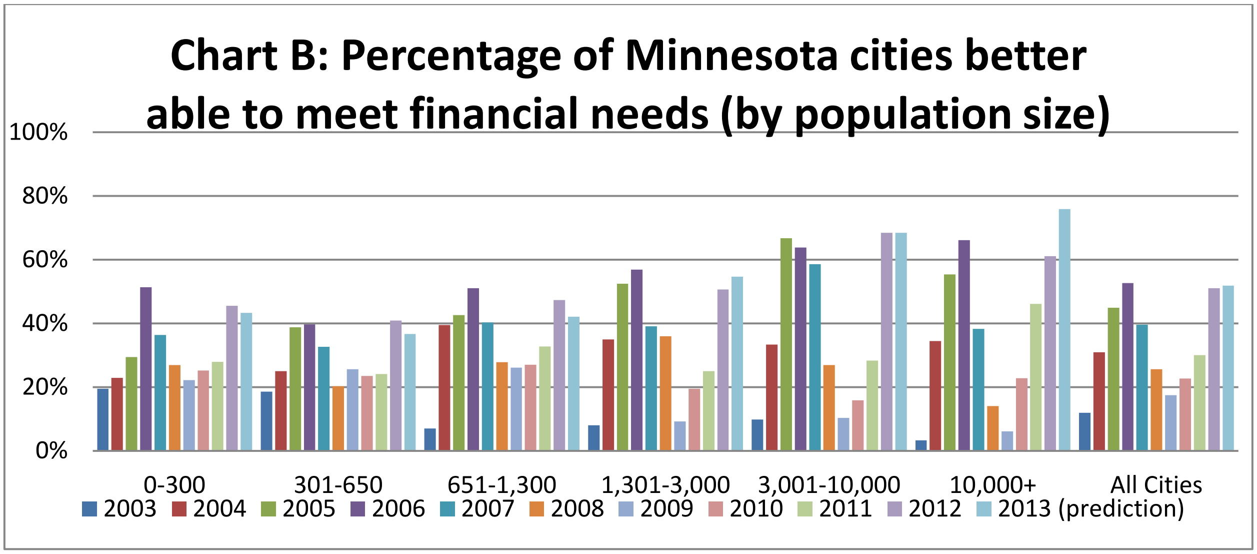
[3] Decision Resource LTD., “Just-in-Time Politics: Running Government like Amazon.com.” presented to Metropolitan Area Managers Association, 10 January, 2013.
[4] Pagano, Michael A., Christopher W. Hoene and Christina McFarland. “Research Brief on America’s Cities: City Fiscal Conditions in 2012,” National League of Cities, Sept. 2012.



The increase in the proportion reporting more favorable conditions from 2011 to 2012 is smallest among the largest cities. This smaller increase may be due to large jumps in this share experienced in 2010 and 2011. Looking ahead, the smaller cities are less likely to predict better times in 2013. This share increases or stays the same for all other size categories. However, for cities of all sizes, the share predicting an improved ability to meet needs in 2013 is greater than the share that reported improved conditions in 2011.

Cities in most regions report improved conditions in 2012

Highlights of this section

- Metro cities were much more likely to report an improvement in conditions than Greater Minnesota cities.
- Across the state, all but the Headwaters region showed an increase over last year in the proportion of cities reporting an increased ability to meet needs.

As in recent years, the share of cities reporting an easier time meeting needs is greater for cities in the seven-county metro area than for Greater Minnesota cities (70 percent vs. 47 percent). This share is a big jump over the share of metro cities doing so in 2011 (44 percent). The same trend is true among cities classified as metropolitan statistical areas (MSAs) compared with those that are not (see Table A).[5] Given that population is a component in MSA status, it is not surprising that MSA cities are more likely to report improved conditions. As discussed above, 61 percent of cities with population over 10,000 reported an increased ability to meet needs in 2012. This trend

[5] A metropolitan statistical area (MSA) is defined by the U.S. Census Bureau as a geographical area containing at least one urbanized area of at least 50,000 inhabitants with a total area population of at least 100,000. The area consists of one or more counties. As of December 2009, there are eight MSAs that include at least one Minnesota county: Duluth, Fargo, Grand Forks, La Crosse, Mankato-North Mankato, Minneapolis-St. Paul-Bloomington, Rochester, and St. Cloud.

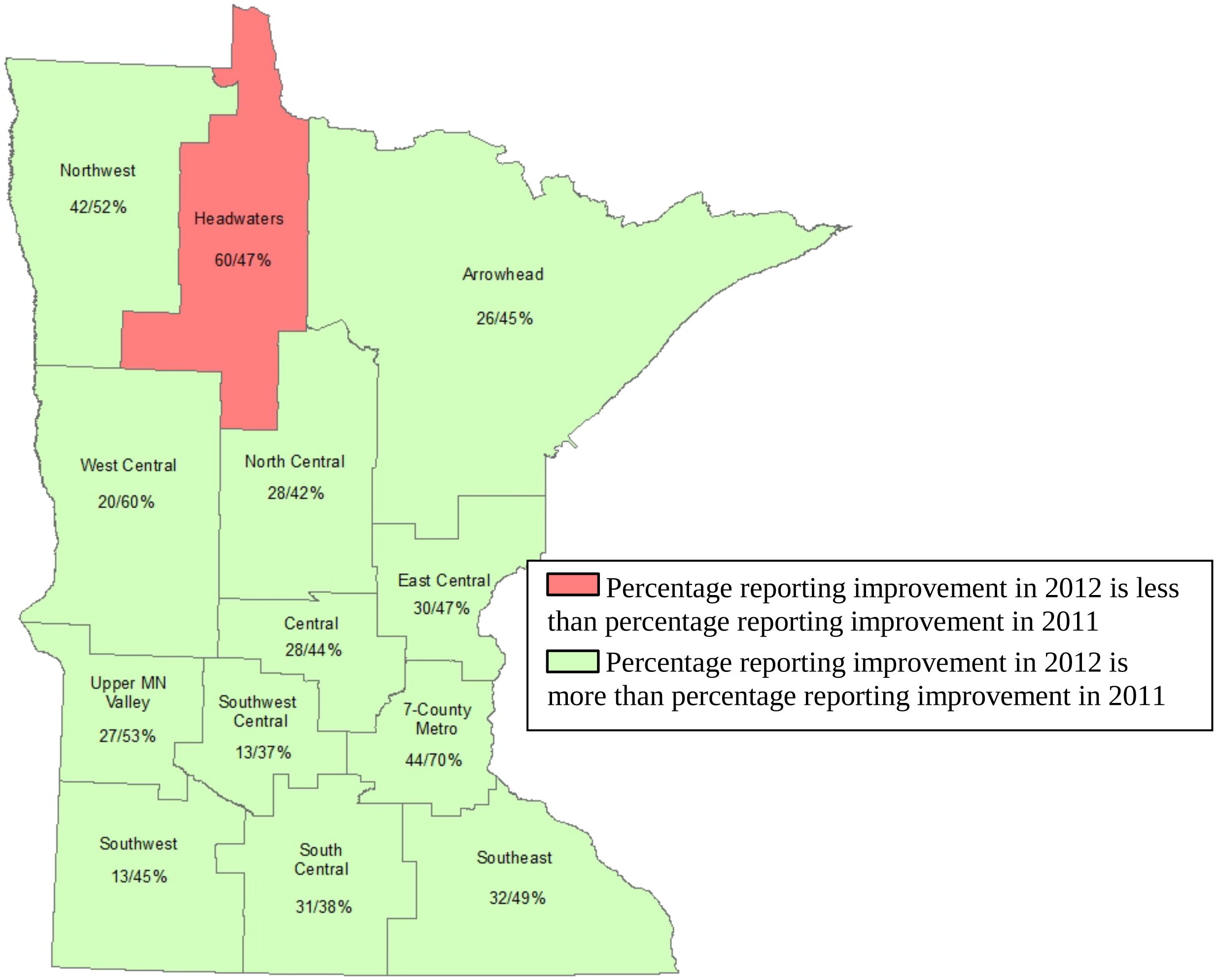
continues when looking to 2013, with 61 percent of MSA cities predicting more favorable conditions compared to 46 percent of non-MSA cities.

Table A: Percentage of Minnesota cities better able to meet needs (by MSA status)

	2004	**2005**	**2006**	**2007**	**2008**	**2009**	**2010**	**2011**	**2012**	**2013 predicted**
MSA cities	35%	48%	57%	46%	24%	15%	25%	35%	57%	61%
All Cities	31%	45%	53%	40%	26%	17%	23%	30%	51%	52%
Non-MSA cities	29%	43%	50%	34%	27%	20%	21%	26%	47%	46%

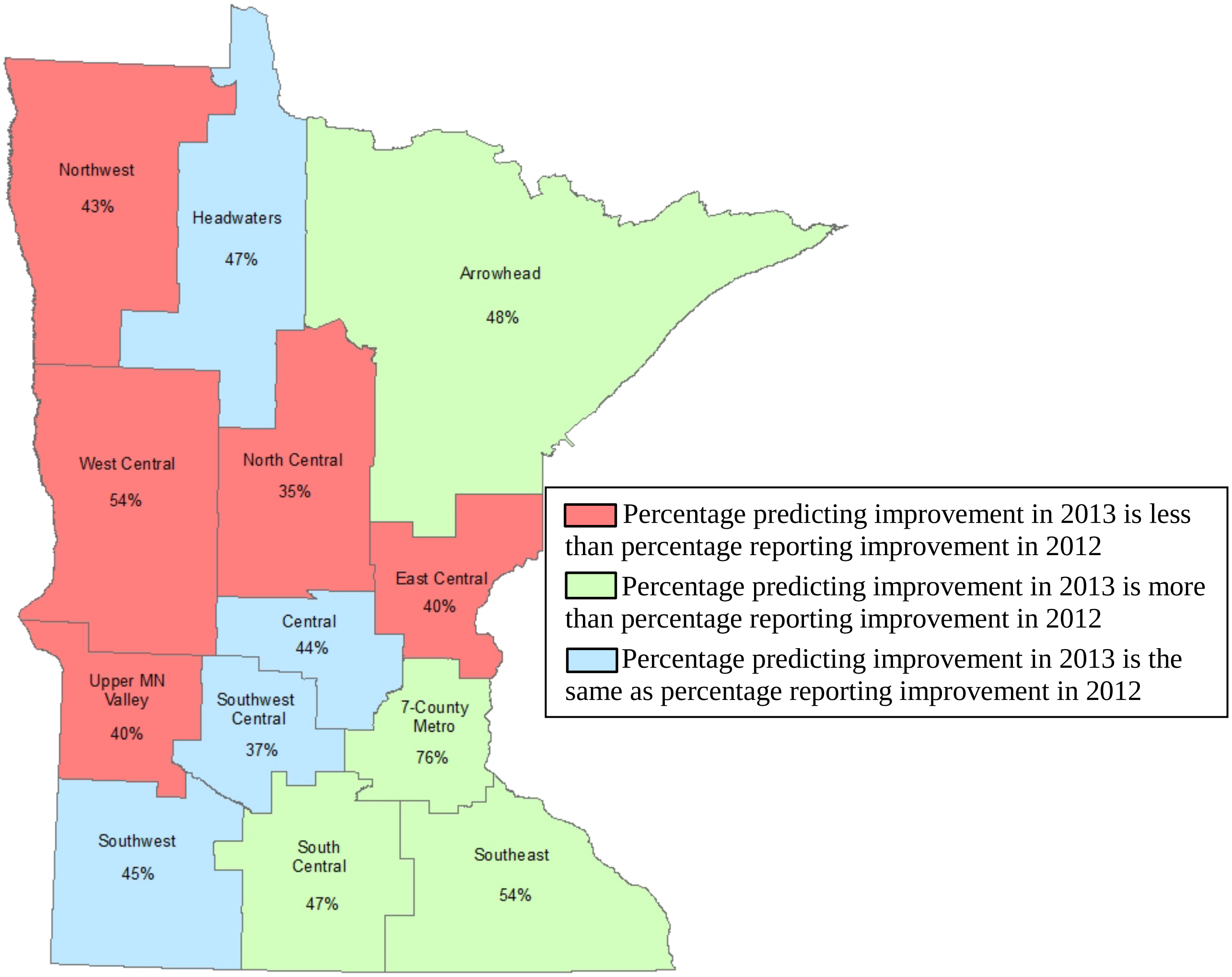
Across the state, all but the Headwaters region showed an increase over 2011 in the share of cities reporting an increased ability to meet needs. The Southwest region experienced the biggest change in this proportion, increasing from just 13 percent in 2011 to 45 percent in 2012. Over half of cities in the Northwest, West Central, Upper Minnesota Valley and 7-County Metro regions reported improved conditions in 2012. (see Figure 1).

Figure 1: Percentage of cities better able to meet needs in 2011/2012 (by region)



Looking ahead to 2013, slightly more regions predict a decreased ability to meet needs (see Figure 2). Five regions show a decline in this portion from 2012 while the remaining eight regions are split evenly among those expecting an improved ability and those forecasting no change. For the second year in a row, the regions in the southwestern corner of the state see an increase while the regions along the southeastern border of the state see a decrease in this share.

Figure 2: Percentage of cities predicting improved conditions for 2013 (by region)



Context: Bigger picture influences cities' ability to meet needs

The last several years have been difficult for cities. The Great Recession and its slow recovery created numerous economic problems, including unemployment, foreclosure, a lackluster real estate market, delayed or cancelled development, and business closures. Budget difficulties at the state level have added to and exacerbated the challenges facing cities. Cities have made, and continue to make, adjustments as they navigate in the new normal.

Budget uncertainty at the state and local levels has influenced cities' ability to meet needs. Cities have lost LGA and market value homestead credit (MVHC) reimbursement payments for several years. Aid amounts for a given year are certified the summer prior, giving cities time to build their budgets around this amount. In past years, cuts announced after certification made adjusting budgets and meeting needs very difficult for cities. While LGA was reduced for 2012, the announcement of this reduction was made in 2011, prior to certification, allowing cities time to plan for less state revenue. In other words, the amount they received equaled the amount they were certified to receive. Changes for the 2013 distributions—cities over 5,000 in population will receive their 2012 LGA amount while smaller cities will receive the greater of their 2012 amount or their 2013 formula amount—were part of the 2012 tax bill. MVHC was eliminated beginning in 2012 and replaced with a homestead market value exclusion program, which excludes a portion of a homeowner's market value from property taxes. For the first time since 2009, cities did not face levy limits, which had been in place for cities with populations over 2,500.

The 2012 legislative session came on the heels of the contentious 2011 session, which, due to no budget agreement at the end of regular session, lead to a state government shutdown in July 2011. Despite a budget agreement during the special session, the state's budget was left structurally unbalanced. However, a bit of good news came right before the start of the 2012 session with the release of the state's November 2011 Forecast.[6] The state's general fund was projected to have a surplus of $876 million for the balance of the biennium. Without an immediate shortfall, legislators could focus on non-budget priorities.

While many challenges persist, some appear to be stabilizing, or at least not worsening. The state's unemployment rate for December 2012 fell to 5.5 percent, down from 5.7 percent in 2011.[7] Minnesota gained 50,741 jobs over the year in December 2012, up 1.9 percent from 2011.[8] Sectors seeing the greatest growth include education and health services, and trade, transportation, and utilities. Mining and logging was the only sector to see job losses in 2012.

In November and December 2012, Minnesota's net general fund revenues totaled almost 4 percent more than forecast.[9] Corporate income tax receipts accounted for most of the additional revenue. Individual income tax receipts were also above forecast, but sales tax receipts lagged. Despite this seemingly good news, analysis suggests that this surplus is more likely due to one-time items and timing than increased economic activity. Recovery in the new normal continues to be slow.

Foreclosures continue to decline throughout the state. Data from the third quarter of 2012 show a 10 percent decline in the total number of foreclosures statewide.[10] However, decline has not been even across the state. Metro foreclosures were down 12 percent compared to just 7 percent for cities in Greater Minnesota. Despite the year-over-year improvement, the annual foreclosure total is still more than 300 percent greater than it was prior to the housing crisis. However, the real estate market is starting to show signs of improvement. Data through December 2012 show a 10 percent increase in the statewide median sales price over the same period in 2011.[11] However, due in part to lags in assessment, total city market value was down 9 percent in 2012.[12] It is important to note that most of this decrease is due to the conversion from MVHC to the homestead market value exclusion program. Taking out the effects of this exclusion, total city market value still shows a 3 percent decline over 2011.

[6] Minnesota Management and Budget, Dec. 2011.
[7] "State and National Employment and Unemployment," DEED, Jan. 2013.
[8] Ibid.
[9] "January 2013 Economic Update," Minnesota Management and Budget, Jan. 2013.
[10] "Minnesota Foreclosure Update: 3rd Quarter 2012," Housing Link, Nov. 2013.
[11] "Local Market Update for December 2012," Minnesota Association of Realtors, Feb. 2013.
[12] "2012 Property Tax Report," *Minnesota Cities*, "Sept.-Oct. 2012.

Despite ongoing challenges, cities continue to provide services that many have come to expect and rely on. Cities may also offer new services as citizen needs and service demands change. City officials utilize a wide variety of budget-balancing strategies as they balance the needs of the community with available resources, all the while mindful of their future outlook. As cities continue to operate in the new normal these strategies may change as new needs arise.

Share of cities reporting shortfalls declines in main revenue categories for second year in a row

Highlights of this section

- For the second year in a row, the share of cities reporting a shortfall in each of the main revenue categories declined.
- More than half of cities continue to report a shortfall in property taxes.

For 2012, smaller or equal shares of cities reported shortfalls in all revenue sources than in 2011(see Table B). This is the second year in a row that these shares have decreased. Cities may have adjusted expectations for revenues. In some cases, such as state aid cuts being announced in 2011, cities may have been better able to plan for less revenue. The share of cities reporting shortfalls in property taxes remains over 50 percent.

Table B: Percentage of Minnesota cities reporting revenue shortfalls*

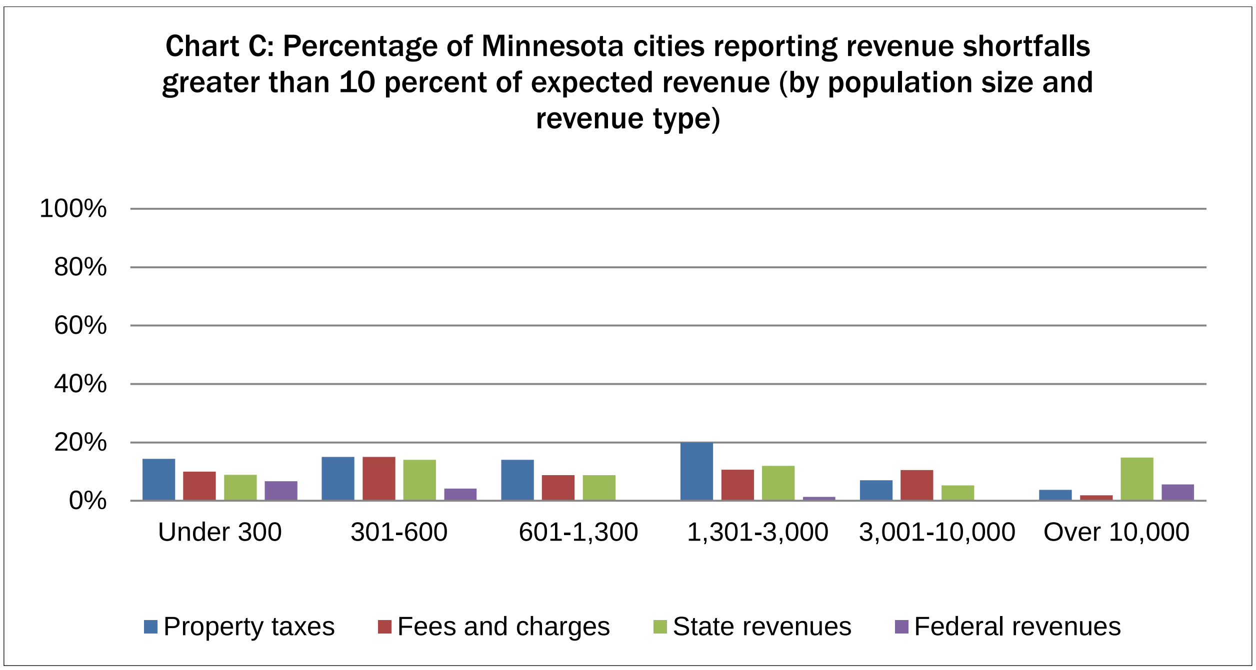
	Property taxes	Fees and charges	Sales tax	Local income tax	Lodging and restaurant taxes	State revenues	Federal revenues
2003	28%	17%	3%	n/a	5%	82%	12%
2004	27%	24%	1%	0%	3%	55%	8%
2005	40%	25%	3%	2%	4%	39%	12%
2006	40%	33%	4%	2%	4%	31%	13%
2007	43%	36%	6%	3%	5%	35%	15%
2008	54%	41%	7%	3%	8%	41%	14%
2009	62%	57%	8%	3%	12%	61%	16%
2010	68%	51%	8%	3%	11%	73%	22%
2011	67%	43%	4%	2%	7%	65%	17%
2012	60%	39%	4%	2%	6%	35%	13%

* Combines shortfalls of greater than and less than 10 percent of expected revenues

The shares of cities reporting shortfalls in the four main revenue sources (property taxes, fees and charges, state revenues, and federal revenues) generally increased each year from 2006 to 2010. A slight dip last year suggested that cities were adapting to operating in the new normal, which may mean budgeting for less. This year's continued decline lends further support to this notion. Some challenges that cities have faced in recent years, such as levy limits and cuts to the MVHC reimbursement, were not factors in 2012. Cities have continued to adapt to other ongoing challenges such as state aid cuts and market value declines. While the 2012 LGA appropriation was cut, cities learned of these cuts in 2011 instead of after aid had been certified. This allowed cities to adjust expectations regarding state revenues.

Over half of cities continue to report a shortfall in property taxes. Foreclosures and delinquencies may impact property tax collections. Most of the cities doing so reported a shortfall of less than 10 percent. Just 13 percent of cities experienced a shortfall of 10 percent or more. Greater Minnesota cities were more likely to report a shortfall in property taxes than cities in the metro area (62 vs. 53 percent). Unlike in past years, the smallest cities were least likely to report shortfalls in property taxes. The mid-sized cities were most likely to report this type of shortfall. Cities with populations between 1,301 and 3,000 were most likely to report significant shortfalls in property taxes, with 20 percent of cities doing so (see Chart C).

Larger cities generally have more options for implementing fees, rely on them more, and thus, typically are more likely to report significant shortfalls in this revenue category. However, a very different pattern is seen this year with just 2 percent of the largest cities reporting a significant shortfall. Last year 15 percent of the largest cities reported a shortfall of more than 10 percent in fee revenue. In 2012, cities between 301 and 600 in population were most likely to report this type of shortfall with 15 percent doing so.



Greater Minnesota cities were more likely than metro cities to report shortfalls of greater than 10 percent in property tax revenue (15 percent vs. 4 percent). Similar patterns were observed in past years. The gap is much smaller when looking at significant shortfalls in fee revenues—10 percent of outstate cities, and 8 percent of metro area cities reported a shortfall of more than10 percent in fee revenues. Metro cities were slightly more likely to report significant shortfalls in the other two main revenue categories. While aid was reduced in 2012, smaller shares of cities reported shortfalls greater than 10 percent than in past years with just 10 percent of Greater Minnesota cities, and 12 percent of metro cities doing so.

Little change in the shares of cities reporting no change in most budget factors

Highlights of this section

- Opposite of trends seen since 2006, the share of cities reporting an increase in the tax base rose in 2012 while the share reporting a decrease fell. Over half of cities still report a decline in the value of the city tax base.
- The five budget factors identified by the most cities as having increased in 2012 were prices, cost of living, and inflation; cost of employee wages and salaries; infrastructure needs; cost of employee health benefits; and public safety needs.
- The top factors identified as having at least a moderate impact on cities' budgets in 2012 were prices, inflation, and cost of living; infrastructure needs; tax base changes; employee wages and salaries; and local economic health.

Each year cities are asked to indicate whether a wide variety of budget factors increased, decreased, or remained the same when compared with the prior year. Many of the trends observed this year follow those seen in previous years. Last year in many factors, the share indicating no change increased over the share doing so in 2010. This year most factors saw a very slight increase or decrease in the share reporting no change. The share reporting no change in population saw a bigger increase, growing from 36 percent in 2011 to 45 percent in 2012.

The bursting of the housing bubble and slow recovery in the housing market has negatively affected the value of property tax base in many cities. From 2006 to 2011 the share of cities reporting a decline in the value of the tax base has increased while the share reporting an increase in value has fallen (see Chart D). In 2010 and 2011 cities were more likely to report a decrease in value than an increase. While that is true for 2012, the portion reporting greater value inched up while the portion experiencing a decline fell slightly over the prior year. While the real estate market does show signs of improvement, the median home sales price in 2012 was up 10 percent over 2011, it will take several years for this to show up in the tax base.[13] This is because assessors determine market values by January of the year before taxes are payable. In other words, values for taxes payable in 2012 were determined in January 2011. Thus any continued improvement in the housing market will take time before influencing tax bases. Of course, changes in the other categories of property—commercial, agricultural, and other—will contribute to the overall annual change in city tax base as well.

City market value was also affected by the change from MVHC to the homestead market value exclusion program. For 2012 the immediate effect of the exclusion was a decrease in the tax base. The extent of this decrease depended on the portion of homestead property in each city. City tax rates had to rise in order for a city to generate the same amount of city property tax dollars as in 2011. The exclusion also resulted in a shift in tax burden from homestead properties to other types of property. Again this effect varied from city to city based on the portion of homestead property made up of lower valued homes.

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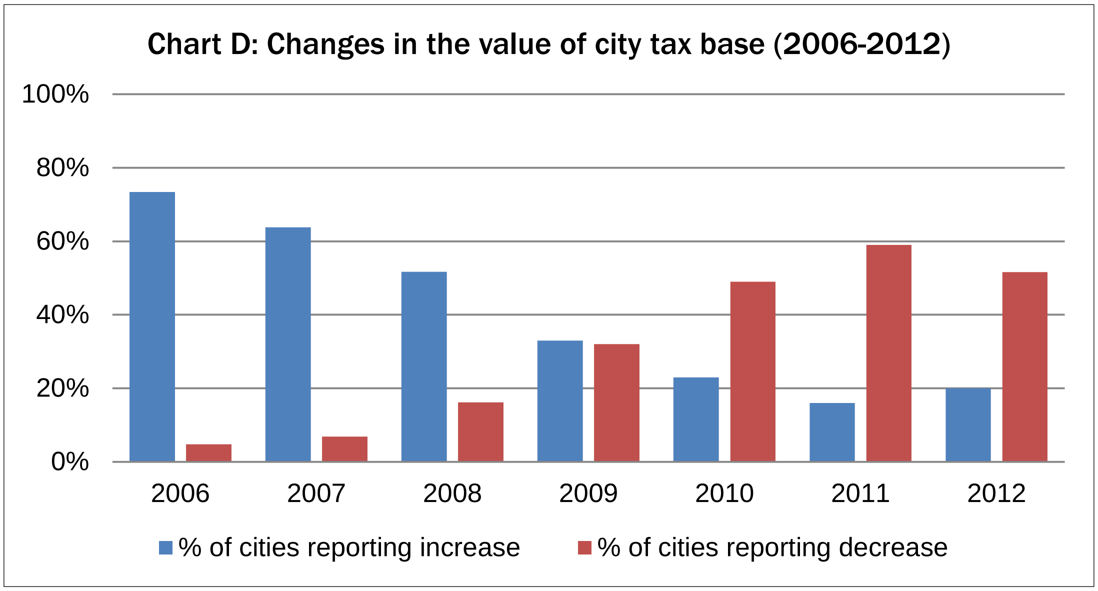
[13] Minnesota Association of Realtors. "Annual Report on the Minnesota Housing Market." 2012. Accessed 2/7/2013 at http://www.mnrealtor.com/docs/housing-report/mnar_ann_2012.pdf?sfvrsn=0.

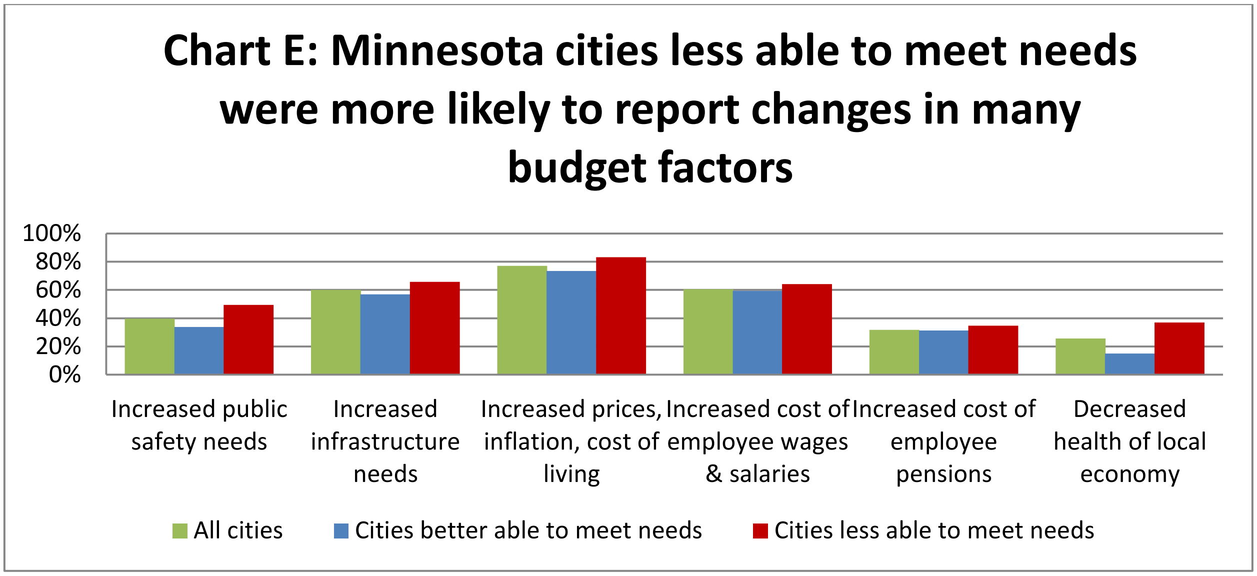


Prices, cost of living, and inflation; cost of employee wages and salaries; infrastructure needs; cost of employee health benefits; and public safety needs were the five budget factors identified by the most cities as having increased in 2012. The same top factors were identified in 2009, 2010, and 2011, with the exception of public safety needs, which replaced the cost of employee pensions in 2011. The share reporting an increase in public safety needs fell from 59 percent in 2011 to 40 percent in 2012. The portion indicating an increase in employee wages and salaries grew from 56 percent in 2011 to 61 percent in 2012. This may be due to cities beginning to retire wage freezes that have been in place for several years. The change over 2011 in the shares reporting an increase in the other factors was very minimal.

Many of these top factors were also the leading factors identified by city officials across the U.S. in the recent NLC survey. The cost of pensions was included in the top five instead of cost of employee wages and salaries. The shares identifying an increase in each factor were larger among city officials nationwide than for officials in Minnesota cities.

The share of cities reporting a decline in the health of the local economy dropped for the third year in a row, from 41 percent in 2011 to 26 percent in 2012. The majority of cities, 52 percent, reported no change in this factor while 19 percent indicated an improvement in local economic health. This suggests that many of the economic problems that have plagued cities are stabilizing and, in some cases, even improving.

Changes in each budget factor influence the ability to which a city is able to meet fiscal needs (see Chart E). How a city is able to respond to changes in these budget factors is dependent on their unique circumstances. Cities less able to meet needs were more likely to report negative changes in many budget factors. The greatest difference between cities better able to meet needs and those less able was in the share reporting a decrease in the health of the local economy (15 percent vs. 37 percent).



Besides being asked how a particular budget factor changed over the last year, cities are also asked to indicate whether each factor had a moderate, major, or no impact on their 2012 budget. For all but three budget factors, the share reporting at least a moderate impact on their budget in 2012 fell from the share doing so in 2011. The greatest increase is in the share indicating at least a moderate impact due to changes in employee wages and salaries (60 percent in 2012 vs. 56 percent in 2011). The largest decrease between 2011 and 2012 was in the share reporting at least a moderate impact due to changes in the value of the tax base (71 percent in 2011 vs. 64 percent in 2012).

The top factors identified as having at least a moderate impact on cities' budgets in 2012 were prices, inflation, and cost of living (73 percent); infrastructure needs (65 percent); tax base changes (64 percent); employee wages and salaries (60 percent); and local economic health (53 percent). The same leading factors were identified in 2011.

A city's ability to meet fiscal challenges is affected not only by the combination of problems it is faced with, but also by how great an impact budget factors actually have on the city. For all budget factors, the share of cities reporting no impact on the budget was greater for those cities that reported being better able to meet needs in 2012. However, for some factors, the difference was very slight. Except for federal environmental mandates, cities that reported a more difficult time meeting needs in 2012 were more likely to indicate a major impact from changes in budget factors. A similar pattern was observed last year.

Cities report utilizing fewer budget strategies in 2012

Highlights of this section

- Almost all cities (95 percent) reported using at least one strategy in 2012. The average number of strategies utilized by a city was 2.69, down slightly from 2011 (3.1 strategies on average).
- Except for revenue increases and increasing efficiencies, both of which saw a very slight increase over 2011, the portion of cities taking action in each category fell in 2012.

What a city does in response to fiscal challenges is influenced by a variety of factors. A city's local tax base, resident needs and preferences, services provided and how they're delivered, local policies and ordinances, state laws and mandates, and opportunities for raising revenue all shape its response. The type of challenge a city is facing also informs the response. Some challenges create cost pressure while others leave the city with less revenue. The strategy selected must address the problem faced. Additionally, cities are only able to do what they have been authorized by the state to do. For example, unlike cities in other states, most Minnesota cities cannot implement a sales tax. Given all of these factors, not every strategy is feasible for every city.

Years of state aid and credit reimbursement payment cuts combined with broad economic challenges have lead many cities to adjust how they budget. Some develop budgets that minimize or eliminate reliance on state aid payments, intending to use any funds received for one-time expenditures. Others have begun to try new strategies, perhaps relying on others less, as they confront various challenges.

Cities were asked to identify the strategies taken in 2012 in preparation for 2013. Almost all cities (95 percent) reported taking at least one strategy in 2012. The average number of strategies employed by a city was 2.69, down from prior years (see Table C). The share of cities utilizing between one and three strategies increased over 2011, growing from 59 percent to 69 percent in 2012. Accordingly, the shares of cities utilizing greater numbers of strategies are down. These trends were also observed last year. This suggests that cities are increasingly able to meet challenges with a smaller number of strategies, or perhaps they no longer have the option to implement certain strategies. The share of cities that reported taking no strategies in 2012 was 5 percent, equal to the share that indicated no strategies in 2011.

Table C: Number of budget-balance actions employed by Minnesota cities in 2012

	Implemented in 2012
Average number of strategies per city	2.69
1 - 3 strategies	69%
4 - 6 strategies	21%
7 - 13 strategies	4%
No reported strategies	5%

Most of the strategies cities are asked about can be grouped into broad categories. Trends in these categories for the past 10 years are shown in Table D. The revenue increases category is comprised of property tax increases and increases in fees, charges, and license fees. Cuts in infrastructure, public safety, and other spending, as well as reductions in the overall growth rate of spending, are included in the spending category. Increasing efficiencies includes increases to productivity levels, contracting out or privatizing, and increasing inter-local agreements.

Table D: Budget-balancing actions taken by Minnesota cities (2003-2012)

	Revenue increases	Spending decreases	Increasing efficiencies	Workforce cuts	Service cuts	Draw down reserves
FY2003	85%	55%	33%	26%	20%	60%
FY2004	84%	47%	34%	22%	15%	46%
FY2005	83%	12%	32%	5%	9%	33%
FY2006	83%	11%	31%	5%	3%	31%
FY2007	85%	12%	32%	6%	6%	32%
FY2008	76%	32%	26%	15%	13%	47%
FY2009	70%	46%	29%	26%	16%	44%
FY2010	71%	35%	30%	25%	16%	35%
FY2011	68%	32%	30%	20%	11%	40%
FY2012	69%	22%	31%	16%	9%	32%

Except for revenue increases and increasing efficiencies, both of which saw a very slight increase over 2011, the portion of cities taking action in each category fell in 2012. The share drawing down reserves decreased after a bump up last year.

While the share of cities implementing spending decreases fell for the third year in a row, this does not mean that cities are spending more. Just 12 percent of cities reported an increase in each of the four actions that comprise the spending category. Almost 80 percent of cities reported no change in at least one of the actions that comprise the spending decreases category. Just under 20 percent reported no change in all four actions in this category. Continually cutting spending may not be possible in some instances without hampering service levels. Delaying spending, especially in regards to infrastructure improvements, may come with added costs as conditions deteriorate. Some costs may be out of the control of cities.

Table E: Specific budget-balancing actions taken by Minnesota cities (2007-2011)

	Increase in taxes	Increase in fees/charges	Decrease in growth rate of spending	Decrease in infrastructure spending	Decrease in public safety spending	Decrease in other spending	Increase in number/scope of inter-local agreements
FY2007	79%	36%	5%	6%	3%	4%	12%
FY2008	67%	36%	14%	20%	11%	18%	13%
FY2009	61%	35%	30%	21%	17%	33%	13%
FY2010	60%	37%	20%	14%	13%	23%	14%
FY2011	55%	33%	18%	12%	10%	17%	17%
FY2012	58%	30%	9%	10%	7%	8%	15%

The proportion of cities implementing tax increases was up slightly after trending downward for four years (see Table E). Of those indicating an increase for 2013, 88 percent reported that this increase was slight. Almost one-third of cities made the policy decision to reduce or hold taxes steady in 2013, perhaps out of recognition of the economic challenges facing taxpayers. Statewide, city levies for 2013 are up just 2.27 percent over 2012. While the shares reporting decreases in the spending categories are down, the portion indicating no change was the largest in each category. For several actions, differences in the share that reported change are very slight when compared with 2011. This may be partially reflective of the fact that a different mix of cities responds to the survey each year. It may also provide further support of the idea that cities are adjusting to the new normal and adapting to meeting different challenges.

While the share of cities reporting an increase in the number or scope of inter-local agreements is down slightly from 2011, many cities are actively engaged in these types of arrangements. Less than 1 percent reported a decrease in this category while 72 percent reported making no changes. Many cities have been working collaboratively for years, although there has been a renewed push for cities to work together in light of budget challenges. Some cities may wish to enter into these types of partnerships but may need to overcome barriers to collaboration.

Human resource-related changes are another way cities may address budget challenges. For the third year in a row, the portion of cities taking these types of actions fell from the prior year (see Table F). The share of cities taking each action in 2012 was down from or the same as in 2011. Cities may not be able to take further or continued action without severely influencing service levels. After several years of not increasing employee wages, some cities are beginning to implement increases again. Just 1 percent of cities reported an increased use of furloughs in 2012. The same size share reported a decreased use of furloughs in 2012. Almost half of cities do not have the use of furloughs as an option.

Table F: Percentage of cities making HR-related budget-balancing reductions

	2009	**2010**	**2011**	**2012**
Reduced workforce	26%	25%	20%	16%
Cut or maintained wage levels	65%	63%	48%	39%
Increased use of furloughs	6%	3%	1%	1%
Reduced employee benefits	11%	9%	8%	6%
Made at least one HR action	74%	70%	61%	51%

Cities responding to the recent NLC survey were also asked about actions taken to address budget challenges.[14] The most common spending-related actions reported by officials nationwide were reductions to the size of the municipal workforce, capital project delays or cancellations, and cuts to services other than public safety, human-social services, and education (48 percent, 33 percent, and 25 percent). The share taking action in each of these categories is down substantially from the share doing so in 2011. The leading revenue-related actions were increases to the level of fees, increases to the number of fees, and property tax rate increases (43 percent, 23 percent, and 22 percent).

[14] The list of actions cities were presented with differed from that on the Minnesota survey. Cities in different states may have different actions and strategies available to them.

Conclusion

The share of cities reporting an improvement in fiscal conditions climbed over 50 percent for the first time since 2006. It must be remembered that the ability to meet needs is a relative measure and does not indicate how well a city is able to meet needs. In other words, conditions may be better than last year but still not "good." Ongoing fiscal challenges may have led cities to adjust expectations for their ability to meet needs. Cities have also utilized a variety of strategies—cutting spending, reducing staff, or doing things differently—that have influenced their ability to meet needs going forward. The specific needs of a community may also have changed. After several years of a down, and then recovering, economy, cities have adapted to operating in the new normal.

Like cities overall, the share of cities in each size category reporting an easier time meeting needs increased, sometimes dramatically, over 2011. As in past years, metro cities were more likely to report more favorable conditions in 2012 than were cities in Greater Minnesota.

The share of cities reporting a shortfall in 2012 fell or stayed the same across all revenue sources. While this is the second year in a row that the share reporting a shortfall in property tax revenue has fallen, over 50 percent of cities continued to see a shortfall. Unlike in previous years, cities had more time to plan for state aid cuts in 2012.

How well a city is able to meet fiscal needs is influenced by changes in a variety of budget factors. This year, many factors saw little difference from 2011 in the share reporting no change in 2012. Reversing trends seen since 2006, the share of cities reporting an increase in the tax base rose in 2012 while the share reporting a decrease fell. Over half of cities still report a decline in the value of the city tax base. One of the influences on a city's ability to meet fiscal needs is the impact that changes in budget factors has on the city. The top factors identified as having at least a moderate impact on cities' budgets in 2012 were prices, inflation, and cost of living; infrastructure needs; tax base changes; employee wages and salaries; and local economic health.

A city's response to fiscal challenges is dependent on a variety of factors. Cities were asked to identify the strategies taken in 2012 in preparation for 2013. Almost all cities reported undertaking at least one strategy. Except for revenue increases and increasing efficiencies, both of which saw a very slight increase over 2011, the portion of cities taking action in each category fell in 2012.