

MINNESOTA • REVENUE

PROPERTY TAX Local Government Aid – Formula Modification

April 5, 2006

Preliminary Analysis

	Yes	No
DOR Administrative Costs/Savings		X

Department of Revenue
Analysis of S.F. 2475 (Skoe) **As Proposed to Be Amended**

	Fund Impact			
	<u>F.Y. 2006</u>	<u>F.Y. 2007</u>	<u>F.Y. 2008</u>	<u>F.Y. 2009</u>
			(000's)	
General Fund	\$0	\$0	(\$40,000)	(\$160,000)

Effective beginning with aids payable in 2007.

EXPLANATION OF THE BILL

Current Law: For determining the amount of local government aid, the city formula aid is equal to the need increase percentage multiplied by the difference between 1) the city's revenue need multiplied by its population, and 2) the sum of the city's net tax capacity multiplied by the tax effort rate, and taconite aids to any city except a city directly impacted by a taconite mine or plant, multiplied by the following percentages:

- 50% for aids payable in 2006;
- 75% for aids payable in 2007; and
- 100% for aids payable in 2008 and thereafter.

The need increase percentage must be the same for all cities, and no city may have a formula aid amount less than zero. The city revenue need is multiplied by the ratio of (i) the annual implicit price deflator for state and local governments for the most recently available year to (ii) the 2003 implicit price deflator.

A city with a population of 10,000 or more in 2000 and located outside the seven-county metropolitan area receives a city aid base determined by its 2000 U.S. Census population, up to a maximum of \$2.5 million.

The maximum aid for any city shall not exceed the sum of (i) 10% of the city's net levy for the year prior to aid distribution plus (ii) the total aid in the previous year. The total aid for a city with a population of 2,500 or more may not decrease from its total aid in the previous year by an amount greater than 10% of its net levy in the prior year. The total aid for a city with a population under 2,500 must not be less than its previous year total aid minus 5% of its 2003 certified aid amount.

The total appropriation for local government aid to cities is limited to \$485,052,000 for aids payable in 2006 and thereafter.

Proposed Law: The bill makes a number of changes to the local government aid formula. The base year of the implicit price deflator ratio used to adjust revenue need for inflation would be changed from 2003 to 2002 for aids payable in 2007, and to year 2000 for aids payable in 2008. The bill would set the need increase percentage at 90% for aids payable in 2008, and 100% for aids payable in 2009. The bill would also eliminate taconite aids from the city formula aid calculation and use current population rather than 2000 Census population to calculate regional center aid base.

As proposed to be amended, the bill would follow current law in that no city may have a formula aid less than zero and the need increase percentage must be the same for all cities.

The bill changes the maximum aid for cities by adjusting the percentage of net levy increase. The total aid for a city shall not exceed the sum of its total aid in the previous year, plus the following percentage of the city's net levy in the previous year:

Aids Payable	% of Levy
2007	30%
2008	50%
2009	50%
2010	10%

The minimum aid for all cities becomes the same. For aids payable year 2007 and thereafter, a city must not receive less than its total aid in the previous year minus 5% of its 2003 certified aid.

The appropriation for local government aid is increased to \$525,052,000 for aids payable in 2007. For aids payable in 2008 and thereafter, there is no set appropriation limit, rather the total aid amount would be determined by the fixed need increase percentage.

REVENUE ANALYSIS DETAIL

- The proposal was analyzed using the baseline 2007 Local Government Aid model.
- The appropriation limit for aids payable in 2007 is increased to \$525,052,000. For aids payable in 2008 and thereafter, there is no set appropriation limit, rather the aid distribution amount would be determined by the fixed need increase percentage. The following table is the estimated cost increase to the state general fund from increasing local government aid:

Aids Payable	Fiscal Year	Estimated Cost Increase to State General Fund
2007	2008	\$ 40 million
2008	2009	\$160 million
2009	2010	\$265 million

REVENUE ANALYSIS DETAIL (continued)

- Eliminating the taconite aid offset from the formula would increase aid to 20 cities receiving taconite aid.
- Using current population to calculate regional center aid base instead of 2000 Census population would make 7 additional cities eligible for the aid base and increase aid to cities with population growth since 2000. Cities with population decline since 2000 would receive a reduced regional center aid base.

Number of Taxpayers: 853 cities eligible to receive local government aid.

Source: Minnesota Department of Revenue
Tax Research Division
http://www.taxes.state.mn.us/taxes/legal_policy