

Chapter Eight

Revenue, Finance & Debt

§ 8-1. Sources of Town Revenue

There are several sources of town revenue, some of which are available to all townships and others that are available only under certain circumstances. The money from some sources may also come with restrictions on its use. The most common sources of revenue are described here.

A. Property Taxes

Property taxes are the primary source of revenue for town government. The electors set the town's property tax levy at the annual town meeting. The town clerk certifies the amount of the levy to the County Auditor annually by September 15th. A property tax statement is mailed to each property owner showing the amount of the town levy as well as the levies being imposed by other governmental entities. The town receives tax money twice a year, once in June and again in December. Minn. Stat. §§ 276.09; 276.11; 276.111. Any remaining property tax proceeds are distributed in January.

The town levy may be set only at a town meeting. It is important to distinguish between the budget and the levy. The budget is produced by the board to suggest a plan for spending in the next year. The levy is the tax set by the voters, which may consider the budget suggested by the board.

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Because the annual town meeting is held on the second Tuesday in March, some towns find it difficult to predict their financial needs and approve a levy nearly a year in advance. To remedy this, some towns continue the annual town meeting to August so it can better anticipate its financial needs in the upcoming year before setting the levy. Once the levy is set, it still must be certified to the County Auditor by September 15th.

Regardless of how much effort a town puts into determining a budget and setting the levy, it may still be necessary to change the levy after it is set. In that situation, a special town meeting may be called to ask the electors to modify the levy. Towns may modify the levy up to five working days after December 20th. Minn. Stat. § 275.07, subd. 1. If a need arises to modify the levy after September 15th, be sure to notify the County Auditor as soon as possible of the possible change.

B. Aid Programs

Towns receive income from a variety of aid programs established by the state to assist local governments and property owners. Aid programs are discussed at the Legislature every year, and changes are frequently made. Because of the volatile nature of local government aids, towns must be aware of how proposed changes to the programs may affect the town budget. The following are the aid programs that most significantly impact towns.

C. Local Government Aid (LGA)

Local government aid (LGA) is a vital source of funds for local governments; unfortunately, towns have traditionally been at the bottom of the list to receive such aid. The amount of LGA available for towns is set by the Legislature and distributed based on a formula. The formula considers the geographic area of the town, its population, and the amount of agricultural property as a ratio of all other property in the town. Minn. Stat. § 477A.013, subd. 1. The current formula essentially favors towns with larger agricultural areas.

D. Disparity Reduction Aid (DRA)

Disparity reduction aid helps areas where a disparity exists in the amount of taxes imposed across an area. Minn. Stat. § 273.1398. To help address this, the state established a formula the County Auditor uses to reduce the tax rate applied to properties in the more heavily taxed areas. The aid from the state makes up for the rate reduction.

E. Highway Aid

Highway aid is a significant source of financial help for towns. Counties and cities with a population of over 5,000 also receive highway aid. Highway aid is reserved for road building, repair, and maintenance activities only. Highway aid for towns provides funding for both town roads and bridges. Minn. Stat. §§ 161.081, subd. 1; 161.082, subd. 2a.

Much of this aid comes from the state gas tax, a portion of which is placed into a town road account. Minn. Stat. § 162.081. Money from the account is then apportioned to each county based on the total miles of town roads located in the county compared with the overall total of town road miles. The apportioned amount is distributed to the County Treasurer to be redistributed to each town based on a formula adopted by the County Board. The distribution formula must consider each town's levy for road and bridge purposes, its population, the town's road miles, and other factors the county board deems advisable to achieve an equitable distribution among towns. Each town should receive its distribution from the county by March 1.

For a town road to be included in the road mileage for which the town receives a gas tax distribution, the road must be kept open and maintained by the town at least eight months of the year.

The town bridge account provides funds for town bridges that are ten or more feet in length and for culverts that replace existing town road bridges. Minn. Stat. § 161.082, subd. 2a(a). The county engineer inspects town bridges and

those in need of replacement are ranked and placed on a list. When funds become available to replace the bridge, the town works with the county engineer to initiate the replacement project. Towns are usually responsible for paying the engineering and approach work costs for the replacement.

Some towns also receive funds from the state park road account. Minn. Stat. § 162.06, subd. 5. One of the uses for this fund is for the reconstruction, improvement, repair, and maintenance of town roads that provide access to public lakes, rivers, state parks, and state campgrounds.

F. Payment-in-Lieu of Taxes (PILT)

Because the federal and state governments do not pay property taxes on land they own within townships, towns receive money to offset the lost revenue. Minn. Stat. §§ 477A.12-.14; 471.653. These payments, called payments-in-lieu of taxes, are made through the county. The amounts paid depend on factors such as the classification given to a piece of property by the state and the amount of revenue generated on the property.

§ 8-2. Town Debt

Towns incur debt for a variety of reasons, which may range from construction of a town hall to acquisition of a new piece of road equipment. Town debt goes by several names, including “bonds,” “certificates of indebtedness,” and “lease-purchase agreements.” Regardless of its name, public borrowing is not as simple as going to a bank and requesting a loan. As with the exercise of any power granted by the Legislature, it is important for towns to carefully follow the required statutory procedures applicable to the power. Unfortunately, the specific requirements and tax issues associated with incurring debt are often misunderstood.

In some cases, voter approval is required to issue debt. Certificates of indebtedness are an exception to this rule, but they must have a

G. Revenue Distribution Programs

In the Twin Cities metropolitan area, the Metropolitan Revenue Distribution Act was created to redistribute some of the economic benefits occurring in some areas because of commercial development to other areas that were not experiencing the same degree of growth. Minn. Stat. Chap. 473F. A similar, but to date much smaller, program was established for an area including Aitkin, Cook, Crow Wing, Itasca, Koochiching, Lake, and St. Louis Counties. Minn. Stat. Chap. 276A.

H. Mining Taxes

Towns located in the Taconite Tax Relief Area impacted by mining activities receive funds from mining taxes. Distributions are made to towns where mining and concentrating occur and to towns that are affected by mining because they are within three miles of a taconite mine pit. Minn. Stat. § 298.28. A taconite municipal aid account also provides payments to certain towns in September based on a complex formula that considers fiscal need. Minn. Stat. § 298.282.

term of ten years or less. Minn. Stat. § 366.095. Depending on the amount of the certificate of indebtedness compared to the town’s estimated market value, the issuance may also be subject to a petition calling for a reverse referendum.

The interest paid on town debt may be tax free to the recipient. Many banks and other lenders are therefore willing to lend money to a town at a rate below that is charged to private individuals and companies. The tax exemption depends on compliance with federal law and Internal Revenue Service, regulations and many banks will require an opinion from a qualified bond attorney.

Refer to Document **F6000** for additional information on town debt.

§ 8.3. Town Financing Options

Towns have historically borrowed very little, particularly when compared with other units of government. Increasingly, towns are faced with large capital acquisitions — infrastructure projects for roads and bridges, equipment purchases like graders or fire trucks, and construction of buildings — that cannot easily be paid for on a cash basis. Below are some options for financing town purchases.

A. Town Financed

The most obvious method to finance a large project or purchase is for the town to pay the costs with existing funds. If the funds for the project have already been levied and exist in one of the town's account, i.e. road and bridge or fire, it is permitted to undertake the project on its own initiative. If, however, the funds are not already available, the board will likely need to consider incurring debt to secure the needed funds.

If the project is relatively small and the debt incurred can be paid back within ten years, the board can consider issuing **certificates of indebtedness** under Minn. Stat. § 366.095 to finance the project. If the amount of the certificates to be issued does not exceed 0.25 percent of the market value of the town, the board can incur the debt on its own initiative. If the amount exceeds the 0.25 percent, then notice must be published giving the town electors the opportunity to call for a vote on whether to issue the certificates.

Bonds are the common financing tool for larger projects or purchases or those that need to have the payback extended for more than ten years. See Minn. Stat. Chap. 475. With some exceptions, a referendum vote is needed before a town can issue bonds. The cost of issuing bonds is higher than issuing certificates, but bonds are a much more flexible financing

tool. Any board considering whether to use bonds to finance a project or purchase needs to speak with a bond attorney. Having someone knowledgeable with all of the bonding requirements that can walk the board through the procedure is very important to avoid problems that could delay or kill a project.

B. Privately Financed

Occasionally a business owner or a group of owners express a willingness to pay for a town improvement on their own. Usually this will occur with a road project where they wish to pave the road leading to their business. Because there are no statutory procedures specifically addressing privately financed improvement projects, boards must be careful in how they handle such requests.

Another variation boards sometimes encounter involves the group of owners expressing a willingness to pay all of the costs, but asking the town to finance part of the project and assess over time the owners who could not pay up front for their share of the costs. In a sense, it is a special assessment procedure without going through the assessment procedure. This process has been used successfully, but it raises some serious concerns regarding authority and the enforceability of the owner's obligation. If one of the owners sell the property before the obligation is paid in full, the board would have a difficult time collecting any outstanding balance.

If a board is approached with a private financing proposal, it should seek the assistance of an attorney before agreeing to any part of the project. The attorney can help identify if the board has the authority to undertake the project, determine how the project can best be accomplished, and draft the appropriate documents to make the obligation as enforceable as possible.

C. Special Assessment

Perhaps the most common method used to undertake a public improvement project to be paid in part by the benefited owners is the special assessment procedure in Minn. Stat. Chap. 429. All towns are authorized to use the special assessment procedure for road improvement projects and a limited number of other types of improvement projects. Minn. Stat. 429.011, subd. 2b. Towns with urban powers are authorized to use the special assessment procedure for the full range of improvement projects listed in the statute. Minn. Stat. § 429.021, subd. 1.

If a board receives a petition, or is considering initiating a special assessment project, it is strongly encouraged to retain the services of an attorney familiar with the process. There are a number of procedural steps that, if not properly followed, could expose the board to suit and jeopardize its ability to assess owners for the improvement.

Here is the beginning process:

1. **Starting the process.** Either the town board or a petition signed by the affected property owners may initiate the proceedings. Minn. Stat. § 429.031.
2. **Report Prepared.** The town board must have a report prepared on the necessity, cost-effectiveness, and feasibility of the proposed improvement. An engineer or some other competent person prepares the report. Minn. Stat. § 429.031, subd. 1 (b).
3. **Public Hearing Notice.** The town must publish a notice for the public hearing twice in the newspaper, at least one week apart. In addition, the local government must mail a notice to all property owners in the proposed assessment area at least ten days prior to the hearing. Minn. Stat. 429.031, subd. 1(a).
4. **Public hearing.** The public hearing must be at least three days after the second notice in the newspaper. At the hearing, the methodology used in calculating the individual assessments as well as a reasonable estimate of the total amount to be assessed, must be available. **Exception:** A public hearing is not required if 100 percent of the landowners request the proposed assessment. Minn. Stat. § 429.031 subd. 3.
5. **Ordering the Improvement.** If a petition is supported by the owners of at least 35% of the frontage of real property abutting the proposed improvement, then a simple majority of the board may approve the project. Minn. Stat. § 429.031, subd. 1(f). If the local government initiated the proposed assessment, or 35% of property owners did not petition, a four-fifths vote is needed to pass the resolution. *Id.* This means that on a typical three-supervisor town board, a unanimous vote is required to pass the resolution. In both cases, the resolution must be adopted within six months of the hearing.
6. **Prepare Assessment.** Once a town decides to move forward on a project, the actual cost of the project must be determined for assessment purposes. Minn. Stat. § 429.041. The municipal contracting law applies to local improvement contracts. *See Chapter 9.*
7. **Proposed assessment roll.** The town must calculate the proper amount to be specially assessed against each property that will benefit from the improvement. "The cost of any improvement, or any part thereof, may be assessed upon property benefited by the improvement, based upon the benefits received, whether or not the property abuts on the improvement..." Minn. Stat. § 429.051. Because the amount of benefit conferred by an improvement is often contested, a great deal of case law has developed around the special assessment procedure and the permissible methods for determining benefit. Benefit essentially refers to the market value increase in the property as a result of the improvement. In deciding how much it will assess a proper-

ty, the board must determine that the assessment does not exceed the amount of benefit incurred. The method the board intends to use to calculate these amounts must be determined very early in the process. This is just one of the reasons why having the assistance of legal counsel is particularly important before initiating this procedure.

8. **Public hearing on the proposed assessment.** The town must publish notice of the hearing in its official newspaper at least once, not less than two weeks prior to the scheduled meeting. The notice must state the date, time, place, general nature of the improvement, area proposed to be assessed, total amount of the proposed assessment, and describe the process for objecting to the improvement. In addition, the local government must mail a notice to each affected property owner at least two weeks prior to the public hearing on the proposed assessment. The notice must state the amount to be specially assessed against the property owner's property, the prepayment options, the interest rate if the payment is not prepaid, and that the local government may adopt the proposed assessment at that hearing. The notice must also state that no appeal may be made as to the amount of the assessment adopted at the hearing unless the property owner has objected in writing prior to the hearing or in person at the hearing. Minn. Stat. § 429.061, subd. 1.
9. **Final assessment rolls.** If the board approves the assessment after the hearing, it must direct the town clerk to certify the final assessment roll to the County Auditor. If the adopted assessment differs from the proposed assessment, the clerk must provide mailed notice to property owners affected by the change. Minn. Stat. § 429.061, subd. 2.

10. **Certification of assessments.** The clerk may certify the assessments to the county auditor either once or on an annual basis. Minn. Stat. § 429.061, subd. 4.

Refer to **Document Number F4000** for additional information on special assessments.

D. Subordinate Service District

In 1989, the Legislature created Minn. Stat. Chap. 365A granting towns the authority to establish subordinate service districts. A subordinate service district is a defined area within a town receiving one or more town services, or enhanced services, provided specifically for that area and financed from revenues from the area. Minn. Stat. § 365A.02. While districts can be created for any service the town is authorized to provide, some common uses are road improvement projects, clustered septic systems, and dust control.

At least 50% of the property owners within the proposed district must sign the petition requesting the creation of a district. Upon receipt of a sufficient petition, the board must give notice and hold a hearing within 30 days. The board must decide whether to approve or disapprove the request within 30 days after the public hearing. Minn. Stat. § 364A.04.

If the district is created, it can be the subject of a reverse referendum. If 25% of the property owners in the district petition for a referendum, a special election must be held. If a majority of those voting on the question favor creation of the district, the district shall begin upon certification of the vote by the town clerk. Minn. Stat. § 365A.06.

Not only is the subordinate service district authority procedurally less complicated than the special assessment procedure, the options for financing the districts are more flexible.

The board may impose a property tax, a service fee, or both to finance the service. Minn. Stat.

§ 365A. 08. Subordinate service districts can be used to pay for on-going costs and does not require the charges to match the benefit. This procedure also does not contain the strict benefit calculation disclosure and limitations found in the special assessment procedure. This makes using a subordinate service district for town projects even more desirable.

Once created, subordinate service districts can be discontinued. At least 75 percent of the owners in the district can petition to request the removal of the district. The board must give notice, hold a hearing, and decide whether to

discontinue the district. No election is held. Minn. Stat. § 365A. 095, subd. 1.

If a town subordinate service district is discontinued and revenues remain after all outstanding obligations have been paid, the town board may vote to refund any surplus tax revenue or service charge. The refund must be distributed equally to the owners of any property within the discontinued district during the most recent tax year for which the tax or service fee was imposed. Any surplus not refunded under this section must be transferred to the town's general fund. Minn. Stat. § 365A.095., subd 2.

§ 8.4. Automatic Electronic Fund Transfers

With the advent of electronic banking, can the township enroll in an automatic electronic fund transfer (EFT)?

The short answer: No, townships should not enroll in automatic EFT that renews a contract because there is no statute authorizing automatic recurring payments.

Minn. Stat. 471.38, subd. 1, says if a claim against a town can be itemized, then the board “shall not audit or allow the claim” until the claimant provides a written, itemized, and signed claim. The statute prohibits the claim from being considered or paid, until the claim is received in the way described by the statute. The process provides the safeguard to taxpayers that all claims are reviewed by the board before payment is authorized. Allowing a payment to be automatic and recurring would reverse the presumption described by the statute because automatic EFT authorizes the payment before the claim is authorized by the Board. This undermines the protection of public funds.

Other statutes allow townships to pay bills electronically or by wire fund transfer (Minn. Stat. § 471.381) and to pay by credit card (Minn. Stat. § 471.382), but neither statute authorizes an auto-

matic payment or otherwise change the process required by Minn. Stat. § 471.38.

The Minnesota State Auditor stated in a position paper that there is no clear statutory authorization for debit card transactions. The position paper describes the problems with debit card transactions as: (1) immediate removal of public funds from a bank account; and (2) circumvention of the statutory safeguards provided by the claim statutes. http://www.osa.state.mn.us/other/Statements/creditcardusepolicies_0703_statement.pdf

An electronic fund transfer appears like a debit card transaction since it immediately removes funds upon the scheduled transaction date, and lacks any procedural safeguard before the money is debited. Since the EFT transactions have the same procedural shortcomings, it seems likely that automatic recurring payment would be viewed in the same way.

That is not to say all automatic EFT's may be disallowed, as MAT has previously taken the position that automatic recurring payments for utilities may be allowed when the amount of the recurring payment is set; meaning the amount is guaranteed to be the same every month. That is usually for the length of a specific contract period; i.e., for one year.

