INFORMATION MEMO

Budget Guide for Cities

Learn about new and current state and federal laws that significantly affect city budget decisions, including annual financial figures for minimum wage, cost-of-living adjustments, local government aid (LGA), and more. Includes information on taxation notification procedure for fuel excise tax.

RELEVANT LINKS:

I. Basic budget information

This guide presents recent legislative and administrative changes, as of its revision date, which might be considerations in developing a budget for the coming year. Please note, this guide reflects changes following the 2020 regular legislative session, and it will be updated to account for changes due to subsequent special sessions as appropriate. Basic budgeting for cities, such as how to compose an annual budget and the legal timeline for budgeting, are not in this guide. Please see chapters 20 and 21 of the Handbook for Minnesota Cities for this information.

Handbook chapter 20 describes what a budget is, and how to use it to communicate to the public. It describes what revenues and expenditures a city must examine as a necessary part of budgeting, other factors that may affect the city’s budget, and where to find more information on the budgeting process.

Handbook chapter 21 gives more background information on taxes and taxation notification law. For information on the new laws affecting cities, see the League’s 2020 Law Summaries, which will be released as soon as possible after the Legislature’s special session or sessions.

II. Local government aid (LGA)

The House Research Department has updated estimates of 2021 LGA and a wealth of other related data. City officials should keep in mind that the amounts displayed in the revenue document are estimates only at this point. Aid amounts for 2021 will be certified by July 2020.

III. Legislative changes for 2020

Every year, the League offers the Law Summaries, a comprehensive guide to changes and proposed changes from the last legislative session(s). With the current COVID-19 pandemic impacting the legislative session, this information will be updated as more information becomes available.
Budget-related highlights from the 2020 regular legislative season include the following.

**Onetime exception to restrictions on use of Minnesota Investment Fund (MIF).** Effective March 29, 2020, cities that have uncommitted money in their revolving loan fund (RLF) may use those funds to issue loans to retail stores, service providers, hospitality businesses, as well as for any purposes provided in the MIF statute. This authority extends to the end of fiscal year 2020.

This exception is in addition to similar legislation from the 2019 special session. The 2019 exception provided that cities could use 80% of the uncommitted money as a general purpose aid for any lawful expenditure, provided the other 20% of the money was transferred to the state by June 30, 2020.

In either case, cities that take advantage of this authority must submit to “the chairs of the legislative committees with jurisdiction over economic development policy and finance” an accounting and explanation on the use and distribution of the funds by Feb. 15, 2021.

Cites wishing to take advantage of this should contact the Department of Employment and Economic Development (DEED) and fill out a Request for Exception Form.

**Modification of expenses relating to charter commissions.** Members of the commission are still not entitled to compensation; however, the commission may employ an attorney and other personnel to assist in the drafting and production of the charter. The amount of reasonable and necessary charter commission expenses that shall be paid by the city is the greater of .07% of the city’s current certified property tax levy, or $1,500. These expenses are not to exceed $20,000 in any one year. However, the council may authorize additional expenses. This change takes effect Aug. 1, 2020.

**Local grants to support election efforts.** Although grants are speculative sources of money and may or may not affect a given city’s budget, cities should be aware that local grants are available from the secretary of state for the purposes of:

1. Ensuring the health and safety of election officials and voters.
2. Doing public outreach and preparing to conduct elections with social distancing.
3. Facilitating increased absentee voting.
4. Training and preparing training materials for election officials.
5. Preparing new polling location.
6. Acquiring an electronic roster system and equipment.

Cities must apply to the secretary of state. The deadline for this application has not yet been set. This authority takes effect as of July 1, 2020, with the funds to be available until March 27, 2022, at the latest.
IV. Taxation notification procedure

The table below outlines the annual taxation notification procedure and deadlines (sometimes called “truth in taxation” or “TNT”). The deadline for cities to adopt the preliminary tax levy and certify it to the county auditor is Sept. 30. The deadline for “special taxing districts,” such as economic development authorities (EDAs), housing and redevelopment authorities (HRAs), port authorities, and others, is also Sept. 30.

According to the Department of Revenue, cities with populations of 500 or less and all special taxing districts (except the Metropolitan Council, the Metropolitan Airports Commission, and the Metropolitan Mosquito Control Commission) are exempt from the requirement to hold a meeting with public input prior to adoption of the final levy. All cities, including cities with populations of 500 or less, and special taxing districts must still certify proposed property tax levies to the county auditor on or before Sept. 30, 2020.

<table>
<thead>
<tr>
<th>Taxation Notification Summary Chart for Taxes Payable 2021</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Date</strong></td>
</tr>
<tr>
<td>On or before Sept. 30</td>
</tr>
<tr>
<td>On or before Sept. 30</td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td></td>
</tr>
</tbody>
</table>
### Relevanl Links:

<table>
<thead>
<tr>
<th>Date Range</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Nov. 11 to Nov. 24</td>
<td>County auditor prepares and sends parcels specific notices.</td>
</tr>
<tr>
<td>Nov. 25 to Dec. 28</td>
<td>Cities of population greater than 500 hold meeting (at 6 p.m. or later) to discuss the budget and property tax levy and, before a final determination, allows public input.</td>
</tr>
<tr>
<td>On or before Dec. 28</td>
<td>Cities certify the final levy. Cities must also file the certificate of compliance with the Department of Revenue by Dec. 28, 2020. The Department usually supplies a Form TNT for these purposes closer to the time of certification.</td>
</tr>
</tbody>
</table>

Minn. Stat. § 275.07, subd. 1.


Social Security Administration, Election Workers (Defined). Election Officials and Workers.

Internal Revenue Service, Election Workers: Reporting and Withholding.

PERA Employer Manual, Ch. 3. Minn. Stat. § 353.01, subd. 2(a)(3).

All cities and special taxing districts must certify the final property tax levy to the county auditor on or before Dec. 28, 2020 (five working days after Dec. 20). If this deadline is missed, the final levy will stay the same as it was in the preceding year.

### V. Election judge wages and withholding

**Income tax withholding.** Election judges’ pay is exempt from state and federal income tax withholding. Election judges are responsible for declaring the wages as personal income and may have to pay income tax depending on the judge’s personal situation—but the city need not withhold income taxes.

**Federal and/or state tax withholding, including withholding for Social Security and Medicare.** If an election judge is paid less than $1,900 in 2020, no Social Security or Medicare taxes are withheld. Cities do not need to issue W-4s for judges earning less than $1,900. At the time of publication, the threshold for 2021 had not been established.

**Issuing W-2s.** If an election judge earns $600 or more in a year, cities must issue that person a W-2. According to IRS contacts, W-2s may be issued to judges earning less than $600 for software and bookkeeping purposes.

**PERA withholding.** Election judges are local governmental employees, but the wages earned in these positions are not subject to PERA withholding. For example, if a city employee is also employed by the city as an election judge, the wages earned as a city employee are subject to PERA withholding (assuming the earnings threshold is met).

However, any wages paid for the election judge services must be subtracted from the gross wages prior to calculating the PERA contributions, as the earnings as an election judge are excluded from PERA withholding.
Payroll. The federal government classifies election judges as employees. Therefore, it seems reasonable to pay them through the payroll system, rather than other accounts, to ensure accurate tracking of wages paid to each judge. However, this is offered as a practical tip, not as a requirement in law or rule.

VI. Employment-related changes

A. Optional standard IRS mileage rate

IRS Standard Mileage Rate for 2020 is 57.5 cents per mile for business miles driven, down from 58 cents for 2019.

The IRS normally updates the mileage rates once a year in the fall for the next calendar year. At the time of publication, 2021 rates are not yet available.

B. 2020 PERA contribution rates

The 2020 regular legislative session resulted in no changes to employer or employee contributions to either the defined benefit or defined contribution plans.

<table>
<thead>
<tr>
<th>EMPLOYEE CONTRIBUTIONS</th>
<th>Calendar year 2020</th>
<th>Calendar year 2021</th>
</tr>
</thead>
<tbody>
<tr>
<td>Defined Benefit Plan (DBP)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Basic</td>
<td>9.10%</td>
<td>9.10%</td>
</tr>
<tr>
<td>Coordinated</td>
<td>6.50%</td>
<td>6.50%</td>
</tr>
<tr>
<td>Police and Fire</td>
<td>11.8%</td>
<td>11.8%</td>
</tr>
<tr>
<td>Defined Contribution Plan (DCP)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Elected Officials</td>
<td>5.00%</td>
<td>5.00%</td>
</tr>
<tr>
<td>Physicians</td>
<td>5.00%</td>
<td>5.00%</td>
</tr>
<tr>
<td>City Managers/Administrators</td>
<td>6.25%</td>
<td>6.25%</td>
</tr>
<tr>
<td>Ambulance/Rescue Squad Personnel</td>
<td>Rate set by employer</td>
<td>Rate set by employer</td>
</tr>
<tr>
<td>Certain volunteer or on-call firefighters not covered for that service by the PERA Police and Fire Plan or by a relief association under chapter 424A.</td>
<td>7.5% or more made either solely from compensation paid to the firefighter or through a combination of member and employer contributions.</td>
<td>7.5% or more made either solely from compensation paid to the firefighter or through a combination of member and employer contributions.</td>
</tr>
</tbody>
</table>
## EMPLOYER CONTRIBUTIONS

### Defined Benefit Plan (DBP)

<table>
<thead>
<tr>
<th></th>
<th>Calendar year 2020</th>
<th>Calendar year 2021</th>
</tr>
</thead>
<tbody>
<tr>
<td>Basic</td>
<td>11.78%(^1)</td>
<td>11.78%</td>
</tr>
<tr>
<td>Coordinated</td>
<td>7.50%(^2)</td>
<td>7.50%</td>
</tr>
<tr>
<td>Police and Fire</td>
<td>17.7%</td>
<td>17.7%</td>
</tr>
</tbody>
</table>

### Defined Contribution Plan (DCP)

<table>
<thead>
<tr>
<th></th>
<th>Calendar year 2020</th>
<th>Calendar year 2021</th>
</tr>
</thead>
<tbody>
<tr>
<td>Elected Officials/Physicians</td>
<td>5.00%</td>
<td>5.00%</td>
</tr>
<tr>
<td>City Managers/Administrators</td>
<td>6.5%</td>
<td>6.5%</td>
</tr>
<tr>
<td>Ambulance or Rescue Squad Personnel</td>
<td>Rate set by employer</td>
<td>Rate set by employer</td>
</tr>
<tr>
<td>Volunteer or On-call Firefighters not covered for that service by the PERA Police and Fire Plan or by a relief association under chapter 424A.</td>
<td>7.5% or more made either solely from compensation paid to the firefighter or through a combination of member and employer contributions</td>
<td>7.5% or more made either solely from compensation paid to the firefighter or through a combination of member and employer contributions</td>
</tr>
</tbody>
</table>

1. This represents the employer match of the Basic Plan employee deduction (9.10%) and an employer additional amount at 2.68%.
2. This rate represents the employer match of the Coordinated Plan employee deduction (6.50%) and an employer additional amount of 1.00%.

In 1997, the Legislature authorized annual aid to public employers to offset a PERA employer contribution rate increase. This statutory authorization expired June 30, 2020, with its final payment occurring December of 2019.

According to PERA, June 2020 was expected to be the time when the plan would be fully funded. However, the PERA Board of Trustees reaffirmed its support for the extension of the aid as part of its 2020 legislative initiatives.

### C. Employee contributions to deferred compensation

**Deferred compensation.** Please note: Each calendar year in the fall, the IRS updates the annual contribution limits, based on cost-of-living adjustments (COLA). *At the time of publication, 2021 information is not available.*
2020 Annual Maximum Contribution Limits*

<table>
<thead>
<tr>
<th>Participant age</th>
<th>Contribution Limits</th>
</tr>
</thead>
<tbody>
<tr>
<td>Under age 50</td>
<td>$19,500</td>
</tr>
<tr>
<td>Age 50 and over</td>
<td>$26,000</td>
</tr>
<tr>
<td>Catch up provision</td>
<td>$39,000</td>
</tr>
</tbody>
</table>

*The maximum deferral amounts change each year due to changes in the COLA, if any. Although the employee contributions to a deferred compensation plan reduce the individual’s taxable income, the city will still need to budget for the employer’s share of Social Security and Medicare to the same extent that these withholdings would be required on the employee’s regular earnings.

D. Social Security and Medicare withholding

The 2021 Social Security and Medicare withholding amounts are not available at the time of this publication.

In 2020, for employers:
- The Social Security tax rate is 6.2%.
- The Medicare tax rate is 1.45%.

This combined rate of 7.65% is unchanged from 2019.

E. Unemployment costs

A conservative estimate of the amount of unemployment benefits a city may pay a laid off employee is approximately half the employee’s average weekly wage, up to the maximum of $740 per week. Most cities are classified as “reimbursing employers.” This means the city reimburses the state for unemployment benefits paid out to a former employee.

F. Health and dental insurance costs

Cities need to make sure they are complying with the federal Affordable Care Act (ACA). On Feb. 10, 2014, the IRS released the final regulations implementing the employer shared responsibility mandate which affects many cities.

While it is unclear what the impacts of the pandemic will be with regard to health insurance costs, it’s possible that some plans may see larger-than-normal cost increases due to the high cost of hospitalization, especially intensive care and ventilators. The city should check with its broker or health plan for more information on projected costs.
The U.S. Department of Labor (DOL) released guidance in 2014 pertaining to employers reimbursing employees for individual health insurance plans, on either a pre-tax or after-tax basis. This guidance primarily affects cities that do not meet the definition of “large employer” under the ACA because large employers typically do not offer this type of arrangement.

Employers are permitted to disregard seasonal employees when determining employer size if the employer’s workforce exceeds 50 full-time equivalent (FTE) employees for no more than 120 consecutive days and the number of employees exceeding 50 during that time were seasonal employees, based upon the prior years’ average number.

While most health care reform provisions apply to employers uniformly, regardless of size, there are a few provisions that may specifically benefit small cities that qualify as small employers. The benefits to small employers include:

- Exemption from penalties since they need not offer coverage.
- Availability of coverage through state exchanges effective Jan. 1, 2014.
- Exemption from reporting health care costs on W-2s.
- The ability to use a SIMPLE Cafeteria Plan.
- Since January 1, 2017, small employers can provide a Qualified Small Employer Health Reimbursement Arrangement (QSEHRA) that reimburses employees for the medical care expenses of the employee, the employee’s spouse, and the employee’s dependent children, including individual health insurance policies purchased on the individual market. Certain requirements must be met before a city offers a QSEHRA.

There are other provisions and compliance issues associated with health care reform for all employers such as requirements for coverage of preventive care, prohibitions against pre-existing exclusions, essential benefits, break times for nursing mothers, and other employee protections.

The Department of Labor and the IRS continue issuing critical guidance regarding implementation details for health care reform. We recommend you visit the League website for the most up-to-date information and guidance on federal health care reform legislation and pending regulations.

The ACA has reporting requirements for providers of health insurance and applicable large employers which must be sent to covered individuals and the IRS which started the beginning of 2016. Cities are encouraged to plan ahead each year to meet the reporting deadlines as they will occur each year and continue with the reporting requirements until further notice.
G. Cost-of-living adjustment information

Cities often look at cost-of-living adjustments when setting salaries for the coming year. One measure is the consumer price index (CPI), published by the Bureau of Labor Statistics, U.S. Department of Labor. The CPI is a measure of the average change over time in prices paid by consumers for goods and services.

The Consumer Price Index (CPI) for the Midwest urban region declined 0.4 percent between April 2019 and April 2020. Other methods of adjusting salaries for inflation may also exist, depending upon the particular city, and these may be used instead of the CPI.

VII. Coverage and dues

These are not guarantees. Annual actuarial reviews, other rate development work, and reinsurance costs will be calculated this fall, at which time LMCIT will be able to give a definite answer on premium rates for 2020-2021. Final rates can vary substantially from our preliminary estimates. For example, preliminary 2019 estimates suggested workers’ compensation rate increases of 5% or less. Projected PTSD claim costs subsequently skyrocketed far beyond expectations, resulting in the need for a 9% rate increase to keep pace with this increase.

There are two circumstances this year that make it particularly difficult to provide guidance on projected premium rate levels with precision:

1) The COVID-19 pandemic is having significant but still unclear impacts on reinsurance costs, losses, the investment environment, city finances, and the overall economic picture; and
2) LMCIT is conducting a fund balance adequacy review project, which could affect our evaluation of how large a fund balance we need

A. LMCIT coverage

Most Minnesota cities are members of the League of Minnesota Cities Insurance Trust (LMCIT) for property, liability, auto, and workers’ compensation coverage. Cities purchasing insurance from a private company should ask their provider about insurance coverage options, claim trends, and costs. Cities looking for possible ways to reduce their premiums can reference the memo Reducing LMCIT Premium Costs.

LMCIT members’ annual premium costs are affected by rates, exposures, and experience. In addition to rates, which are set by LMCIT in the fall, cities’ costs can fluctuate if there are changes in exposures — such as payrolls, city expenditures, or property values — or changes in experience rating for workers’ compensation, municipal liability, or auto liability.
This memo discusses LMCIT experience rating formulas, but generally the formulas compare expected losses for individual members within a recent three-year period to the actual losses during the same period, and if losses are greater (or less) than expected, a premium debit (or credit) is applied.

Below are preliminary estimates for premium rates, which would take effect for property/casualty coverages renewing on or after Nov. 15, 2020, and workers’ compensation coverages renewing on or after Jan. 1, 2021.

As always, cities can check with LMCIT starting in October for an updated outlook on premiums. Or if you’d like to learn more about your city’s specific situation, contact your LMCIT underwriter.

**Workers’ compensation.** Data as of the end of 2019 shows total incurred costs for claims occurring in 2018 and 2019 were relatively high — driven in large part by a rapid increase in PTSD claim costs. There’s still a lot of uncertainty behind how PTSD claim costs will continue to develop.

Further, there’s a lot of uncertainty behind how COVID-19 will impact workers’ compensation costs. A presumption bill was passed for first responders in 2020. While we’re hoping for a companion funding bill, where the state would step in as a financial backstop above a certain dollar threshold, as of the date of this memo (May 26), no such companion bill has been passed.

LMCIT suggests cities allow for a workers’ compensation premium rate increase in the 5% to 10% range, to be safe, recognizing the uncertainty behind so many factors this year.

**Property.** Property losses in 2019 were down from the previous two calendar years but are above the five-year average. Reinsurance costs are a significant part of LMCIT expense for property coverage and, as noted earlier, it’s uncertain how the reinsurance market will behave later this year. Given the experience other pools have had in recent months, we anticipate the possibility for increased costs.

We’re also reviewing how we price individual building types — identifying types of buildings we may be undercharging for or overcharging for based on actual claim experience. It’s likely we will be making some pricing adjustments for specific building types, so depending on members’ specific mixes of building types, some members could see higher or lower premium changes than others.

Given the reinsurance uncertainty and the potential variability by member, for budgeting purposes, cities may want to allow for a 5% to 10% increase for property coverage rates.
**Liability.** Loss costs in 2019 for municipal liability claims were average overall, but patterns for specific types of liability claims continue to evolve, as is the case with police liability, sewer backup liability, employment practices, and land use litigation, for example.

LMCIT suggests cities allow for possible rate increases in the range of 1% to 5%. We hope we’re able to hold rates flat overall, but there’s a chance we’ll need to adjust some specific liability rates.

**Auto.** Auto coverage loss costs in 2019 were a little higher than in previous years, but LMCIT expects overall auto rates to remain relatively stable. We’d suggest allowing for a 1% to 5% increases for auto rates.

### B. League dues

Many factors influence the LMC Board’s decision when setting dues, including cities’ financial situations, inflation, strategic plan initiatives, non-dues revenue sources, and various other factors.

To estimate dues payable Sept. 1, 2021, cities should complete the following three steps:

1. Estimate the city’s population for 2019.
2. Use the estimated population from step 1 with the table below to compute the estimated dues payable Sept. 1, 2020.
3. Take the amount calculated in step 2 and increase it by 3.0% to estimate the dues payable Sept. 1, 2021.

League dues for the upcoming fiscal year (2021) are billed on Sept. 1, 2020, and cover membership from September 2020-August 2021. The estimated dues payable on Sept. 1, 2020 are computed based on the maximum dues schedule below:

<table>
<thead>
<tr>
<th>Population</th>
<th>Amount</th>
<th>Per capita rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>249 OR LESS</td>
<td>$408</td>
<td>0</td>
</tr>
<tr>
<td>250 - 4,999</td>
<td>$142</td>
<td>1.0770</td>
</tr>
<tr>
<td>5,000 - 9,999</td>
<td>$1,124</td>
<td>0.8804</td>
</tr>
<tr>
<td>10,000 - 19,999</td>
<td>$2,437</td>
<td>0.7490</td>
</tr>
<tr>
<td>20,000 - 49,999</td>
<td>$8,316</td>
<td>0.4551</td>
</tr>
<tr>
<td>50,000 - 299,999</td>
<td>$24,617</td>
<td>0.1291</td>
</tr>
<tr>
<td>300,000 AND OVER</td>
<td>$41,459</td>
<td>0.0730</td>
</tr>
</tbody>
</table>

Example: If your city’s estimated 2019 population is 6,251 residents, your estimated dues payable on Sept. 1, 2020, would be $6,627 ($1,124 + 6,251*0.8804). Based on that calculation, your estimated dues payable on Sept. 1, 2021, would be $6,826 ($6,627*1.03).
If you need assistance estimating population or dues, call the League’s assistant finance director.

**VIII. Excise taxes on motor fuel**

Cities are exempt from federal excise tax on diesel fuel and gasoline under various sections of the Internal Revenue Code. Cities may make tax-exempt purchases or apply for a refund of taxes paid upon filing certain certificates.

See IRS Publication 510 Appendix for Model Certificates:
- M - Ultimate Purchaser;
- P - Diesel Fuel Tax Exemption; and
- R – Buyer of Taxable Fuel.