Shared Sacrifice for the Greater Good

Proposed 2018 Levy and General Fund Budget

City of Duluth
Emily Larson, Mayor

August 14, 2017
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2018 Preliminary Levy and General Fund Budget

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2018 City of Duluth Budget Presentation
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Councilors, thank you for your service.

Tonight I am pleased to present to you my proposed budget and property tax levy for 2018.

This is a nuts and bolts budget, focused on addressing infrastructure in 3 ways:

- Increased funding for physical infrastructure of streets
- Investment in cost-efficient energy infrastructure of renewable energy
- Identifying and tackling ongoing structural budget deficit issues

I think you’ll find this budget reflects a variety of important priorities, the most important being that of streets. It also reflects choices and priorities along with the difficult decisions that come with choosing among them.

But before I do that, I’d like to share how the presentation of this budget is very different than what has been done in the past.

First off, we are presenting the budget to you, and the community, early. Very early. I will be proposing our tax levy for 2018 a full 6 weeks before you are required to set it. That is intentional on my part – this budget has some highlights we can celebrate, but it also has some realities that are important for you to have time enough to fully digest. As you know, I propose a levy, but you as a Council have the ultimate authority to set it.

Second, as a team we started early, and began our budget conversation back in April. Over the course of the past 18 months our team of administration and Directors have worked hard to build a collaborative working environment. We have set aside time for Director Tours - taking a few hours, a couple of times per year, to get into the community and literally look at and experience projects that have multi-department impact. Doing this has helped us all understand how our work is connected, and our decisions impact one another. The same spirit of understanding and commitment is true for our budget conversations.

Lastly, this is, in part, a budget of sacrifice, and unity. Because of increased health care and labor costs, revenue streams that don’t keep up with inflation and a commitment to add to our streets budget, I gave our Director’s clear and difficult direction: identify efficiencies, realignments and budget reductions. In response, this team of Directors have been honest, candid and committed to our common good. I am incredibly proud and grateful to work with them.

For all of these reasons, I have taken a different approach to presenting this budget, which I am calling “Shared Sacrifice for the Common Good.”
This budget adds $1 million to our streets funding, currently at $2.8 million, bringing our total proposed spending for streets to $3.8 million for 2018. As I know you’ve heard over the past week, I have designated a streets plan and asked the public, and you, to consider a referendum for a one-half percent (0.5%) sales tax dedicated exclusively to streets and sidewalks. While tonight my focus is on our budget and not the referendum, the two are inextricably linked. Because I could not, in good conscience, ask our public to support a new sales tax without demonstrating the internal discipline required to prioritize it ourselves.

I am also proposing a $895,000 withdrawal from our General Fund Reserves to invest as a commercial tenant in the Community Solar Garden of MN Power. We are in the process of finalizing terms allowing the City of Duluth to enter into an agreement by which we are estimated to save a conservative $2 million dollars for the City over the course of the 25-year agreement. Because we pay for our energy costs through the General Fund, this upfront investment would have real impact, realizing savings to the General Fund of $70,000 annually.

Using our reserves makes sense in this case – it’s a one-time investment that yields significant ongoing savings. Our reserves, once a negative $1.7 million in 2007, are now sitting at a healthy $13 million. Just another indicator of our internal financial discipline. As you likely know, having a two-month reserve makes a big difference in our ability to leverage bonds and other investments because it makes us a smart financial risk for lenders. Because I have proposed using reserves, making this investment in the Solar Garden does not come at the expense of City services or to our General Fund.

But investing in streets does. Let me explain.

We began this budget cycle with a $3.2 million deficit. As a status quo starting point. Our deficit starting point is due in large part to increasing health care costs and wage growth, which greatly outpace our stagnant revenues. Our single largest source of revenue, Local Government Aid, does not increase at the rate of expenditures they pay for.

Herein lies the last nuts and bolts element of this budget: identifying and tackling our ongoing structural budget deficit. Simply put, to keep steady as an organization we need to find ways to cut spending each year. Because of my commitment to increase streets funding using these same stretched and stressed General Fund revenues, as a team we needed to address both the $3.2 million deficit AND the $1 million I required for streets.

We did it. But getting here was not easy, and I do believe we will see impact on our services. This budget presents a good example of our current struggle to balance the needs of operating a complicated and critical set of basic public functions with the realities of what we have to pay for them.
Each Director participated in this shared sacrifice. Including, for the first time, our public safety divisions who, upon my request, cut a combined total of $700,000+ from their budgets.

Ironically, as we walk through the budget together it’s hard to see how these savings actually translate. That’s because the health care costs and wage growth have worked their way into the final numbers and absorbed every penny available.

All told, I am proposing a budget where we cut $2.1 million of expenses, while investing in long term renewable energy, adding in $1 million for streets and taking into account the advantage of $1.1 million in anticipated new growth of tax capacity. This growth is critical – the tax impact of an 8.45% levy increase is mitigated by new growth in tax capacity and results in a 4% tax rate increase. Modest and mindful, a 2018 property tax increase of $21 for a $160,000 home – the average valuation within the City of Duluth.

So while I am proud of this budget, it represents difficult choices. Due to previous years’ worth of accumulated cuts and other reductions in growth, we are no longer able to find ways to do more with less. I believe this budget starts us on a course of doing less with less.

The referendum for dedicated sales tax revenue for streets is an opportunity for Duluth to halt this direction in future years. Should the public, or the legislature, choose to not grant us permission to enact this one-half percent (0.5%), I will continue to place priority on our streets.

I recognize the determinations you need to make about the levy and the referendum are separate in nature. But I also hope that you can see how one informs the other.

My thanks to you and your families for your service and leadership. It is an honor to serve as Mayor of our community, to work with all of you and to have the dedication and support of an amazing City of Duluth team.

~ Emily
The City’s total budget exceeds $250 million and encompasses a variety of funds that account for city services. The General Fund is an important part of that budget, and the one which is directly impacted by property tax, but does not represent all the services and work that is done.
This graph shows the major categories of revenues expressed as a percent of total General Fund revenues estimated for budget fiscal year 2018. The City's policy of maintaining a diverse revenue base is reflected in the categories of revenues listed above, with almost 200 separate budgeted sources of revenue. Although the City does have a wide variety of revenues, the reader will note the City's relative dependence on Local Government Aid, which constitutes 35% of all General Fund revenues and does not adjust for inflation. For this reason, we closely monitor Local Government Aid every session at the State Legislature.
This graph shows the General Fund departmental budgets as a percent of the total General Fund expenditures for budget fiscal year 2018. The largest category of expense is public safety with the Police and Fire departments comprising 46% of the total; followed by the Public Administration department which includes Human Resources, Information Technology, City Clerk, Park Maintenance, Library, and Facilities at 20%. The General Fund portion of the Public Works department comprises 11% of the total. Retiree health care comprises 9% of the total. The remaining five departments totaled together are 14%, with no department exceeding 4%.
City of Duluth Minnesota - 2018 Budget

2018 Proposed General Fund Revenues by Source

General Fund revenues are comprised of three revenue sources that provide in excess of 70% of the resources needed for operations. Of these three revenues, only property tax is under the direct control of the City. Growth in Local Government Aid does not keep pace with the rate of inflation. Sales and use tax has been fairly consistent in recent years, but is an industry that is impacted by e-commerce. These factors can put additional pressure on the property tax portion of revenue.

Property tax makes up 19% of our 2018 budget but is the only variable we can adjust – and we can only adjust it upon itself. Meaning that when we raise the property tax levy 1% we do so only on that 19% of the budget, not the entire budget. For that reason, raising property taxes yields far less than what people expect – roughly $250,000, give or take.
We are in a service industry and our primary “cost” are the hard working people who provide these important services. Because of collective bargaining agreements and contract negotiations, wages are known, agreed upon and predictable. Health insurance is the single most volatile factor that we cannot predict, and it has real impact; annual health care cost increases have averaged eight percent since 2012. For 2018, premium rates are expected to increase ten percent.

Since 2010, salary wage increases have averaged less than two percent and FTE counts have remained flat. We are mindful of spending in this area and so are our employees. If we had the ability to better isolate or contain health care costs, this would be of huge benefit to the City and our taxpayers.
Revenue sources are forecast to remain flat and expenses are expected to increase due to health care cost increases, wage growth and inflation. Left unchecked, significant deficits are expected for 2018 and beyond that would result in significant tax increases.

This is the core structural budget deficit we are working to address.
These graphs compare our most volatile cost driver (health care) with our largest revenue source (Local Government Aid, LGA) and is another example of a structural budget issue. While health care consumes a larger majority of the budget each year, LGA does not grow with inflation to help absorb these costs. This places additional pressure on other budget areas.

Local government aid (LGA) is the largest funding source for general fund operations and accounts for 35% of total general fund revenues. Since 2009, LGA has not kept pace with the rate of inflation. If LGA had kept pace with the rate of inflation, our aid would be in excess of $34 million for 2018 as compared to the certified aid amount of $29.66 million. Structural budget issue: solved.
Multiple strategies to achieve greater good & a balanced budget:

In the following pages, we demonstrate our shared focus for 2018: decreasing our spending, investing in energy and increasing our investment in streets. This has been accomplished by a model of shared sacrifice across all divisions of the organization. We have managed to balance the internal structural budget issue for 2018 with sustainable spending cuts – meaning these savings will carry over into future years and are not simply short-term or one-time pay-offs. A chart follows these pages with a summary of budget cuts per department.

We have chosen to fund a one-time $895,000 investment in Minnesota Power’s Community Solar Project to achieve both energy and financial savings, and will use our General Fund Reserves as the source of payment. We anticipate this one-time investment to yield a General Fund savings of $2 million over the course of the 25-year agreement. In 2008, the reserves had a negative balance – it currently stands at more than $13 million. For this reason, it is a good source for this one-time investment, taking future pressure off the General Fund and providing a General Fund savings of $70,000 per year. Two charts follow these pages: one with a visual of our anticipated financial savings, and another charting the General Fund Reserve growth since 2009.

Finally, we have made good on our commitment to streets, increasing our investment in this area to a (still deficient) $3.8 million dollars for 2018. To be clear, not all of this goes to fund streets. Until 2023 we will be paying down old bond debt for street work done years ago, meaning that the dollars we use today in this area are not covering the needs of today. They are not covering even the need of yesterday, since we are well behind in our funding of infrastructure. That said, we have made sacrifices in other parts of the organization this year to increase funding for streets and are doing the best with what we’ve got. A chart follows these pages which outlines the inconsistency of streets spending in recent years.

We have achieved all of this through months of meetings as an administrative team. Additionally, because of our overall economic growth, we have the benefit of property tax value growth this year. In the end, this proposed balanced budget accomplishes a substantial amount with the modest proposed city levy tax impact of 4%. The homeowner of the average valuation home of $160,000 will pay a total of $21 more in property taxes to the City of Duluth in 2018 than they did in 2017.

The City of Duluth is 24% of the total property tax for residents – the remainder go to the School District (27%), voter-approved Parks Fund (3%), St. Louis County (42%) and other (4%). There is a pie chart later on in this budget that provides a visual for readers.

In the appendix of this Budget Book is information about the streets plan and referendum we anticipate being placed before voters in November. While the referendum is a separate set of actions than the 2018 budget, the two are inextricably linked, since funding of one hinges on the availability of funds in the other. Also in the appendix is a Question & Answer section that relates to both the budget and the referendum.
## City of Duluth Minnesota - 2018 Budget

<table>
<thead>
<tr>
<th></th>
<th>2016 Approved Budget</th>
<th>2017 Approved Budget</th>
<th>2018 Proposed Budget</th>
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<td>9.44</td>
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<td>Transfers and Other Functions</td>
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<td>10.10</td>
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<td>83.98</td>
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<td>Fund Balance Reserves - Community Solar Program</td>
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<td><strong>Total Budget</strong></td>
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<td>82.58</td>
<td>84.88</td>
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### City of Duluth Minnesota - 2018 Budget

#### Breakdown of Average Homestead Property Tax Bill by Taxing Entity

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<tr>
<th>Taxing Entity</th>
<th>2018 Proposed</th>
<th>Change in Levy</th>
<th>% Change in Total City Levy</th>
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<tbody>
<tr>
<td>Parks</td>
<td>3%</td>
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<tr>
<td>School</td>
<td>27%</td>
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<tr>
<td>County</td>
<td>42%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>County</td>
<td>42%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Other</td>
<td>4%</td>
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#### 2018 Proposed Property Tax Levy

<table>
<thead>
<tr>
<th>Levy Description</th>
<th>2017 Approved</th>
<th>2018 Proposed</th>
<th>Change in Levy</th>
<th>% Change in Total City Levy</th>
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<tr>
<td>General Operations Levy</td>
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<td>General Operations</td>
<td>$14,628,200</td>
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<td>Provision for Tax Delinquency</td>
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<td>Total General Operations Levy</td>
<td>$14,778,200</td>
<td>$15,928,600</td>
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<td>4.52%</td>
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<td>Capital Projects Levy</td>
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<td>Debt Service</td>
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<td>Total Capital Projects Levy</td>
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<td>Street Light Levy</td>
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<tr>
<td>Street Maintenance Utility Levy</td>
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<tr>
<td>Street Maintenance Utility Levy 2018</td>
<td>$2,800,000</td>
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<td>Total Street Maintenance Utility Levy</td>
<td>$2,800,000</td>
<td>$3,800,000</td>
<td>$1,000,000</td>
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<td>Total City Property Tax Levy</td>
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<td>$27,598,792</td>
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<td>Property Tax Value Growth</td>
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<td>Proposed City Levy Tax Impact</td>
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#### Proposed 2018 City Tax Levy - Estimated Annual Tax Impact to Property Owners

<table>
<thead>
<tr>
<th>Property Value Range</th>
<th>Annual Tax Impact</th>
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<tr>
<td>$100,000 Residential</td>
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<tr>
<td>$160,000 Residential</td>
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<td>$225,000 Residential</td>
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<td>$500,000 Commercial</td>
<td>$139</td>
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<td>$750,000 Commercial</td>
<td>$214</td>
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Shared Sacrifice:
reductions across the organization

<table>
<thead>
<tr>
<th>Department</th>
<th>Proposed Reduction</th>
<th>Reduction as % of Dept Budget</th>
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<tbody>
<tr>
<td>Legislative &amp; Executive</td>
<td>$ (286,400)</td>
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<tr>
<td>Public Administration</td>
<td>$ (561,200)</td>
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<td>Finance</td>
<td>$ (125,000)</td>
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<td>Planning &amp; Construction Services</td>
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<td>Business &amp; Community Development</td>
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<td>Fire</td>
<td>$ (386,800)</td>
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<td>Police</td>
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<td><strong>Total Reductions:</strong></td>
<td>$ (2,100,000)</td>
<td>2.54%</td>
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Each department and Director committed to being a partner in decreasing expenses. Together, we make a whole, and the sacrifices were shared. The first column is the dollar amount of the decrease to each department; the second is the percentage of the decrease to their total department budget. Budget savings will be realized through a combination of retirements, attritions, position elimination and organizational realignments.
General Fund Reserves are, literally, the reserves of the city and exist to mitigate future risks including unplanned reductions in aids and unforeseen events. Credit rating authorities carefully monitor fund balance in evaluating a government’s creditworthiness. Since, 2008 fund balance has increased from a $1 million deficit to in excess of $13 million today. Fund balance reserves exceed the City’s fiscal policy of maintaining an optimum level equal to ten percent of General Fund expenditures. This makes this a good source for one-time investment of energy financial savings into Minnesota Power’s Community Solar Garden. The chart above illustrates the growth of the General Fund Reserves while the chart below outlines the financial savings of this one-time investment over the course of the 25-year agreement.

Community Solar Garden: 630,000 kWh
one-time investment saves $2 million over 25 years
In the past ten years we have employed four different methods of paying for our streets. Always doing the best we can, it’s time for us to do more and to identify a solution by which we can fully address the problem of aging infrastructure. This is, by far, the number one priority we hear from the community. This year we have chosen to prioritize spending in this area by cutting in others and by raising the levy. For future long term reliability, we are proposing the referendum for a dedicated sales tax for streets. Further information can be found in the appendix on this option being placed before voters in November.
Budget Review Process

MAYOR’S BUDGET PRESENTATION TO COUNCIL

Aug. 14  2018 Proposed General Fund budget and tax levy presentation to Council
Sept. 25  Council sets preliminary budget and maximum property tax levy

COUNCIL BUDGET REVIEW

Sept-Nov  Schedule set by Council Finance Chair
Oct-Nov  Capital Improvement presentation to City Council

PROPOSED TRUTH IN TAXATION MEETINGS

Dec. 4  Truth in Taxation hearing
Dec. 11  Council approves final budget and levy
APPENDIX
RESOLUTION APPROVING A HALF PERCENT SALES AND USE TAX DEDICATED TO FUND A STREET IMPROVEMENT PROGRAM AND CALLING FOR A REFERENDUM REQUESTING AUTHORIZATION FOR SUCH TAX.

CITY PROPOSAL:
RESOLVED, that the city council of the city of Duluth hereby makes the following findings:

(a) The city’s transportation infrastructure is vital to the current and future economic vitality of the city as well as critical to health, welfare and wellbeing of all of its citizens, its neighbors and its visitors; and

(b) Duluth is home to 86,293 residents and serves as a critical regional center with more than 35,000 daily work commuters and 6.7 million annual tourists; and

(c) The need for maintenance, improvement and replacement of the city’s road infrastructure results from its use by not only property owners within the city but also from its use by persons and entities from outside the taxing jurisdiction of the city; and

(d) There are approximately 450 miles of city-owned roadways and more than 400 miles of city sidewalks in the city of Duluth requiring maintenance, improvement, and replacement but current funding through property taxes allows us to fund only a few miles per year; and

(e) The city public works and utilities department has developed a long-term program for a capital improvement project implementing said program, which program, entitled “Duluth Street Improvement Program 2017”, is attached hereto as Exhibit A (the “Street Improvement Program”), and determined the minimum revenues necessary to address the city’s most pressing transportation needs over the next 25 years under the Program; and

(f) The city acting through its mayor designated the Street Improvement Program on August 8, 2017, as required by Minnesota Statutes Section 297A.99, Subd. 3(b); and

(g) Because the need to implement and therefore to fund the Street Improvement Program results from use by persons and entities from without as well as within the city, the most fair, reasonable and equitable source of the necessary funding is an increase in the city’s general sales and use tax; and

(h) To fund the city’s most pressing needs under the Program, the administration and council support a 0.5% increase in the city’s general sales and use tax for a term of 25 years from the date of first collection thereof, which will be dedicated in its entirety to help pay for a portion of the cost of the necessary maintenance, improvement and replacement of the city’s transportation infrastructure; and

(i) Pursuant to Minnesota Statutes Section 297A.99, in order to enact such a tax, the authorization of the state legislature is required and before requesting such authorization, the conditions of that statute must be complied with including the approval of the imposition thereof by the voters of the city at a general election.

FURTHER RESOLVED, that pursuant to the requirements of Minnesota Statutes Section 297A.99 Subd. 2, the city council of the city of Duluth hereby confirms the August 8, 2017, designation of the Street Improvement Program and approves of the imposition of a 0.5% increase in the city’s general sales and use tax as herein described for a term of up to 25 years from the date of first collection thereof to fund the implementation of the Street Improvement Program.

FURTHER RESOLVED, that the city council hereby calls for a referendum at a general municipal election to be held on November 7, 2017, for the purpose of submitting to the electors of the city a resolution requesting that the legislature authorize the imposition of a 0.5% increase
in the city’s general sales and use tax to be used exclusively to fund the implementation of the Street Improvement Program and the clerk is authorized and directed to prepare and mail or publish any and all notices of such referendum question as are required by law.

FURTHER RESOLVED, that the question presented to the electors on the ballot of the said general election shall read as follows:

“Should the city of Duluth request the Minnesota State legislature to authorize the city to enact a 0.5% general sales and use tax on sales and use of goods and services as currently applied within the city for a term of up to 25 years from the date of first collection thereof dedicated to funding implementation of the city’s designated Street Improvement Program?

A “yes” vote means you favor the city of Duluth requesting authority to enact a 0.5% sales and use tax dedicated to fund the Street Improvement Program.

A “no” vote means you do not favor the city of Duluth requesting the authority to enact a 0.5% sales and use tax dedicated to funding the Street Improvement Program.

..Statement of Purpose
STATEMENT OF PURPOSE: This resolution indicates the council’s approval of the increase of the city’s general sales and use tax by an additional 0.5% for a term of up to 25 years and submits to referendum a resolution asking the legislature to authorize the city to enact such a tax for the purpose of funding street improvement projects as set forth in the designated Street Improvement Program. If the legislature agrees, it will pass legislation authorizing the tax and that will go to the city council for approval. Upon approval, the city council will be empowered to enact the new tax by ordinance. Once enacted, the dedicated sales and use tax would be added to the existing $2.8 Million annual dedicated Streets Fund.
Frequently Asked Questions
about the ½% Dedicated Sales Tax Proposal
AND our 2018 General Fund Budget Proposal
August 2017

How will this ½% sales tax be used?

It will be dedicated entirely to streets and sidewalks, with the vast majority of that being streets. We expect it to generate about $7 million annually. We would add our current streets dedication of $2.8 million, bringing the total to an expected $10 million. All told, we have over 450 miles of roads and more than 400 miles of sidewalks. We can certainly put these funds to good use.

How can I be sure this money will be used as it’s intended?

The language in the question that will be on the ballot in November states that the funds will be “dedicated to funding implementation of the Streets Improvement Plan.” This means that the ½% sales tax money would be legally required to fund only items within the Streets Improvement Plan. That plan is listed on our website and includes roads, sidewalks, bridges, and where necessary, curb and gutter improvements. This would require legislative approval – we would be absolutely locked into usage based on that process, too. Put simply, this money would not be allowed to be used on things such as mountain bike trails, parks, or anything else other than the Streets Improvement Plan. There are a lot of legal checks and balances to make sure that doesn’t happen.

Why is it proposed to only be for 25 years? Won’t there still be a need to fix streets then?

Because funding mechanisms can and do change. The City has had 4 different methods for paying for streets in the past 10 years alone – some based on opportunity, others from necessity. All the more reason to rely on a dedicated source to reliably meet our needs. Also, this is an innovative ask from the legislature and we wanted to be mindful of the many other considerations they need to balance when working with cities. While we are not requesting money from them, they do need to grant us approval.

Has this been done before?

Yes. The legislature has approved dedicated Sales Tax opportunities for many counties and an increasing number of cities. Hermantown and Proctor recently were approved for 1% sales tax, for instance. St. Louis County has activated their transportation Sales tax to meet broad County needs and has invested
$15 million in the past three years on County roads within the City of Duluth. That’s three times more than what we ourselves have been able to accomplish with existing funding.

**Will this money be used to build bike trails?**

No. It will not be used for any trails. It is only going to be used for streets and sidewalks.

**If voters support this referendum, does it automatically go into effect?**

No. If it passes in November of this year, we need to work with the legislature next session to get approval. There are no guarantees, but there would certainly be no ability to even make the ask if we did not have broad community support.

**What happens if we don’t get it?**

If the community says no, or the legislature says no, it’s likely we will have both cuts in services and higher property taxes starting next year. We will make streets a continued priority, and it will mean that other priorities will need to change.

**What impact will this increased sales tax have on businesses?**

Duluth currently collects a 1% undesignated sales tax that helps pay for public safety and other core service – this was established 49 years ago. This would be in addition, but is different because it would be dedicated and has a sunset. While sales taxes absolutely add up, so does the disrepair of our streets. We believe the investment is well worth the additional cost.

**Don’t my taxes already pay for this?**

Yes, they do. Your taxes provide $2.8 million for streets. If solely placed upon residents of Duluth, generating the kind of revenue we anticipate through a dedicated sales tax would increase the property tax burden for residents between 35-40%, for a built infrastructure intended to serve an additional 35,000 daily commuters and 6.7 million annual tourists. Our City budget is 83% people: salaries, benefits and health care. We manage each of these elements as closely as we can. As Mayor I have demonstrated a commitment to increase street investments twice in my first two years of office: the one-time $800,000 infusion from our general fund surplus and the proposed budget being issued on August 14 which allocates additional resources.
If we can’t pay for our roads, why are we spending money building trails?

Because they are paid for from different sources of revenue. Money for trails and parks come from the Parks Fund – a fund that legally has to be spent on things such as trails and parks, Legacy Funds, grants from outside sources, St. Louis River Corridor investments or donations. These dollars cannot be used for streets. It is frustrating for residents to see shiny new wonderful trails and deteriorating potholed streets. People don’t necessarily care how funds can’t be used, they just want to know why streets aren’t getting done. I get it, and that’s why we are doing this. Trails and parks generate specific and dedicated revenue sources to cover their costs. That’s a good thing. Now we need to do the same for streets.

Sometimes a road is torn up one year for water main fixes and then another year for street fixes. It’s frustrating.

You’re right. Currently, when a water line needs a repair, we don’t have any ability to seize that opportunity to also address the street. Because there is no money available. Our current system is completely reactionary and does not allow us to be efficient. It’s one of the reasons we want to address long term streets funding. If we can secure the sales tax, we will be able to plan a streets system that aligns with utilities. Imagine that!

What is my Return on Investment for this ½% sales tax?

The League of Minnesota Cities found that every $1 spent on street maintenance saves $7 on repairs. Additionally, the American Society of Civil Engineers estimates that driving on roads in need of repair in Minnesota costs each driver $480 per year. We need to find ways to get ahead of the deterioration. We think this combined return makes sense, and we think that residents will too.

What about state and federal funding? Can’t they help us with streets?

We’d love that! But it’s not happening for local roads, and we’re not going to wait any longer for a rescue. If the legislature chooses to pass increased transportation funding, it’s likely state and federal resources will focus their efforts on their own state and federal highways and bridges, and not on municipal streets. Currently, the state collects a gas tax that get allocated through a complicated system that essentially pays for Municipal State Roads – these dollars are call MSA (Municipal State Allocation) and are used on the state designated routes like Superior Street.
Do nonprofits pay taxes, or will they participate in the dedicated sales tax?

Nonprofits can apply for tax-exempt status. This means they do not pay property tax and can be exempted from sales tax. While on the surface this can be initially frustrating for tax payers, we have found that the amount of money that would be generated by nonprofits through a taxation system is currently not as significant as in many other communities, like St. Paul, for instance. Additionally, they provide important sets of services that government can’t sustain, so we appreciate their partnership.

Why sales tax for streets and not other revenue sources such as tourism tax?

Because currently 86,296 Duluth residents are paying for a built infrastructure that supports themselves, 35,000 daily commuters and 6.7 million annual tourists, and sales tax is a fair and equitable way to have all beneficiaries co-invest in the solution. Although a sales tax does require legislative approval, state law does not allow us to use tourism tax on streets.

What are Tourism Taxes and if tourists use streets, why can’t they help pay for them?

Tourism taxes are legislatively authorized taxes that have a specific application: tourism. A total of about $11 million is collected through hotel and motel stays, food and beverage taxes, etc. They are collected by entities which serve tourists, sent to the City to reallocate back into entities whose primary focus involves serving or growing tourism – essentially a circle of closed reinvestment. There are very clear parameters for the application and use of these funds. For instance, we provide funding (through a public process which requires city council authorization) to Visit Duluth, Lake Superior Zoo, Great Lakes Aquarium, Spirit Mountain and many others. In limited circumstances, the City has benefitted from this funding source to fund tourism-facing investments like fixing the pedestrian blue bridge and restoring parts of the Lakewalk. Using this source of funding for core, non-tourism city services or for streets is not only not possible, it is illegal and goes against state statute. However, tourists pay sales tax; should the referendum pass and the legislature approve it, tourists would be paying into our proposed streets solution.

I hear a lot about “bonding” and “bond payments” for streets but I’m not sure what it means.

Bonding is a form of financing, like a loan. You draw down a front payment and then pay it back gradually over the term of the bond. It can work really well in a lot of scenarios – a home mortgage can be a very good thing, for instance, as long as it’s within your means. But you want to avoid taking out loans for smaller items that lose their value – you would not want to take a loan out for a new stove, for instance. The same is true for government – streets tend to lose value, since they need constant care.
and attention, and if you bond without a pre-dedicated plan to repay those bonds, you end up paying
interest and taking money away from other budget areas to pay for a street that will probably need to
be redone by the time you make that last payment. That’s why we are committed to a “pay as you go"
model. It is hard to get the money upfront, but it can save more later. Some counties and cities have
chosen to bond against the transportation sales tax revenues collections to jump start street work - in
the right lending environment, and with the right bond rating, this can work.

**When I budget in my family I have to make really hard choices in order to make ends meet. I can’t just “raise” my income like government raises taxes. Why can’t you do the same thing?**

We do. Every year, it is pretty standard for a government entity to start with a deficit. We deliver
services but do not sell items to make up for those increased costs. We don’t directly charge for your
crime calls, for instance, but the cost of that call goes up every year because of the cost of body
camera, health insurance increases or new training requirements. All are good things. We just need to
pay for them. Multiply that reality by eight city divisions delivering utilities, library books, public safety,
building inspections, criminal investigations and more. This year we started our budgeting process in
April. Together, we made some very difficult decisions to translate your priority for streets. We value
your investment in the City, we recognize you work hard to do the right thing and pay your taxes and we
believe we do a good job of giving you good value. We don’t like raising your taxes any more than you
like paying them.

**Where exactly do my property taxes go?**

When people think about property taxes, they often think about the City. We do collect property tax –
24% of your total property tax bill goes to the City of Duluth for general operations. The remaining
portions go to St. Louis County (42%) Duluth School District ISD709 (27%), 3% to the voter-approved
county parks fund and an additional 4% to other sources. The impact of others’ taxation is a consideration for
us. We know that while our City portion is the smallest part, it’s the part which is most closely watched
and we want to provide good value. There is a chart in this book with the breakdown of the property tax
bill by taxing entity.

**Aren’t there other revenue sources besides taxation to meet the needs of cities?**

Actually, there are many revenue sources but none that we have direct control over like property taxes.
Think of our city budget of $83+million like a pie, with a variety of revenue sources, each of them a
different slice of that pie. There is a chart elsewhere in the budget that outlines this pie.

Put together, the slices make a whole. Because we essentially operate as a nonprofit, we do not charge
rates, fines or fees beyond what we can claim is our expense of providing that service. So we can’t
simply raise a rate or permit cost to make up for a budget deficit elsewhere. Other slices of the pie are set by outside entities – LGA makes up over 35% of our budget but is set by the legislature, for instance. We can move through each slice, but the summary is this: property tax makes up 19% of our 2018 budget but is the only variable we can adjust – and we can only adjust it upon itself. Meaning that when we raise the property tax levy 1% we do so only on that 19% of the budget, not the entire budget. For that reason, raising property taxes yields far less than what people expect – roughly $250,000, give or take.

That’s why you’ll often hear people speak to EXPANDING the tax base, so more taxation capacity is brought into the fold. This generally happens at a rate of 1-5% per year, depending on the overall growth in our economy. For all of these reasons, building a total $83+million budget requires caution, an understanding of all variables and the ability to be efficient with our spending.

Are staff wage increases part of the problem of budgeting?

Staff wages are a considerable part of our budget, but they aren’t a part of a budgeting problem. Because we are an employer who works within contracts we have predictable wage factors that we can predict from one year to the next, based upon what has been agreed to during negotiations. The single largest budgeting variable is health care, and it’s one that is impacted by trends outside of our control. It’s frustrating for us since an increase of 10% in health care can only be recouped by cuts elsewhere or an increase in the levy. We are in a completely reactive position on this significant factor.

I thought we were on solid financial ground, but in this budget you are making budget cuts across the entire organization. Are we in a financial crisis?

No, we are not in a crisis, but we are experiencing significant, annual financial stress because of a systemic imbalance with revenues and expenses. And unless we identify *sustainable* budget reductions (versus one-time savings) we are simply pushing one budget problem into the next. We’ve found these budget reductions. It’s not easy, not pleasant, but it’s what we must do. Like residents in our community, we need to assess how and where we are spending and how and when we can control those costs.

How can I find out more about the proposed dedicated sales tax or the City budget?

In addition to the public website where you can find information and leave a comment (http://duluthmntestsite/better-streets/) regarding the sale tax, we are holding three public meetings to present the “State of the Streets.” These dates and times are:

- Wednesday, August 16 – Harrison Community Center, 3002 West 3rd St. @ 5:30-7 PM
I will present my budget to the City Council at 6pm on August 14th – this is a public meeting, and you are welcome to attend it in Council Chambers. The presentation will be recorded and will be able to be found on our city website.

What happens next?

On August 14th Council will hear the budget proposal for 2018 and determine whether or not to put the referendum on the ballot for November. These are two separate tasks.

If the referendum language is approved, we will move ahead with public meetings (“State of the Streets”) and proceed to the November 7th election where voters will weigh in with their support or denial of the dedicated tax. If supported, we will focus efforts on establishing support within the state legislature for their approval. If allowed, the .5% dedicated sales tax would likely go into effect in August or November of 2018.

In regards to the budget, the council will review my proposal on August 14th, which begins the public process of decision making. After months of consideration and reflecting the needs of our organization, my team and I will already have made our budget determinations – the council will then get to make theirs. They have ultimate authority on the property tax levy and will commit to levy percentage on or before September 30th. We then move into finalizing the budget for 2018, and will be locked into a “not to exceed” levy, meaning it can go down from what was set at the end of September before the final 2018 budget is approved by council at the end of December, but not above. It is common to have things move around a little bit – sometimes there are unexpected expenses or revenues.