

CITY OF LAKEVILLE, MINNESOTA
EXECUTIVE AUDIT SUMMARY
YEAR ENDED DECEMBER 31, 2017



CliftonLarsonAllen

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June 5, 2018

To the City Council and Management
City of Lakeville, Minnesota

We have prepared this management report in conjunction with our audit of the City of Lakeville, Minnesota's (the City) financial statements for the year ended December 31, 2017. The purpose of this report is to provide comments resulting from our audit process and to communicate information relevant to city finances in Minnesota. We have organized this report into the following sections:

- Audit Summary
- Governmental Funds Overview
- Enterprise Funds Overview
- Government-Wide Financial Statements
- Legislative Updates
- Accounting and Auditing Updates

We would be pleased to further discuss any of the information contained in this report or any other concerns that you would like us to address. We would also like to express our thanks for the courtesy and assistance extended to us during the course of our audit.

The purpose of this report is solely to provide those charged with governance of the City, management, and those who have responsibility for oversight of the financial reporting process comments resulting from our audit process and information relevant to city finances in Minnesota. Accordingly, this report is not suitable for any other purpose.

CliftonLarsonAllen LLP

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Minneapolis, Minnesota
June 5, 2018

AUDIT SUMMARY

The following is a summary of our audit work, key conclusions, and other information that we consider important or that is required to be communicated to the City Council, administration, or those charged with governance of the City.

OUR RESPONSIBILITY UNDER AUDITING STANDARDS GENERALLY ACCEPTED IN THE UNITED STATES OF AMERICA AND GOVERNMENT AUDITING STANDARDS

We have audited the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City as of and for the year ended December 31, 2017, and the related notes to the financial statements. Professional standards require that we provide you with information about our responsibilities under auditing standards generally accepted in the United States of America and *Government Auditing Standards*, as well as certain information related to the planned scope and timing of our audit. We have communicated such information to you verbally, in our Governance Communication Letter, and in our audit engagement letter. Professional standards also require that we communicate the following information related to our audit.

PLANNED SCOPE AND TIMING OF THE AUDIT

We performed the audit according to the planned scope and timing previously discussed and coordinated in order to obtain sufficient audit evidence and complete an effective audit.

AUDIT OPINION AND FINDINGS

Based on our audit of the City's financial statements for the year ended December 31, 2017:

- We issued an **unmodified** opinion on the City's basic financial statements.
- We reported no deficiencies in the City's internal control over financial reporting that we considered to be material weaknesses or significant deficiencies.
- The results of our testing disclosed no instances of noncompliance required to be reported under *Government Auditing Standards*.
- We reported no findings based on our testing of the City's compliance with Minnesota laws and regulations.

Overall, we found the City's financial records to be in excellent condition. This not only provides for an efficient year-end audit, but should also provide confidence in the interim financial data used to manage the City throughout the year.

GOVERNMENTAL FUNDS OVERVIEW

This section of the report provides you with an overview of the financial trends and activities of the City's governmental funds, which include the General, special revenue, debt service, and capital project funds.

These funds are used to account for the basic services the City provides to all of its citizens, which are financed primarily with property taxes. The governmental fund information in the City's financial statements focuses on budgetary compliance, and the sufficiency of each governmental fund's current assets to finance its current liabilities.

PROPERTY TAXES

Minnesota cities rely heavily on local property tax levies to support their governmental fund activities. For the 2016 fiscal year, local ad valorem property tax levies provided 39.8 percent of the total governmental fund revenues for cities over 2,500 in population, and 36.4 percent for cities under 2,500 in population. Property tax levies certified by Minnesota cities for 2017 increased about 5.5 percent over 2016, compared to an increase of 5.5 percent the prior year. Levy limits were not in place for 2016 or 2017.

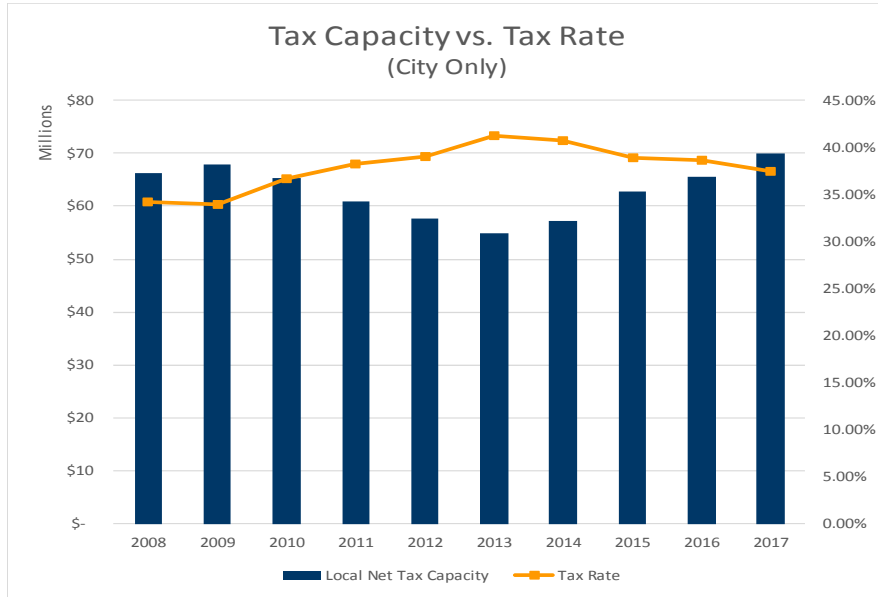
The total market value of property in Minnesota cities increased about 5.6 percent for the 2017 levy year, following an increase of 5.7 percent for levy year 2016, an increase of 8.5 percent for 2015, a slight increase of 1.1% for 2014, and a four-year trend of declining market values for levy years 2010 through 2013. Market values showed increases across all property categories for 2017, with gains in the market values of residential homestead properties (6.9 percent) and non-homestead residential properties (4.8 percent), which were all outpaced by the market value gain of commercial/industrial properties (7.4 percent). Because the assessed valuation used for levying property taxes is based on values from the previous fiscal year (e.g., the market value for taxes payable in 2017 is based on estimated values as of January 1, 2016), market value improvement has lagged behind recent upturns in the housing market and the economy in general.

The City's taxable market value increased 4.9 percent for taxes payable in 2016 and 6.5 percent for taxes payable in 2017. The following graph shows the City's changes in taxable market value over the past 10 years plus 2018:



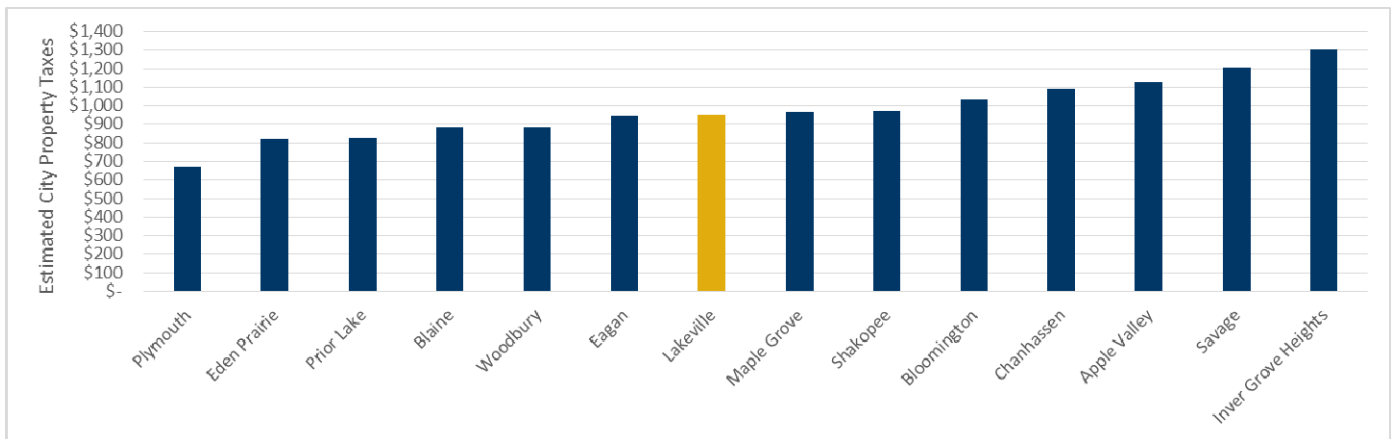
Tax capacity is considered the actual base available for taxation. It is calculated by applying the state's property classification system to each property's market value. Each property classification, such as commercial or residential, has a different calculation and uses different rates. Consequently, a city's total tax capacity will change at a different rate than its total market value, as tax capacity is affected by the proportion of the City's tax base that is in each property classification from year-to-year, as well as legislative changes to tax rates and exemptions. The City's tax capacity increased 6.5 percent and 4.5 percent for taxes payable in 2017 and 2016, respectively.

The following graph shows the City's change in tax capacities over the past 10 years:



The prior year report included a comparison of property tax capacity rates between the City, seven-county metro area, and all cities state-wide average. The 2017 comparison data was not available for the seven-county metro area nor all cities state-wide; therefore, the chart is not included this year.

The following chart provides a comparison of how the City's property taxes compare to other comparable cities:



This chart is based on the City of Lakeville's median home value of \$266,500 and estimated taxable market value of \$252,155. The City of Lakeville when compared to other local cities is right in the middle. This chart is an estimate of only the City's portion of taxes and excludes other taxing jurisdictions (i.e. schools, county, special districts).

GOVERNMENTAL FUND BALANCES

The following table summarizes the changes in the fund balances of the City's governmental funds during the year ended December 31, 2017, presented both by fund balance classification and by fund:

	Fund Balance		Increase (Decrease)
	As of December 31,		
	2017	2016	
Fund Balances of Governmental Funds			
Total by Classification			
Nonspendable	\$ 914,375	\$ 695,830	\$ 218,545
Restricted	29,887,820	37,947,697	(8,059,877)
Committed	26,519,559	21,651,118	4,868,441
Assigned	741,864	1,478,522	(736,658)
Unassigned	12,736,609	12,175,467	561,142
	<u>\$ 70,800,227</u>	<u>\$ 73,948,634</u>	<u>\$ (3,148,407)</u>
Total by Fund			
General	\$ 15,269,442	\$ 15,076,500	\$ 192,942
General Obligation Debt Service	5,176,628	14,903,538	(9,726,910)
G.O. Improvement Debt Service	9,976,390	7,037,315	2,939,075
Building Capital Projects	712,944	808,425	(95,481)
Improvement Construction Capital Projects	937,224	1,450,488	(513,264)
Nonmajor Funds	38,727,599	34,672,368	4,055,231
	<u>\$ 70,800,227</u>	<u>\$ 73,948,634</u>	<u>\$ (3,148,407)</u>

In total, the fund balances of the City's governmental funds decreased \$3,148,407 during the year ended December 31, 2017.

The majority of the decrease was due to the use of restricted fund balances of \$9.7 million which offset an increase in the committed fund balances of \$2.9 million and unassigned fund balances of \$561 thousand, from the prior year. The decrease in restricted fund balances was due to the refunding of the City's Capital Improvement Bonds Series 2007D. The increase in the committed balance was primarily related to the collection of water and sanitary sewer trunk fees in the capital projects funds.

The increase in unassigned fund balance was also primarily due to the City generating \$1.6 million more than budgeted for revenues as well as \$1.1 million under budget on expenditures.

GOVERNMENTAL FUNDS REVENUE AND EXPENDITURES

The following table presents the per capita revenue of the City's governmental funds for the past three years, along with state-wide averages.

We have included the most recent comparative state-wide averages available from the Office of the State Auditor to provide a benchmark for interpreting the City's data. The amounts received from the typical major sources of governmental fund revenue will naturally vary between cities based on factors such as the City's stage of development, location, size and density of its population, property values, services it provides, and other attributes. It will also differ from year-to-year due to the effect of inflation and changes in the City's operation. Also, certain data on these tables may be classified differently than how they appear on the City's financial statements in order to be more comparable to the state-wide information, particularly in separating capital expenditures from current expenditures.

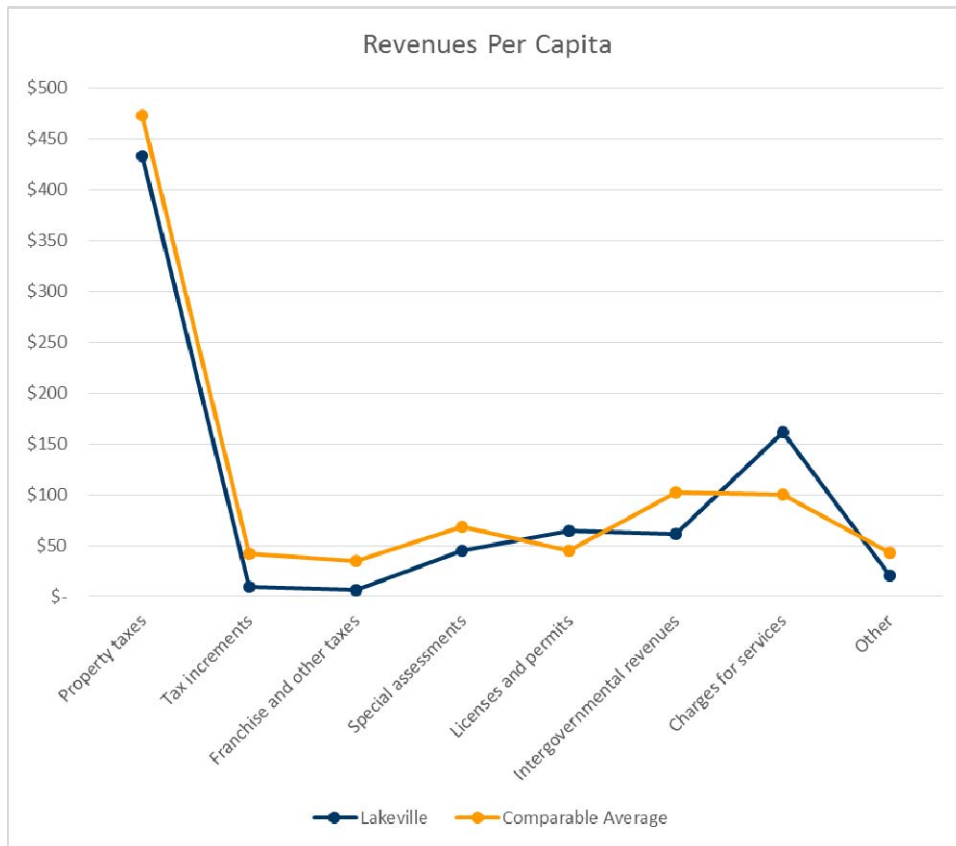
We have designed this section of our management report using per capita data in order to better identify unique or unusual trends and activities of your city. We intend for this type of comparative and trend information to complement, rather than duplicate, information in the Management's Discussion and Analysis. An inherent difficulty in presenting per capita information is the accuracy of the population count, which for most years is based on estimates.

Governmental Funds Revenue per Capita With State-Wide Averages by Population Class				
Year	State-Wide	City of Lakeville		
	December 31, 2016	2015	2016	2017
Population	20,000 - 100,000	59,991	60,965	61,993
Property taxes	\$ 455	\$ 414	\$ 421	\$ 433
Tax increments	42	7	7	9
Franchise and other taxes	45	11	7	6
Special assessments	59	29	38	45
Licenses and permits	42	55	61	64
Intergovernmental revenues	152	87	148	61
Charges for services	103	196	218	162
Other	54	31	29	21
Total Revenue	951	830	929	801

The City's governmental funds have typically generated less revenue per capita in total than other Minnesota cities in its population class.

Total governmental funds revenues were \$49.7 million in 2017, about \$7.0 million (12.3 percent) less than the prior year. On a per capita basis, governmental fund revenue for 2017 was \$128 less than the prior year. Property tax revenue was \$12 per capita higher than the previous year due to a levy increase. Licenses and permits revenue was \$3 per capita higher than last year due to increased development activity. Intergovernmental revenues were \$87 per capita less than last year due to a decrease in municipal state-aid revenue as there were several large capital projects in 2016. Charges for services were \$56 per capita less than last year due to decreased in collections of fees during 2017. Revenue in the "other" category shown above decreased \$8 per capita.

Below is a table of the City of Lakeville’s 2017 governmental funds revenue per capita as compared to the average per capita revenues for the governmental funds of several comparable cities for the year 2016. The comparable cities included in the average below (and in any other instances of a comparable city average included in this report) are Apple Valley, Blaine, Bloomington, Chanhassen, Eagan, Eden Prairie, Inver Grove Heights, Maple Grove, Plymouth, Prior Lake, Savage, Shakopee, and Woodbury.



The expenditures of governmental funds will also vary from state-wide averages and from year-to-year, based on the City’s circumstances. Expenditures are classified into three types as follows:

Current – These are typically the general operating type expenditures occurring on an annual basis, and are primarily funded by general sources such as taxes and intergovernmental revenues.

Capital Outlay – These expenditures do not occur on a consistent basis, more typically fluctuating significantly from year-to-year. Many of these expenditures are project-oriented, and are often funded by specific sources that have benefited from the expenditure, such as special assessment improvement projects.

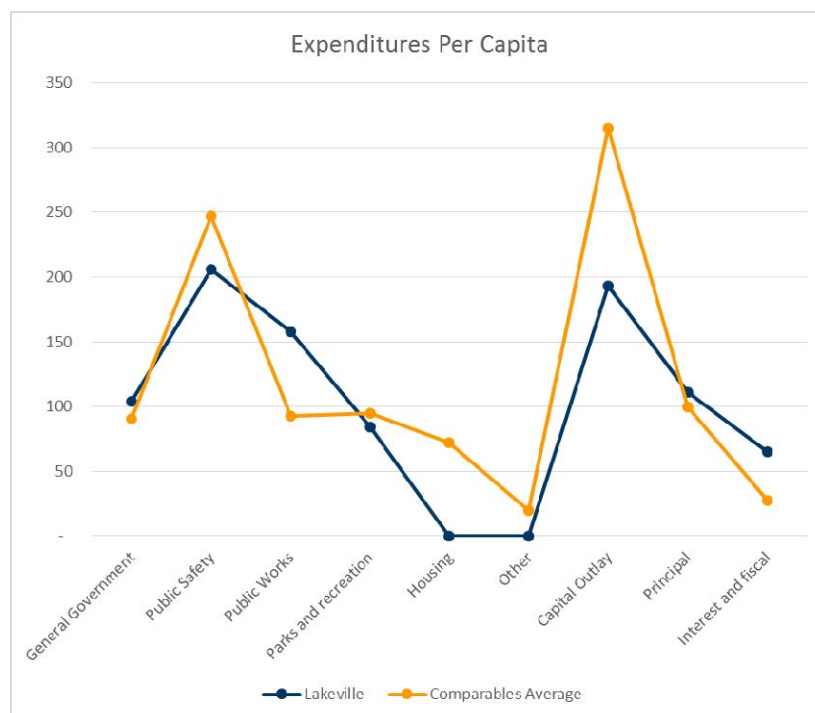
Debt Service – Although the expenditures for debt service may be relatively consistent over the term of the respective debt, the funding source is the important factor. Some debt may be repaid through specific sources such as special assessments or redevelopment funding, while other debt may be repaid with general property taxes.

The City's expenditures per capita of its governmental funds for the past three years, together with state-wide averages, are presented in the following table:

Governmental Fund Expenditures per Capita With State-Wide Averages by Population Class				
Year	State-Wide	City of Lakeville		
	December 31, 2016	2015	2016	2017
Population	20,000 - 100,000	59,991	60,965	61,993
Current				
General Government	\$ 97	\$ 87	\$ 95	\$ 104
Public Safety	273	182	189	206
Public Works	95	64	70	158
Parks and recreation	91	59	57	84
	<u>557</u>	<u>392</u>	<u>411</u>	<u>552</u>
Capital Outlay				
And construction	301	528	622	193
Debt Service				
Principal	115	123	97	111
Interest and fiscal	34	63	70	65
	<u>149</u>	<u>186</u>	<u>168</u>	<u>176</u>
Total Expenditures	<u><u>1,007</u></u>	<u><u>1,106</u></u>	<u><u>1,201</u></u>	<u><u>921</u></u>

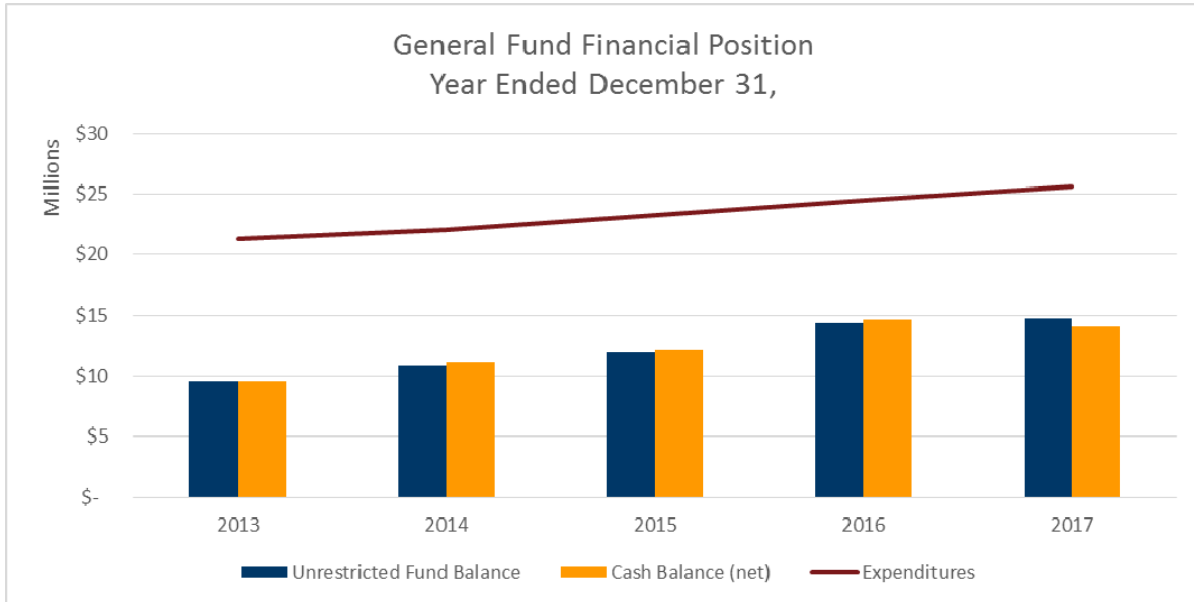
Total expenditures in the City's governmental funds for 2017 were \$57.10 million, a decrease of \$16.1 million (22.0 percent) from the previous year, or \$285 per capita. The decrease was primarily due to capital outlay, which was \$429 per capita less than the previous year, primarily due to several large street and utility improvement projects during 2016. The decrease in capital outlay was offset with increases in public works and parks and recreation spending per capita of \$88 and \$27, respectively. Scheduled debt service principal and interest costs were also \$8 higher per capita than the prior year.

Below is a table of the City of Lakeville's 2017 governmental funds expenditures per capita as compared to the average per capita revenues for the governmental funds of several comparable cities for the year 2016.



GENERAL FUND

The City's General Fund accounts for the financial activity of the basic services provided to the community. The primary services included within this fund are the administration of the municipal operation, police and fire protection, building inspection, streets and highway maintenance, and parks and recreation. The graph below illustrates the change in the General Fund financial position over the last five years. We have also included a line representing annual expenditures to reflect the change in the size of the General Fund operation over the same period.



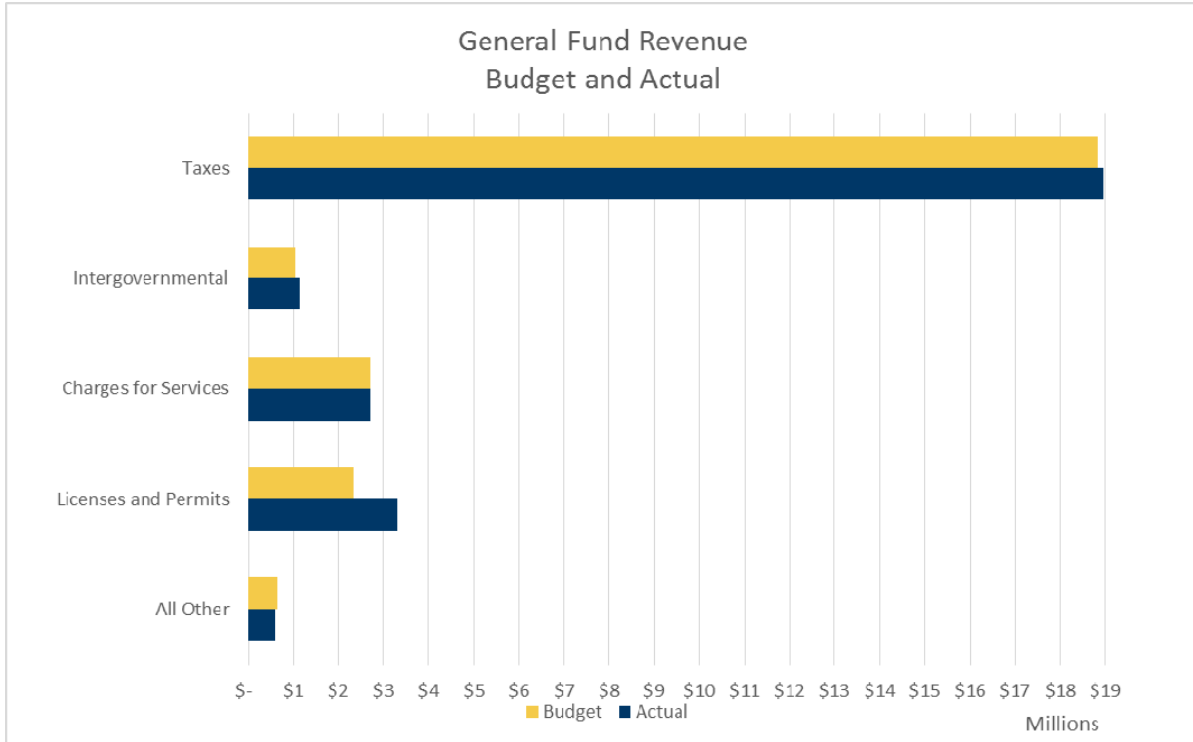
The City's General Fund cash and investments balance at December 31, 2017 was \$14,072,773, a decrease of \$538,098. Total fund balance at December 31, 2017 was \$15,269,442, which is an increase of \$192,942 from the prior year, and \$2,370,495 higher than projected in the City's final budget.

As the graph illustrates, the City has generally been able to maintain healthy cash and fund balance levels as the volume of financial activity has grown. This is an important factor because a government, like any organization, requires a certain amount of equity to operate. A healthy financial position allows the City to avoid volatility in tax rates; helps minimize the impact of state funding changes; allows for the adequate and consistent funding of services, repairs, and unexpected costs; and is a factor in determining the City's bond rating and resulting interest costs. Maintaining an adequate fund balance has become increasingly important given the fluctuations in state funding for cities in recent years.

A trend that is typical to Minnesota local governments, especially the General Fund of cities, is the unusual cash flow experienced throughout the year. The City's General Fund cash disbursements are made fairly evenly during the year other than the impact of seasonal services such as snowplowing, street maintenance, and park activities. Cash receipts of the General Fund are quite a different story. Taxes comprise about 69 percent of the fund's total annual revenue. Approximately half of these revenues are received by the City in July and the rest in December. Consequently, the City needs to have adequate cash reserves to finance its everyday operations between these payments.

The City's General Fund's unrestricted fund balance at the end of the 2017 fiscal year represents approximately 56.1 percent of annual expenditures based on 2017 levels, compared to 58.8 percent at the end of the previous year.

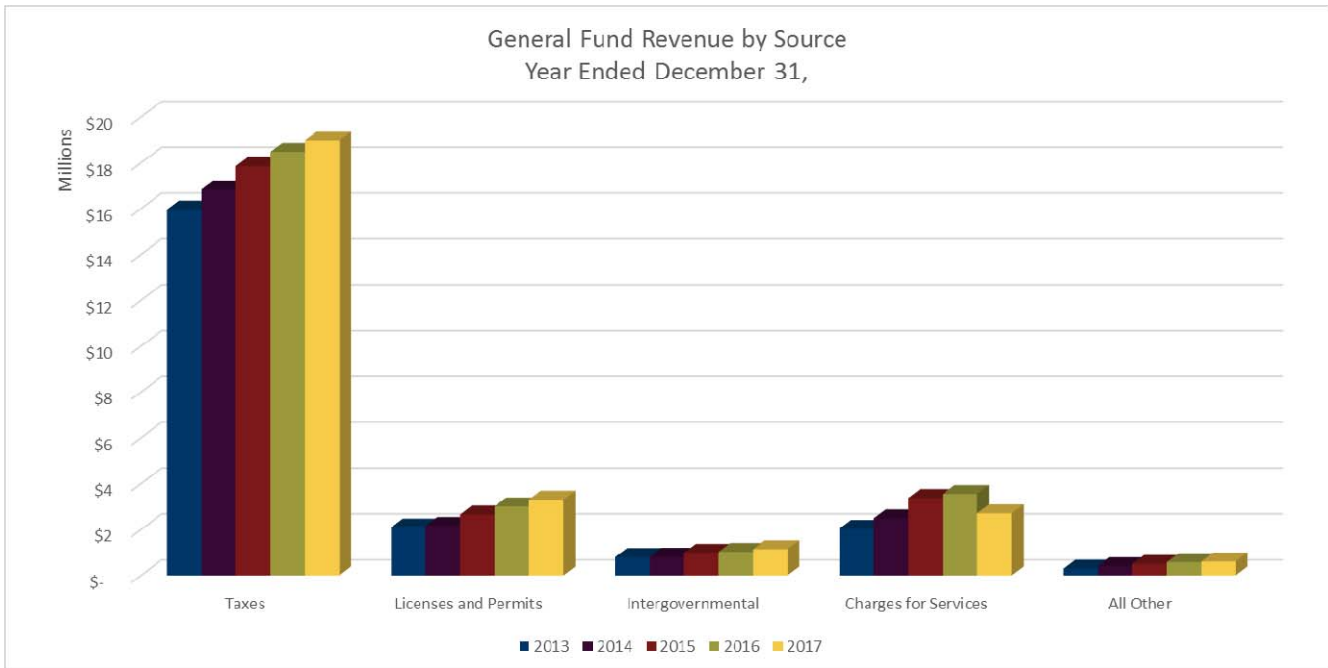
The following graph reflects the City's General Fund revenue sources for 2017 compared to budget:



General Fund revenue for 2017 was \$26,736,039, which was \$1,176,327 (4.6 percent) more than budget.

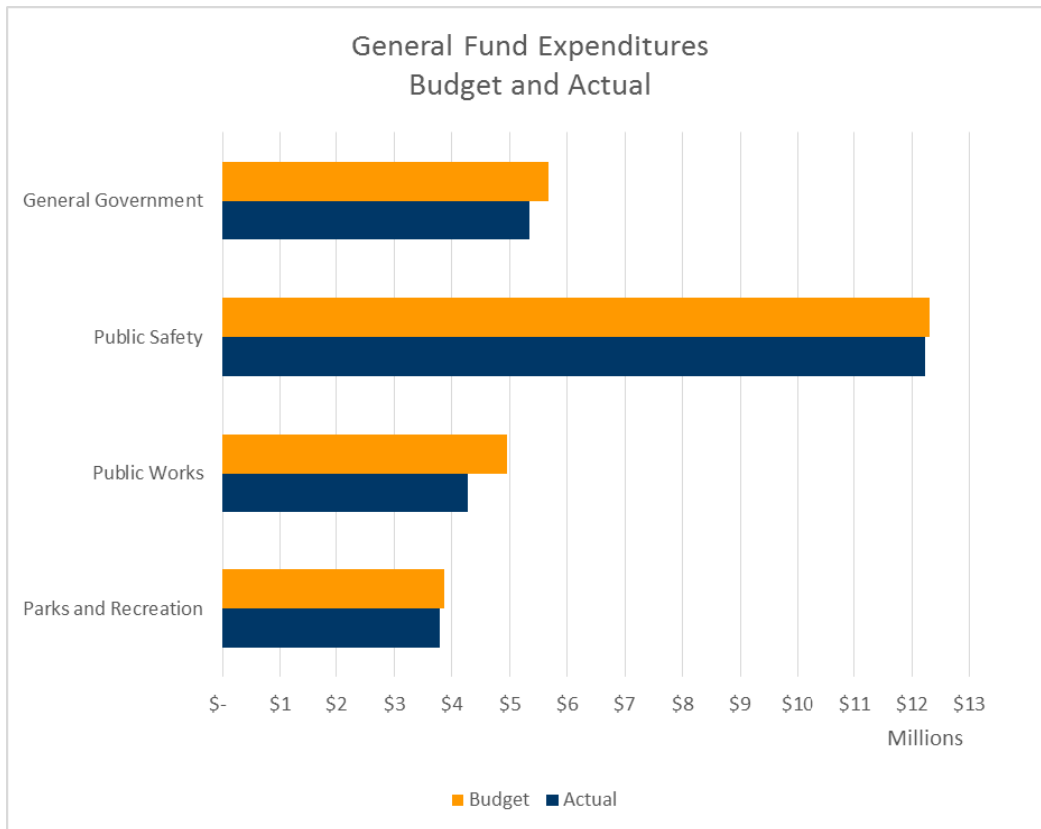
Licenses and permits revenue was over budget by \$965,217, primarily due to the number of residential building and construction related permits issued.

The following graph presents the City's General Fund revenues by source for the last five years. The graph reflects the City's reliance on property taxes and other local sources of revenue.



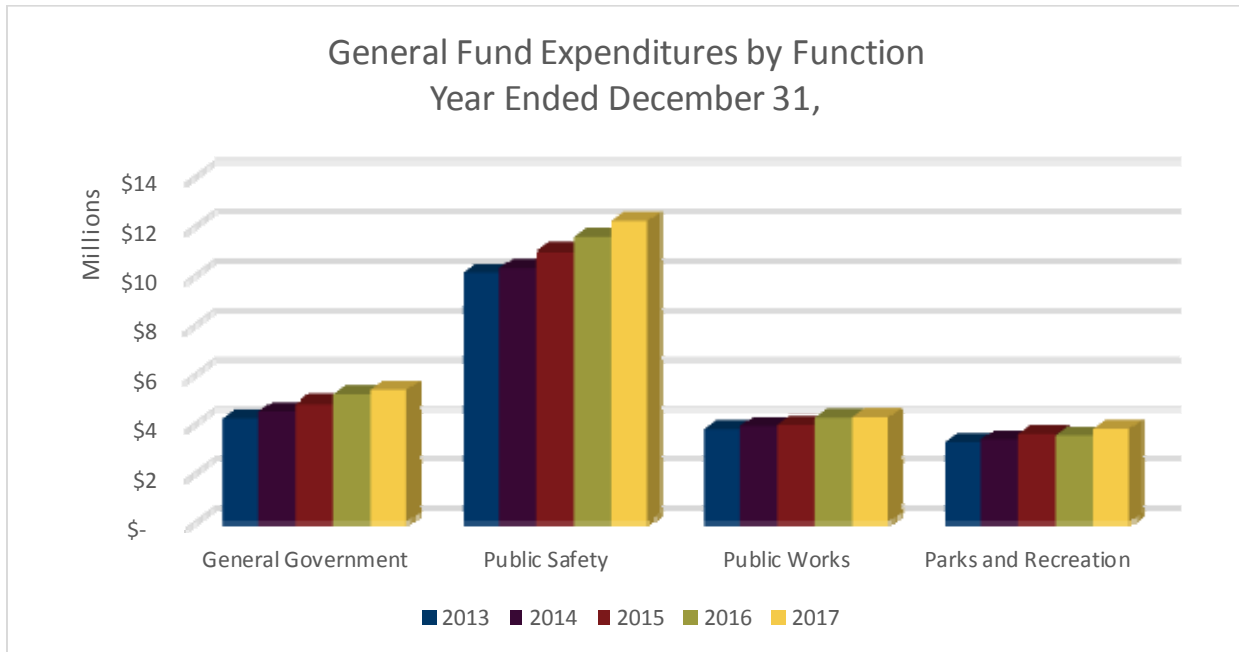
Overall, General Fund revenues increased \$103,858 (0.4 percent) from the previous year. Property tax revenue was \$492,910 more than last year due to a 4.95 percent increase in the property tax levy. Intergovernmental revenue increased \$119,169 due to additional grants being received. Revenue from charges for services decreased \$836,817 due primarily to a decrease in public works fees. Licenses and permits increased \$298,475 due primarily to additional building permits during 2017. Finally, revenue in the “all other” category as shown above was \$30,121 higher than last year, primarily due to an increase in investment returns.

The following graph illustrates the components of General Fund spending for 2017 compared to budget:



Total General Fund expenditures for 2017 were \$25,607,540, which was \$1,194,168 (4.5 percent) under the final budget. General Fund expenditures were under budget in every functional area, as shown in the graph above. General government expenditures were \$333,514 under budget, with the largest savings in planning, community and economic development, inspections, information systems, and human resources. Public safety expenditures were \$87,896 under budget, primarily in police other charges and services and commodities. Public works expenditures were \$675,715 under budget, mainly in engineering other charges and services, operations and maintenance personnel costs, and street maintenance personnel costs. Parks and recreation costs were under budget by \$97,043, mainly in park maintenance personnel and other charges and services.

The following graph presents the City's General Fund expenditures by function for the last five years:



Total General Fund expenditures for 2017 were \$1,156,950 (4.7 percent) higher than the previous year, with the increase spread across all program areas. The majority of the increase was in personnel costs, which were due to contractual wage increases, inflationary benefit cost increases, and the addition of about seven full-time employees compared to the prior year.

ENTERPRISE FUNDS OVERVIEW

The City maintains two enterprise funds to account for services the City provides that are financed primarily through fees charged to those utilizing the service. This section of the report provides you with an overview of the financial trends and activities of the City's enterprise funds, which include the (water, sewer, street light, and environmental resources) Utility Fund and Liquor Fund.

ENTERPRISE FUNDS FINANCIAL POSITION

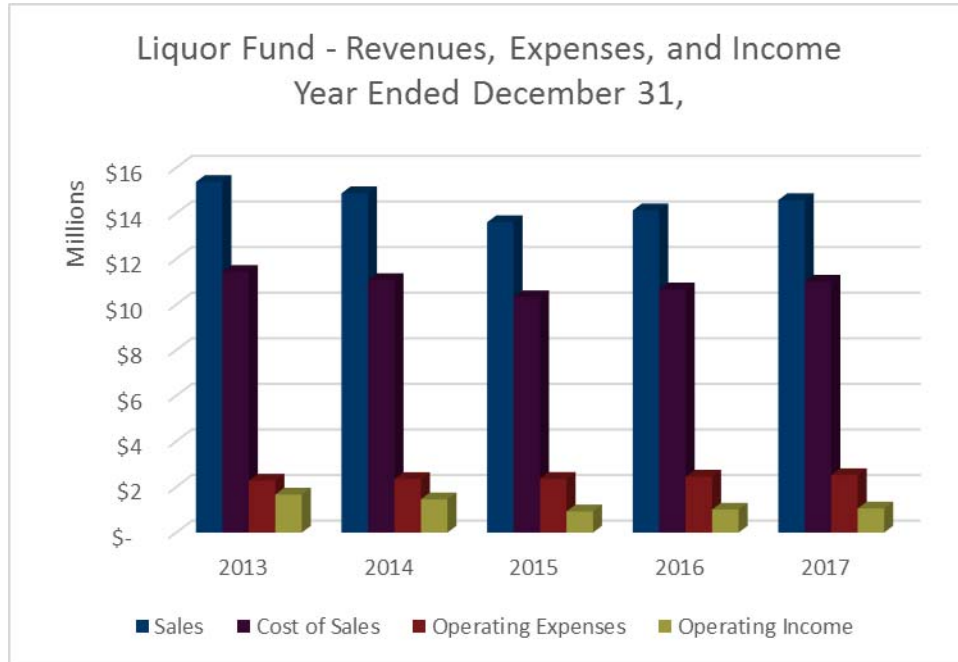
The following table summarizes the changes in the financial position of the City's enterprise funds during the years ended December 31, 2017 and 2016, presented both by classification and by fund:

Enterprise Funds Change in Financial Position			
	Net Position		Increase (Decrease)
	As of December 31,		
	2017	2016	
Net Position of enterprise funds			
Total by classification			
Net Investment in capital assets	\$ 135,324,120	\$ 129,086,090	\$ 6,238,030
Restricted for Debt Service	323,875	323,875	-
Unrestricted	10,627,646	9,584,936	1,042,710
Total Enterprise Funds	\$ 146,275,641	\$ 138,994,901	\$ 7,280,740
Total by Fund			
Liquor	\$ 4,366,329	\$ 3,942,455	\$ 423,874
Utility	141,909,312	135,052,446	6,856,866
Total Enterprise Funds	\$ 146,275,641	\$ 138,994,901	\$ 7,280,740

In total, the net position of the City's enterprise funds increased by \$7,280,740 during the year ended December 31, 2017. The Liquor Fund net position increased by \$423,874, due primarily to net transfers in and out being less than the prior year. Transfers in were \$810 thousand, while transfers out were \$1.3 million. The increases in both the net investment in capital assets and the net position of the Utility Enterprise Fund were primarily due to capital infrastructure contributions of \$9.2 million received from developers, other government agencies, and the City's governmental funds.

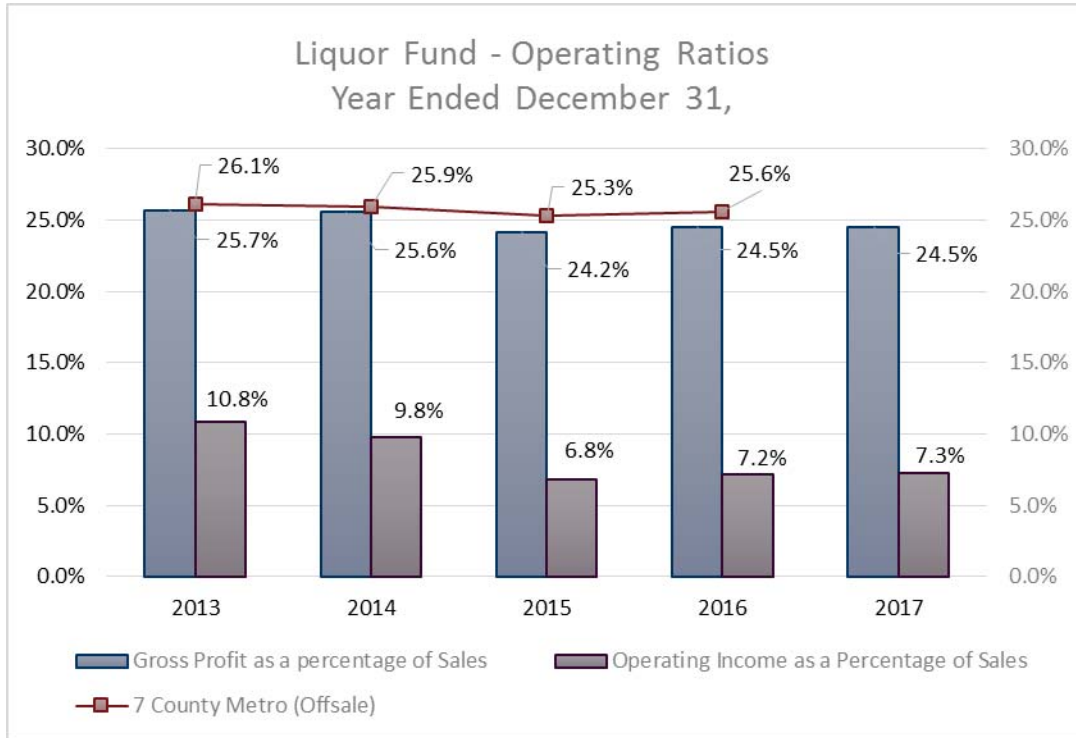
LIQUOR FUND

The following graphs present five years of operating results for the Liquor Fund:



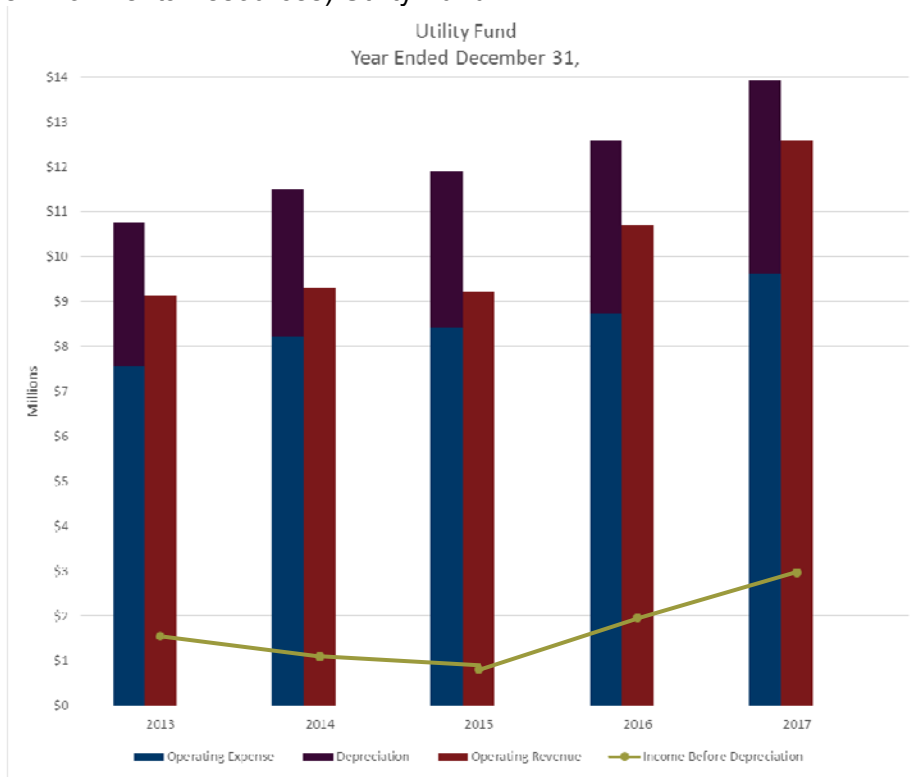
The Liquor Fund ended 2017 with a net position of \$4,366,329, an increase of \$423,874 from current year operations. Of this, \$3,822,026 represents net investment in capital assets leaving an unrestricted net position of \$220,428.

Gross liquor sales for 2017 were \$14,583,514, an increase of \$452,684 (3.2 percent) from 2016. The Liquor Fund generated a gross profit of \$3,578,269 in 2017, or about 24.5 percent, of gross sales. Operating expenses for 2017 were \$2,518,277, an increase of \$64,949 (2.6 percent) from the prior year. Net operating income for 2017 was \$1,059,992, or about 7.3 percent, of gross sales. The increase in gross sales and the resulting increase in the two operating ratios shown below were primarily attributable to stabilization during 2017 as the City has faced significant increases to competition in previous years. The Liquor Fund also made transfers out of \$1,345,322 to support the General Fund, for debt service, and for various capital needs, which was offset by transfers in of \$809,069 due to the transfer of the debt obligation for the Galaxie Liquor Store.



UTILITY FUND

The following graph presents five years of comparative operating results for the City's (water, sewer, street light, and environmental resources) Utility Fund:



The Utility Fund ended 2017 with net position of \$141,909,312, an increase of \$6,856,866 from current year operations. Of the net position balance, \$131,502,094 represents the City's net investment in utility capital assets, leaving \$10,407,218 of unrestricted net position.

Utility Fund operating revenue was \$12,585,450 for 2017, an increase of \$1,893,265 (17.7 percent), mainly due to increase in water usage and sewer discharge coupled with an increase in rates.

Operating expenses (including depreciation of \$4,295,521) were \$13,919,001, which represents an increase of \$1,337,495 (10.6 percent). The increase was primarily attributable to increases in personnel costs and purchased services related to maintenance and depreciation.

The Utility Fund also received capital contributions of \$9,256,100 in 2017 from developers, other governmental agencies, and the City's governmental funds.

GOVERNMENT-WIDE FINANCIAL STATEMENTS

In addition to fund-based information, the current reporting model for governmental entities also requires the inclusion of two government-wide financial statements designed to present a clear picture of the City as a single, unified entity. These government-wide financial statements provide information on the total cost of delivering services, including capital assets and long-term liabilities.

STATEMENT OF NET POSITION

The Statement of Net Position essentially tells you what your city owns and owes at a given point in time, the last day of the fiscal year. Theoretically, net position represents the resources the City has leftover to use for providing services after its debts are settled. However, those resources are not always in spendable form, or there may be restrictions on how some of those resources can be used. Therefore, net position is divided into three components: net investment in capital assets, restricted, and unrestricted.

The following table presents the components of City's net position as of December 31, 2017 and 2016, for governmental activities and business-type activities:

	As of December 31,		Increase (Decrease)
	2017	2016	
Net Position			
Governmental Activities			
Net Investment in capital assets	\$ 144,581,700	\$ 148,684,068	\$ (4,102,368)
Restricted	46,683,603	38,516,463	8,167,140
Unrestricted	6,036,382	2,134,179	3,902,203
Total governmental activities	<u>\$ 197,301,685</u>	<u>\$ 189,334,710</u>	<u>\$ 7,966,975</u>
Business-type activities			
Net Investment in capital assets	\$ 135,324,120	\$ 129,086,090	\$ 6,238,030
Restricted	323,875	323,875	-
Unrestricted	10,791,344	9,757,400	1,033,944
Total business-type activities	<u>146,439,339</u>	<u>139,167,365</u>	<u>7,271,974</u>
Total net position	<u><u>\$ 343,741,024</u></u>	<u><u>\$ 328,502,075</u></u>	<u><u>\$ 15,238,949</u></u>

The total net position of the City increased \$15.2 million during the 2017 fiscal year. Of the increase, \$7.9 million came from governmental activities and \$7.3 million from business-type activities. One of the primary reasons for the increases in both the governmental and business-type activities was the amount of infrastructure contributed by developers and governmental activities during 2017, which totaled about \$16.3 million.

The increase in governmental activities restricted net position was the result of several factors, including an increase in special assessments restricted for future debt service; capital grants (contributions); increases in charges for services and other resources restricted for future capital improvements.

STATEMENT OF ACTIVITIES

The Statement of Activities tracks the City's yearly revenues and expenses, as well as any other transactions that increase or reduce total net position. These amounts represent the full cost of providing services. The Statement of Activities provides a more comprehensive measure than just the amount of cash that changed hands, as reflected in the fund-based financial statements. This statement includes the cost of supplies used, depreciation of long-lived capital assets, and other accrual-based expenses.

The following table presents the change in the net position of the City for the years ended December 31, 2017 and 2016:

	2017		2016	
	Expenses	Program Revenues	Net Change	Net Change
Net (expense) revenue				
Governmental activities				
General government	\$ 4,579,478	\$ 4,479,106	\$ (100,372)	\$ (3,022,427)
Public safety	14,250,572	1,995,696	(12,254,876)	(14,417,433)
Public works	18,944,454	21,482,386	2,537,932	19,237,625
Parks and recreation	6,645,057	2,607,302	(4,037,755)	1,083,534
Interest on long-term debt	3,268,426	-	(3,268,426)	(3,930,168)
Business-type activities				
Liquor	13,638,043	14,590,230	952,187	866,173
Utility	14,138,885	17,542,990	3,404,105	6,218,198
Total net (expense) revenue	<u>\$ 75,464,915</u>	<u>\$ 62,697,710</u>	(12,767,205)	6,035,502
General Revenues				
Property taxes and tax increments			27,317,169	26,173,822
Investment earnings			688,985	459,781
Total general revenues			<u>28,006,154</u>	<u>26,633,603</u>
Change in net position			<u>15,238,949</u>	<u>32,669,105</u>
Net position , beginning			<u>328,502,075</u>	<u>295,832,970</u>
Net position - ending			<u>\$ 343,741,024</u>	<u>\$ 328,502,075</u>

One of the goals of this statement is to provide a side-by-side comparison to illustrate the difference in the way the City's governmental and business-type operations are financed. The table clearly illustrates the dependence of the City's governmental operations on general revenues such as property taxes and unrestricted grants, while its business-type activities are financed predominately through program revenues.

The difference in public works is mainly the result of decreased capital contributions, utility connection charges and special assessments of \$16.7 million during 2017.

LEGISLATIVE UPDATES

Despite the 2018 legislative session ending with a projected budget excess of \$329 million for the 2018–2019 biennium the most recent legislative session made some progress on pensions, bonding, and a few other areas, it resulted in numerous bills being voted and the Governor and Legislators being further apart on their respective views for Minnesota.

The following is a summary of recent legislation affecting Minnesota cities in 2017/2018 and into the future:

Local Government Aid (LGA) – The Legislature completely overhauled the LGA formula for fiscal year 2014 and thereafter, creating a three-tiered formula that includes separate “need factor” calculations for cities with populations under 2,500, between 2,500 and 10,000, or over 10,000. The new formula simplified the LGA calculation, and reduced the volatility of the LGA distribution by limiting the amount it may decline in a given year. Beginning in 2015, any reduction to a city’s calculated LGA distribution will be limited to the lesser of \$10 per capita, or 5 percent of their previous year net tax levy. For cities that gain under the new formula, the increases will be distributed proportionate to their unmet need, as determined by the new “need factor” calculations. The state-wide LGA appropriation was \$516.9 million for fiscal 2016 and 2017, and is \$534.4 million for fiscal 2018 and thereafter. The \$15 million increase in LGA for fiscal year 2018 is a permanent increase which was approved by the omnibus tax bill signed by Governor Dayton. The omnibus tax bills vetoed by Governor Dayton would not have affected LGA in total.

Competitive Bidding – Effective August 1, 2018, the competitive bidding threshold will increase from \$100,000 to \$175,000. This is the first change since 2008 and was made with the support of the League of Minnesota Cities, the Association of Minnesota Counties, the Minnesota Association of Townships, and the Minnesota School Boards Association.

Replacement of Freon Systems – The 2017 Omnibus Tax Bill created a new option for home rule and statutory cities to finance the replacement of Freon-based refrigerant (R-22) in their hockey arenas by issuing capital notes or certificates of indebtedness with up to a 20-year term without voter approval, but are subject to reverse referendum process. The previous limit was 10-years. Chemical producers will no longer be allowed to produce R-22 after January 1, 2020.

Pensions – Governor Dayton signed the Omnibus Pension bill providing additional resources to the PERA – Police and Fire Plan and the State MSRS Plan. It also provides several changes to assumptions for PERA to incorporate which includes rate of return, cost of living adjustments, target funding date, plus several other. It also increased the employee and employer contribution rates effective on January 1, 2019 and another increase set for January 1, 2020. The General Employees Plan’s contribution rates were not adjusted.

Bonding Bill – Governor Dayton signed the \$825 million general obligation bonding bill. The bonding bill provides \$400 million in highway bonds for Corridors of Commerce program, \$35 million in local road improvements, \$39 million in infrastructure funding for drinking water programs, \$80 million in housing infrastructure bonds, and numerous other city-specific projects.

Investment Options – Minnesota Statute Section 118A was amended to allow for additional types of equity investments if a municipality has a AAA bond rating or had a population that exceeded 100,000. The additional investment options include; indexed mutual funds and long-term equity accounts with the State Board of Investment.

Water Tank Service Contracts – Governor Dayton signed into a law a bill which allows for municipalities to enter into multiyear professional services contract for engineering, repair, and maintenance of a water storage tank and appurtenant facility owned, controlled, or operated by the municipality.

Vetoed Bills – Governor Dayton vetoed several bills in the most recent legislative session, these include bills related to tax conformity with the Federal Government, omnibus school and tax bill, the omnibus supplemental budget bill, agriculture policy bill, MNLARS funding, plus several other bills. The majority of these bills were vetoed because Governor Dayton did not view them as addressing enough of his priorities or they did not provide enough funding to where he would support them.

ACCOUNTING AND AUDITING UPDATES

GASB Statement No. 75, “Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions” – the objective of this statement is to improve accounting and financial reporting by state and local governments for postemployment benefits other than pensions (other postemployment benefits or OPEB). The provisions of Statement No. 75 are effective for fiscal periods beginning after June 15, 2017.

GASB Statement No. 83, “Certain Asset Retirement Obligations” – the objective of this Statement is to provide financial statement users with information about asset retirement obligation not previously address in GASB standards, by establishing uniform accounting and financial reporting requirements for these obligations. An example of these assets would be decommissioning a nuclear power plant, wind turbines, sewage treatment facilities, or an x-ray machine. This Statement is effective for periods beginning after June 15, 2018.

GASB Statement No. 84, “Fiduciary Activities” – this Statement establishes criteria for identifying fiduciary activities of all state and local governments. This Statement is effective for periods beginning after December 15, 2018.

GASB Statement No. 86 “Certain Debt Extinguishment Issues” – the primary objective of this Statement is to improve consistency in accounting and financial reporting for in-substance defeasance of debt by providing guidance for transactions in which cash and other monetary assets acquired with only existing resources—resources other than the proceeds of refunding debt—are placed in an irrevocable trust for the sole purpose of extinguishing debt. This Statement also improves accounting and financial reporting for prepaid insurance on debt that is extinguished and notes to financial statements for debt that is defeased in substance. This Statement is effective for periods beginning after June 15, 2017.

GASB Statement No. 87 “Leases” – the primary objective of this Statement is to better meet the information needs of financial statement users by improving accounting and financial reporting for leases by governments. It will require recognition of certain lease assets and liabilities for leases that previously were classified as operating leases and recognized as inflows of resources based on the payment provision of the contract. It also establishes a single model for lease accounting based on the foundational principle that leases are financings of the right to use an underlying asset. This Statement is effective for periods beginning after December 15, 2019.