



To: Mayor and Council Members
From: Darin Nelson, Finance Director
Cc: Bill Reynolds, City Administrator
Date: September 4, 2018
Re: Preliminary Levy Workshop

Background

Each year the city must prepare a budget and property tax levy for the following year. Staff has been analyzing revenues, expenditure information and initiatives to prepare a preliminary budget and levy for your consideration.

For the past two years, staff proposed budgets with minimal or no impact to residents. This year has an even more significant effect for taxpayers. Due to new growth and a decrease in the 2019 levy, most residents will see a city tax decrease. Absent any change in value, homeowners can expect a tax decrease of about \$62 or about 7.2 percent.

Even factoring in an increase in value, 7,147 residential properties will receive a tax cut. The average market value of homes in Shakopee increased by 5.3 percent from \$242,100 to \$255,00 for 2019. The estimated annual city tax impact for homes that increased in value from 0 to 5 percent will be a tax decrease of about \$39 or about 4.5 percent. The proposed budget also decreases our current tax rate, lowering it from 37.971 percent to an estimated 35.231 percent.

Last year's budget focused on right-sizing our organization in several key areas to fit our growing city of more than 41,000. The 2018 budget was also the last year of a three-year transformative budget process that set the foundation to achieve the council's ultimate goals of low taxes, financial stability and a stable tax rate. The 2019 budget is a direct reflection of those prior years' efforts. Future budgets will continue to build upon this foundation and keep these goals in play for the foreseeable future absent a major recessionary period.

The 2019 budget also continues focusing on fiscal transparency, long-term financial stability and ensuring our budget accurately reflects how we spend tax dollars.

The last few years have been more than just a time of change in our budget process. During the first two years of this budgetary transformation, we addressed multiple challenges that in and of themselves could be considered noteworthy. This included successfully inculcating the Community Center debt bond payment, establishment of a franchise fee, realignment of our liability insurance premiums and separation of our insurance from SPUC, creation of a fund to pave the way for future self-insurance and adjustment of internal service fund rent shortfalls.

Through all this change and challenge we still had our bond rating upgraded – a remarkable achievement as well. The city is currently rated Aa1 by Moody's Investors, which is one step below the top bond rating of AAA and ranks the city in the top 7 percent of cities nationwide. Staff is diligently working on setting the stage to achieve that AAA bond rating and place itself in

the top 3 percent of the cities nationwide. In effect, the city is in outstanding financial shape and will continue to be so due to both staff efforts and our steady growth.

Development is expected to continue at a rapid pace through the next several years due in part to a renegotiated annexation agreement with Jackson Township. Redevelopment in the downtown district and Canterbury area is expected to spur additional economic opportunities within the city. These developments help account for new growth in the city's tax base that helps reduce the tax burden of current residents and businesses.

Prudent planning and a strong economy have afforded the city the ability to reduce its property tax levy for 2019. The city is experiencing budget pressures, most notably from increasing infrastructure construction and maintenance costs and from general personnel costs, neither of which are unique to Shakopee nor other local governments. Fortunately, these pressures are mitigated by our previous work to financially position our budgets and by right-sizing our operations.

Schedule for budget and property tax levy development

Date	Who	What
July 17, 2018	Council/Staff	Review Preliminary Capital Improvement Plan (CIP)
September 4, 2018	Council/Staff	Review Maximum Levy, review initiatives and requests
September 18, 2018	Council	Adopt proposed maximum tax levy for City and EDA. Adopt final 2019-2023 CIP
September 30, 2018	Staff	Certify maximum tax levy to the County which will be used for proposed property tax notices
November	County	Proposed tax notices sent to owners
November	Council/Staff	Work session to review budget document
December 4, 2018	Council	Hold public meeting to discuss levy and budget. Review and approve utility rates for 2018.
December 18, 2018	Council	Adopt final tax levy and budget
December 28, 2018	Staff	Certify final tax levy and budget to County and State

Budget Impact Issues

Wages and benefits

All three union contracts went into effect on Jan. 1, 2017, and include 3 percent cost of living adjustments for 2017, 2018 and 2019, respectively. Non-union wage increases typically mirror

the union increases. The 2019 budget is calculated with a 3-percent-across-the-board wage increase, which is approximately \$411,000.

After experiencing a 19-percent increase in health insurance last year, the city is anticipating health insurance rates to remain virtually flat for next year. The city also set aside funds at the end of the 2017 fiscal year to aid in transitioning toward self-insurance funding for health insurance. City staff is still considering all health insurance options and will be bringing more information forward once a plan has been formulated. The preliminary budget includes a 1-percent increase, or about \$14,000, dedicated toward health insurance. For comparison purposes, the 2018 budget included an additional \$240,000 to account for the large cost increase last year.

The 2018 Legislature passed an amendment to the State of Minnesota Police and Fire pension plan to help ensure the fund's long-term sustainability. Part of this legislation includes mandatory employee and employer contribution increases. The 2019 budget impact amounts to about \$41,000.

Additional 2019 personnel changes include the elimination of election judge salaries due to no election taking place in 2019, and the full-year funding for two new police officers that are budgeted to begin on October 1, 2018. These changes amount to a reduction of \$43,000 and an addition of \$132,000, respectively.

No other benefit changes are anticipated or legislated for the upcoming year.

After essentially right-sizing the organization last year to meet the growing needs of our city, there remains a need to add one additional public works maintenance operator in the streets division to maintain current service levels. The city last added to its public works operational staff in 2014, with the addition of a maintenance operator in both streets/utilities and parks. Public works streets/utilities maintenance operators split their time between streets, sanitary sewer and storm drainage. Due to this allocation of time, the General Fund impact of adding an additional maintenance operator in the streets division is \$38,225.

Internal Charges

During this summer's CIP workshop, staffed noted the need to increase the rents on equipment with life expectancies of 10 years or more. Department rent charges have been historically based on the original purchase price of the asset amortized over the life of the asset. The problem we are running into is that the replacement cost of equipment 10 to 20 years after the original purchase is exponentially higher, which will ultimately cause a shortfall in the Equipment Replacement Fund. This is most evident with our latest fire engine replacements. The original fire engines were purchased for \$340,000 each in 1998. The replacement cost of those two engines is now more than \$600,000 each.

Staff is recommending equipment with life expectancies of 10 years or more be charged a rent rate equal to the estimated future replacement cost. This change will ensure the long-term sustainability of the Equipment Replacement Fund. Staff is also recommending we step into full funding of this change over the next four years. Twenty-five percent of this change equates to \$73,900 in additional equipment rent for 2019.

Other Services & Charges

There are no additional new funds required for other expenditures outside of personnel and rent charges. There are specific line items that require additional funds such as building credit card fees and the west end AUAR study, but these increases are offset by reductions from other areas.

Revenues

Typically, governmental revenues such as grants, charges for service, and fees and permits are constant with little fluctuation from one year to the next. Obviously, the economy is typically the biggest factor in revenue fluctuations. The city's building permits have been strong over the past couple years with the influx of commercial development. Those strong permits are expected to continue with the recent housing developments taking shape.

It is fiscally responsible to budget conservatively for building permit revenue. However, we do not want to be ultra-conservative on our forecasts since that can lead to unnecessary tax collections. That being said, we have been steadily increasing our building permits budget to more closely match the increasing actual permits for the last couple years. For 2019, we are increasing the building permit revenue budget by \$295,000 or approximately 25 percent. The 2019 building permit budget is \$1.3 million, which is about \$340,000 below the three-year average. However, we are not expecting to have as many large commercial/industrial building permits issued as available land is becoming scarce.

The community center and ice arena revenues for 2019 are expected to increase by about 4.5 percent from \$2.1 million to \$2.2 million. These additional revenues aid in offsetting operational costs.

Economic Development Authority

Part of the budget discussions last year involved the implementation of a dedicated EDA levy which is separate from the city's general levy. EDA's have the statutory authority to levy a small percentage (up to 0.01813%) of the city's estimated market value, which for 2019 would be a maximum of approximately \$834,400. The EDA and City Council can set the levy at any amount up to this cap.

This move to increase transparency is a budget neutral change. Prior to 2018, annual transfers were made from the General Fund to the EDA to cover EDA operational costs, façade loan funds and other development related activities. This EDA levy eliminates this transfer from the General Fund, thus reducing the city's general levy.

The EDA levy is identified on property tax statements as a separate local tax outside of the city's general property tax. Staff is recommending an EDA levy of \$350,000 for 2019, which is the same levy amount as 2018. This levy has been calculated into our overall levy decrease.

Debt Service

Staff is anticipating that the city's total debt service payments to remain stable at approximately \$2.2 million annually. Staff will need the council to approve debt service reduction resolutions on Sept. 18 due to available fund balances in existing debt service funds. A breakdown and comparison of the individual debt levies can be viewed on the next page.

Levy Request & Impact

Staff is recommending a preliminary city levy of \$19,230,500, which is decrease of \$30,000 over last year, and a preliminary EDA levy of \$350,000, which is identical to last year. The preliminary levy is the maximum the city can levy; the final levy may be less than the preliminary levy but may not be more.

Since the levy is decreasing, homeowners will see a tax decrease if their property value increases up to 5.3 percent. The city experienced 6.80 percent growth in tax capacity for taxes payable 2019. This is on top of 8-percent growth from the previous two years. New construction accounts for about 16 percent or \$634,600 of additional tax capacity. In terms of levy dollars, the new construction tax capacity allows for the city to increase the levy by \$225,000 without having a tax impact on existing properties.

The breakdown and comparison of the proposed preliminary 2019 levy is as follows:

City of Shakopee Preliminary Levy Analysis September 4, 2018				
	2018 Final	2019 Preliminary	Increase/ (Decrease)	% Change
City Levy				
General Fund	\$ 16,694,500	\$ 16,677,400	\$ (17,100)	-0.10%
Abatements	182,400	169,500	(12,900)	-7.07%
Capital Improvement Levy	200,000	200,000	-	0.00%
Debt Service				
2008 A Improve	135,448	-	(135,448)	-100%
2010 A Improve	105,940	115,000	9,060	9%
2016 Abatement	1,942,260	2,068,600	126,340	7%
Total Debt Service	<u>2,183,648</u>	<u>2,183,600</u>	<u>(48)</u>	<u>0%</u>
Total City Levy	<u>\$ 19,260,548</u>	<u>\$ 19,230,500</u>	<u>\$ (30,048)</u>	<u>-0.16%</u>
Shakopee EDA Special Levy	<u>\$ 350,000</u>	<u>\$ 350,000</u>	<u>\$ -</u>	<u>0.00%</u>
Total City and EDA Levies	<u><u>\$ 19,610,548</u></u>	<u><u>\$ 19,580,500</u></u>	<u><u>\$ (30,048)</u></u>	<u><u>-0.15%</u></u>

Items to note with the 2019 preliminary levy include:

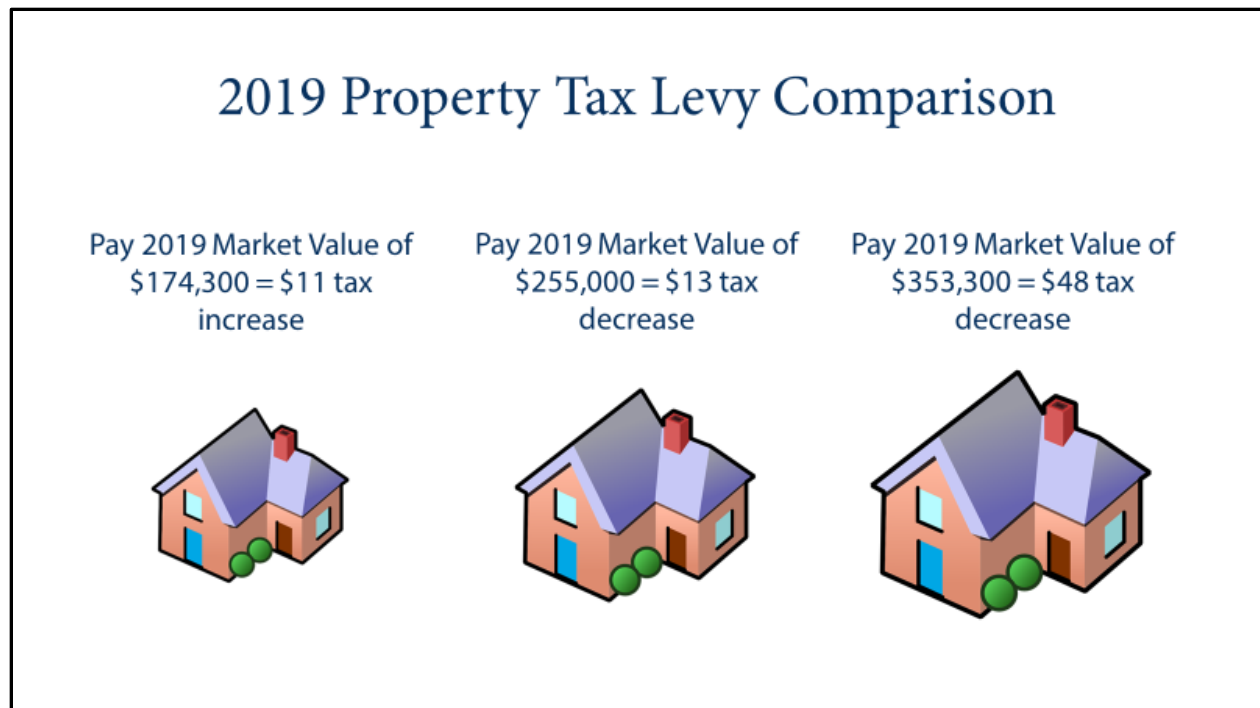
- Levy decrease of \$30,048.
- Flat preliminary levy for the Shakopee EDA.
- The 2008 A Improvement Bond will be paid off in February 2019. The levy savings from this bond levy are being redirected towards the 2016 Abatement Bonds. This redirection of levy was anticipated in the original 2016 Abatement Bond repayment schedule.

Scott County provides the staff with tax impact estimates for residential homestead properties. Residential property values increased on average 5.3 percent from Jan. 1, 2017, to Jan. 1, 2018, for taxes payable 2019. The average market value home in Shakopee increased from \$242,100 to \$255,000. Residential values are increasing for taxes payable 2018.

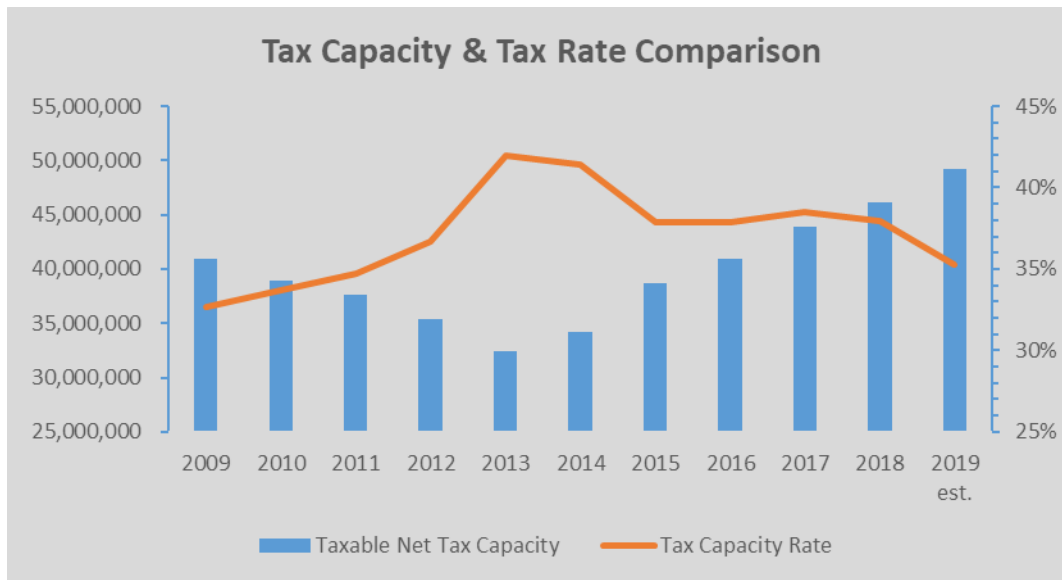
The chart below provides the average percentage change in value for residential properties from taxes payable 2018 to taxes payable 2019. These percentage changes are strictly the averages within each value range. Individual properties valuations will likely be more or less than the averages.

Payable 2018 Value	Properties in Category	Average of Net % Change for pay 2019
<\$100,000	147	4.1%
100000-149999	1,377	10.5%
150000-199999	3,428	8.0%
200000-249999	2,478	5.0%
250000-299999	1,597	3.9%
300000-399999	2,279	3.3%
400000-499999	582	2.4%
500000-699999	150	2.8%
700000-999999	7	10.7%
>\$999,999	2	8.3%
Grand Total	12,047	5.3%

The chart below provides a comparison of the proposed 2019 levy for three different valued homes including the average value home of \$255,000.



The proposed tax levy will drop the city's tax rate from 37.971 percent to 35.231 percent, a decrease of 2.74 percent. These tax rates include the proposed Shakopee EDA levy. Below is a chart comparing the city's tax capacity and rate over the past 11 years, including the 2019 preliminary levy.



Staff is still working on receiving preliminary levy estimates from our comparable cities. Staff will have this information available at the council meeting on Sept. 18.

Summary

Attached is a preliminary General Fund Summary Budget that includes all the items discussed above, including the small reduction in the city's preliminary tax levy. Again, the preliminary levy is the maximum levy that can be levied. The final levy can be reduced but cannot be increased. Between the preliminary levy and the final levy staff will be working on fine tuning the current unknowns.

2019 Annual Budget GENERAL FUND SUMMARY

	Actual 2016	Actual 2017	Original Budget 2018	Requested Budget 2019
REVENUES:				
TAXES	17,019,256.64	16,321,610.33	17,100,000.00	16,724,400.00
TAX INCREMENTS	2,946.93	4,633.26	0.00	3,000.00
SPECIAL ASSESSMENTS	15,817.76	3,874.61	7,000.00	7,300.00
LICENSES AND PERMITS	2,564,729.10	2,837,222.02	1,845,000.00	2,207,200.00
INTERGOVERNMENTAL	1,344,279.22	1,369,027.55	1,486,100.00	1,431,600.00
CHARGES FOR SERVICES	4,750,514.28	5,653,773.86	5,699,800.00	6,322,200.00
FINES AND FORFEITURES	11,213.08	2,718.80	1,500.00	1,000.00
MISCELLANEOUS	218,733.94	242,715.83	206,500.00	198,000.00
TOTAL REVENUES	25,927,490.95	26,435,576.26	26,345,900.00	26,894,700.00
EXPENDITURES:				
GENERAL GOVERNMENT	(3,965,116.02)	(4,387,638.96)	(4,922,900.00)	(4,722,800.00)
PUBLIC SAFETY	(10,585,899.22)	(11,004,434.14)	(11,972,200.00)	(12,523,800.00)
PUBLIC WORKS	(4,662,563.14)	(4,849,108.95)	(5,543,800.00)	(5,717,700.00)
RECREATION	(2,630,776.59)	(3,294,861.21)	(3,918,500.00)	(4,049,100.00)
UNALLOCATED	(34,835.56)	(27,619.38)	(216,300.00)	(131,300.00)
DEBT SERVICE	0.00	(16,605.00)	(22,200.00)	0.00
CAPITAL OUTLAY	(37,422.57)	(93,341.00)	0.00	0.00
TOTAL EXPENDITURES	(21,916,613.10)	(23,673,608.64)	(26,595,900.00)	(27,144,700.00)
OTHER FINANCING:				
TRANSFERS IN	250,000.00	250,000.00	250,000.00	250,000.00
PROCEEDS FROM SALE OF ASSETS	9,133.93	4,660.88	0.00	0.00
BOND PROCEEDS	0.00	79,100.00	0.00	0.00
TRANSFERS OUT	(3,348,754.50)	(1,800,000.00)	0.00	0.00
TOTAL OTHER FINANCING	(3,089,620.57)	(1,466,239.12)	250,000.00	250,000.00
NET	921,257.28	1,295,728.50	0.00	0.00