

**City Council Study Session Item #2
Meeting of August 24, 2015**

Brief Description: 2016 preliminary budget review

Recommended Action: Provide direction on key issues and preliminary levy

We are pleased to propose to the city council a 2016 levy and budget that ensures Minnetonka's position of fiscal responsibility, preserves our standards of excellence, and encourages innovative and creative thinking.

The budget presented here is an effort to right-size staff resources to meet accumulated service demands associated with an increasingly complex and changing environment in both public safety and human resource management during an ongoing improvement in the economy. In the latter case, a rise in revenue offsets expenses associated with the request. The proposed budget additionally addresses the appropriate maintenance needs of city streetscapes and at other city-owned landscaped facilities.

As outlined in this report, staff recommends ***increasing all combined levies for 2016 by 4.2 percent***, aligning with our long-term projections of annual levy increases of three to four percent. Of this total, ***2.0 percent supports capital infrastructure needs*** as provided in the adopted 2016-20 Capital Improvement Program (CIP). Another ***2.0 percent supports the General Fund operating budget***, and the remaining ***0.2 percent is an HRA levy increase***.

Because of the higher capital demands, operating requests are kept modest to stay mindful of reported stagnant wages in the private sector, our taxpayers. Despite continued rises in the cost of employee health care and some market force salary pressures, the city's operating costs are also being held down with the support of a very low inflation rate including reduced energy prices, especially fuel.

New development and redevelopment in the city significantly increased the city's property tax base last year as reported in March by the city assessor. Overall the city's assessed market value increased by 5.8 percent, a significant proportion of which was the result of actual improved real estate as opposed to market forces alone. In addition, commercial property values rose at a greater rate than did residential properties during the period, which causes a shift in the property tax burden from residential to commercial.

As a result, ***city property taxes for the median-valued home in Minnetonka (\$317,800 in 2015) will more than offset the proposed levy increase and will decrease taxes by around 4 percent.***¹

¹ This is an early estimate with some data not yet finalized by Hennepin County, and a more certain estimate will be provided when the information becomes available.

The city's proposed levy increase is likely to place Minnetonka in the middle of our group of similar cities in the metro. While several of our comparable cities began to receive Local Government Aid in 2014, Minnetonka will continue to not receive this state financial support in 2016.

OUR PUBLIC PROCESS

The purpose of this study session is to review key budget issues and provide direction on the 2016 preliminary tax levy and city budget, which will be set by council and certified to the county by September 30, 2015, as required by state law.² This is the maximum amount the city can levy for 2016.

This initial budget study session focuses on the bigger picture. Guided by these initial discussions, detailed budget requests will be reviewed in November, with the final budget adopted in December. The final levy may be less than the preliminary amount, but cannot be greater.

Minnetonka always encourages input on its budget from the public. In addition to the public budget hearing in early December, residents and businesses will again have an opportunity to provide feedback via the city's website, an opportunity that is publicized in the *Minnetonka Memo*. Comments will be shared with council as budget options are considered, and updated information will consistently be posted in the *Memo* and on the city's website.

ENSURING MINNETONKA'S POSITION OF FISCAL RESPONSIBILITY

As detailed in the city's adopted Strategic Profile, the city of Minnetonka takes a responsible, long-term perspective with financial planning and management (see attached 2015 profile status report). Decisions are made with the future in mind to ensure the city's ongoing ability to provide quality services at a reasonable price.

Current Spending & Financial Projections

Revenues. As the city's Comprehensive Annual Financial Report disclosed, 2014 ended roughly even after transfers with ***no additional revenue accumulating to the city's general fund balance*** for the first time in a number of years. This tighter fiscal

² The 2014 State Legislature extended the deadline for certifying city preliminary levies to the county from September 15 to September 30. However, HRA and EDA preliminary levies must continue to be certified by September 15. Although a bill was introduced to correct this inconsistency last session, it was not ratified. Therefore, both the general levy and the HRA levy for Minnetonka are scheduled for adoption by the council on September 14, 2015.

environment is projected to continue with **2015 revenues conservatively projected to just meet forecasted obligations** including capital fund transfers for the year as well.

Continued **low investment interest along with recreation fee revenue below projections** this year is anticipated to be offset by growth greater than budgeted in permits and licenses associated with the improving economy and a modest increase above forecast in public safety fine revenue. Most importantly, revenues are estimated to continue to cover projected obligations from 2016 through 2020 with an ongoing modest trend of rising between 2.3 to 3.3 percent annually during the period.

Spending. Revisions to operating budgeted costs in 2015 are minor. They include funding for unanticipated temporary costs related to work in the planning division, which is financed by permit fee revenue, and hiring before year-end an additional human resource staffer as outlined more fully later in this report (2015 costs of which are offset by the communications manager vacancy). As we approach the council's second detailed budget study session in November, additional information may adjust these current 2015 spending estimates. Per regular procedures, the CIP budget will be amended with levy and budget adoption in December to reflect more accurate capital project costs.

2016 BUDGET

At a cost of \$31.8 million and financed with multiple sources of revenue, the 2016 proposed General Fund operating budget is limited to 2.3 percent greater than the 2015 adopted budget. The new funds will be strategically used to:

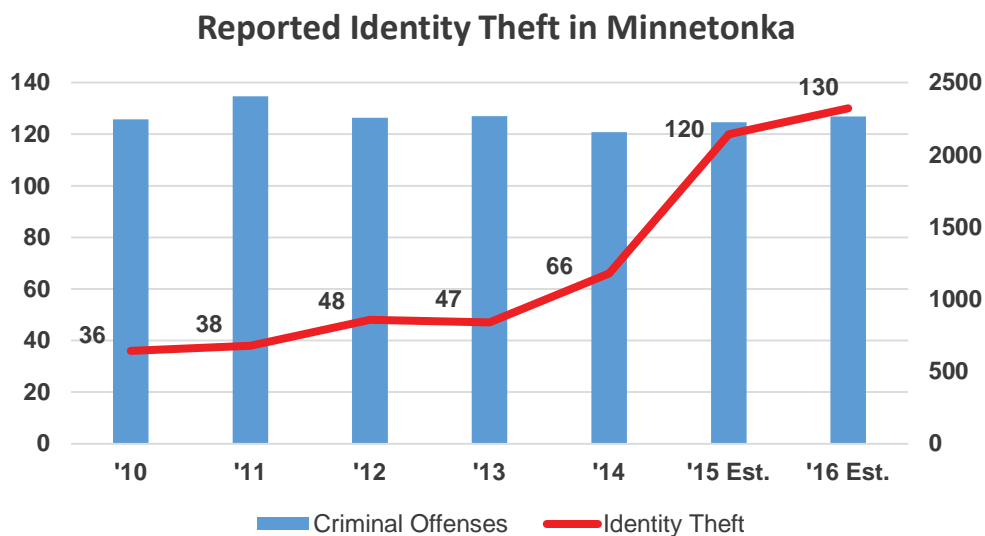
- right-size our public safety staffing to meet the challenges of increasing identity theft crimes and to serve a more robust retail environment;
- ensure we appropriately provide and keep up with all training requirements needed by a fully prepared suburban paid-on-call fire force;
- provide suitable care of our improved public landscapes and streetscapes to uphold our community's commitment to value our natural environment;
- make sure the city continues to be responsive and efficient to development needs as the economy continues to improve; and
- maintain our excellent workforce by investing in their recruitment, development and retention in an increasingly complex and heavily regulated human resource environment.

PUBLIC SAFETY

Police Service. The proposed 2016 budget includes funding for **one additional case investigator to proactively respond to current and rising demands related to identity and retail theft in the city.** The department's investigations team currently

consists of six investigators, of which two are assigned to retail crimes, and an additional four school liaison officers assigned to investigate juvenile-related cases. Organizational restructuring over the last number of years has significantly reduced staffing in this critical area from a period when there were twice as many retail investigators and seven school liaison officers who supplemented other investigations during summer school breaks.

Although some criminal activity has remained stable or diminished, yearly statistics show a marked increase in identity theft over the last five years, especially in the last year. At the same time, identity theft and other crimes such as fraud have become more sophisticated and therefore are more complicated and time consuming to investigate. There have been several cases of identity theft and fraud in Minnetonka with losses totaling over \$1 million. This trend is expected to continue.



With more senior housing units being constructed and as our community continues to age, we anticipate an increase in identity theft and fraud, because seniors are often the victims of these types of crimes. Staff expects additional reports of theft, identity theft and fraud as Ridgedale Mall completes its increase in overall space by 181,000 square feet. And, the significant growth in multi-unit apartments and condos in the city will likely add to the number of cases that are ultimately assigned to each investigator.

An additional investigator will provide resources needed to handle these growing numbers of cases, and the position will afford the police department the opportunity to more appropriately delve into a greater number of cases than would otherwise be possible due to limited staffing levels.

Fire Service. A new firefighter in Minnesota must receive a minimum of 300 hours of training before he/she is certified as a Firefighter/EMT. In 2014, the Minnetonka fire department oversaw and/or delivered nearly 3,900 cumulative hours of training for the

paid-on-call personnel who keep our community safe by responding to fires, hazardous materials incidents, and health-related emergencies, and we anticipate these numbers will be similar or greater in 2015.

The 2016 budget for the **fire department includes one additional full-time position** to ensure ongoing, stable administration of the rigorous and complex training required to maintain a strong and capable suburban fire force. The **new training officer** will absorb the work that has been carried out by two paid-on-call (POC) firefighters since the city's reorganization and downsizing during the Great Recession. Experience has shown that despite great diligence in providing an efficient and high quality training program, part-time firefighters and their POC positions, with requisite work time limitations under the Affordable Healthcare Act (ACA), are unable to support the time and undertaking needed for this essential responsibility.

The new training officer will also respond to fires and other emergencies as do the fire department's other five full-time positions, but his/her primary duties will be to develop and administer training programs. By making sure a grounded position is dedicated to this vital function, the city will secure its ongoing commitment to the paid-on-call fire force structure along with the great efficiencies it bears and the 85 firefighters who serve the city of Minnetonka.

STREETSCAPES & LANDSCAPES

The 2016 proposed budget also includes additional funding to supplement the city's contractual **resources dedicated to maintaining the trees in our streetscapes and landscaping along public rights-of-way**. City employees will continue to be supplemented by the cost-effective use of ICWC crews in a number of areas, but the availability of these crews has been found to be limited.

As major roadway improvements and neighborhood street reconstruction has been completed, one and two seasons into landscaping growth has provided the experience to more fully develop a maintenance and watering plan for each thoroughfare. The 2015 budget currently includes funding for a private vendor that is being contracted to maintain streetscapes and landscaping in the areas of Minnetonka Boulevard and CR101, Shady Oak Road from Bren Road to Excelsior Boulevard, and Glen Lake Station. In 2016, an additional private vendor will provide maintenance services for the two current CR101 projects and Shady Oak Road from Excelsior Boulevard to State Highway 7.

Additionally, as neighborhood roads are revitalized, resident expectations have increased to ensure boulevard trees are appropriately cut back and cared for. The natural resources division will be charged with overseeing **the tree trimming along neighborhood roads** to see that appropriate measures are taken to preserve our street-line arbor's health.

PARKS AND ENVIRONMENT

Natural Resources. *2016 will be the first complete year with full staffing for the pre-Emerald Ash Borer arrival phase of the city's EAB program.* The action plan for managing the bug's imminent arrival in Minnetonka and its inevitable devastation of the city's ash tree canopy began in 2014. The current level budget now funds a forestry technician and administrative assistant added with the last two budgets to the Natural Resources Division to support the program. All operating costs for the EAB program are provided in the General Fund operating budget.

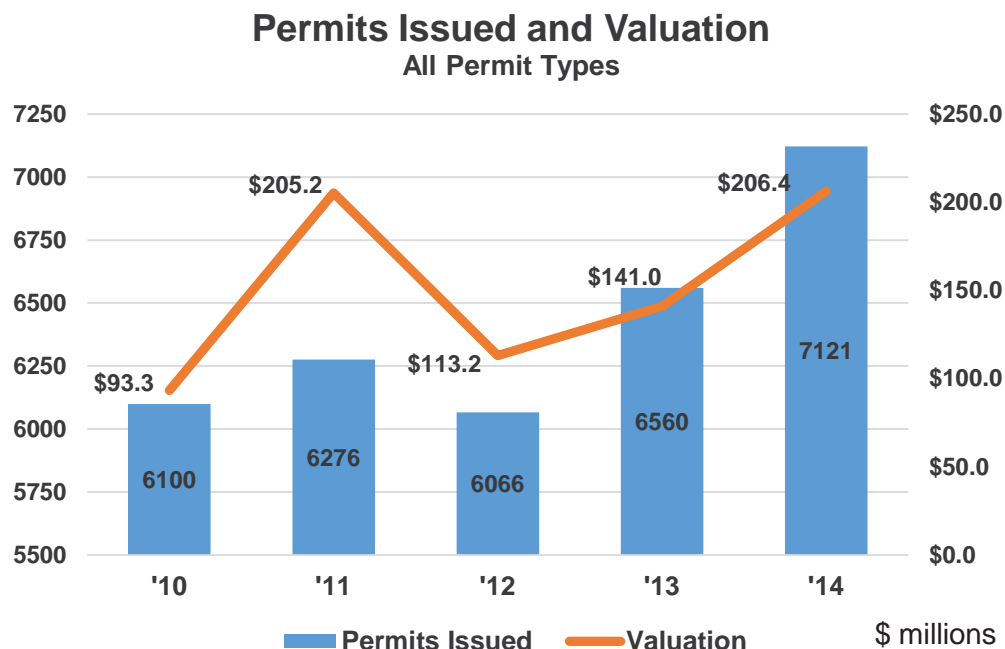
The pre-EAB arrival phase of the program includes chemical treatment of high-value ash trees; continued removal of damaged or unhealthy ash trees in parks and outlots, with slow, systematic removal and judicious replacement of other ash trees in those same areas; and thoughtful and cautious citations for removal of damaged or unhealthy ash trees on street rights-of-way under a continued cost sharing (50:50) plan with adjacent landowners. This year staff launched a bulk discount tree injection component to the program, which allows our residents to inoculate and treat their trees at reduced prices.

The adopted 2016-20 CIP restructured forestry funding in the capital budget to effectively use all resources and lessen the city's property tax burden. The portion of the EAB program in the capital budget provides for associated tree removal, stump grinding, reforestation and capital start-up. The adopted CIP reduced the annual Forestry Fund levy for these costs in the near term and supplanted those resources with settlement funds that were awarded to the city as a part of a class-action lawsuit regarding the use of the chemical herbicide Imprelis. Staff will continue to evaluate damage and destruction of the city's trees sustained due to use of the product and is confident that as the impacted areas mature, they can be suitably restored. The Forestry Fund levy would continue to increase over time as originally planned in preparation for the EAB's eventual arrival.

Also note that the accelerated tree trimming funds included in the proposed 2016 budget will be programmed under the Natural Resources Division general fund operating budget to ensure appropriate stewardship of the city's valuable streetscape trees.

DEVELOPMENT

Workload in the community development department continues to expand as a result of the economy's improvement with pressures from an increase in new development requests and construction permitting. In the two-year period since 2012, the number of permits issued by the city has increased by over 17 percent. While this is positive news, keeping appropriate staffing levels to provide timely customer service continues to be a challenge.



As the number of permit requests have risen, inspections staff have been supplemented with additional part-time employees, more multidisciplinary trained inspectors, and overtime. Although the augmented staffing has allowed us to perform fairly well over the last 18 months, there has been a noticeable increase in wait times for inspections and plan review. This is particularly the case when one inspector is away from the office.

Because the increase in workload is not expected to diminish across construction types in the city (apartments, commercial, industrial, and residential), the 2016 proposed budget includes funding for **an additional full-time inspector position**. The community development department will transition to the new position in 2015 by reducing some of the temporary wage hours. As the building permit system is fee based, revenue generated by the department offsets its costs.

GENERAL GOVERNMENT

Human Resources. Over the past number of years, changing demographics, retirements and generational workplace transformations have increased the challenges and demands upon human resource management. The city employs 241 full-time and regular part-time personnel, 80 POC firefighters, and approximately 400 seasonal employees. The current HR function is supported by two personnel. The revised 2015 and the 2016 proposed budget includes **one additional generalist position for the human resources team**.

At the end of 2014, 36 full-time positions or nearly 16 percent of the city's employees, were anticipated to turn over before the end of 2017. Fourteen have already changed during the first six months of 2015, with at least an additional six retirements anticipated before the end of this year.

With every new employee, transition and development is critical, particularly in a market for a new generation of workers who are more mobile and want a higher level of ongoing involvement. In a lean organization such as the city of Minnetonka, general support in human resources is critical for ensuring ongoing direct services to our public through an investment in one of our most important assets, our employees.

On top of these challenges, mounting complexities in health care and legal mandates are demanding more time than the current two-person HR staff can accommodate. While the city has sought in the past and continues to contract portions of this work to outside vendors, oversight of those contracts requires time on an ongoing basis, including complicated research and understanding in pension benefits, healthcare benefits, workers compensation claims, and now the administrative requirements of the Affordable Care Act (ACA). In 2016, all persons hired by the city will receive an additional tax document similar to the federal W-2 but relates to health care benefits for which data must be collected and reported throughout the year.

In addition to assisting and supporting managers for recruiting, onboarding, required safety and other training, the new human resources generalist position will also coordinate ACA reporting mandates for which the clock began October 2014 and for which data must be collected and analyzed monthly and reported annually beginning in 2016. The additional capacity provided by the new position will ensure that the division supports managers and department directors on all facets of human resource needs at appropriate service levels which are presently often unmet.

Personnel Expenses. Because the city is a service business, workforce-related changes, including the cost of healthcare, have a significant impact on both the city's work and its finances. The city will be negotiating two new 2016 contracts later this year with police officers and police sergeants, because the current contracts for those employee groups expire at year end. The labor agreement with public safety dispatchers expires the end of 2016 and public works personnel the end of 2017. Information currently indicates that there *may be some market wage pressures* from settlements in our comparable cities, if not for 2016, then likely for 2017.

Health care premiums are slated to increase in 2016 by an average of 10.5 percent. This is the third year of double digit increases in premiums after substantial reductions in prior years. The city's contribution is expected to increase to help partially offset these premium increases. As a member of the LOGIS consortium, the city is currently involved in studying the implications of moving toward self-insuring for 2017.

Discussion Question:

- ***Does the council support the proposed strategies for addressing service level pressures in public safety, community development and human resources, along with streetscape and landscape maintenance?***

SOUTHWEST LIGHT RAIL TRANSIT

On July 13, 2015, the city council adopted a resolution committing the city to contribute \$2 million for costs of the Southwest Light Rail Transit (SWLRT) project. The SWLRT project includes two station stops for Minnetonka. In addition to our contribution to the project's costs, the city has planned for its own capital infrastructure improvements around each of the two stations. The latter improvements are included in the city's adopted 2016-20 Capital Improvement Program (CIP), but the former is not.

In order to plan for the additional \$2 million contribution likely to be paid in 2017 or 2018, the 2016 proposed budget includes amendments to the 2016-20 CIP, and staff will outline here financial options and other issues to be considered in the city council's deliberations regarding this commitment.

Funding of the SWLRT project should be considered in light of other significant potential projects currently on the horizon for the city in the next five to ten years as provided in the city's CIP. These include:

- Implementation of a more *comprehensive trails and sidewalks improvement plan*, the unfunded portions of which are currently estimated at over \$11 million;
- *Ridgedale area improvements*, including an unfunded park in the CIP for \$500,000;
- significant capital costs associated with unmet *public safety space needs* (no current cost estimate);
- a *Glen Lake activity center*, currently unfunded at a very rough estimate of \$15 million;
- *Big Willow Park enhancements*, currently unfunded at an estimate of \$1.6 million; and
- *Opus area bridge replacement*, \$3 million from MnDOT bridge funds have not yet been secured for 2016.

Additionally, the council should consider any costs associated with the city's future interests in pursuing economic development enhancement and affordable housing opportunities.

Based on current actual city capital improvement costs and the SWLRT project components as outlined above, staff believes the city can garner over the next few

years **savings from other city capital projects in various funds** (Street Improvement Fund, Storm Water Fund and Electric Franchise Fees) **to support approximately \$1 million of the \$2 million contribution.**

Staff recommends discussing three options for the remaining approximately \$1 million of the commitment. All three options include use of the Special Assessment Construction Fund (SACF), which is limited by the city charter to permanent transfers to the corpus of the Community Investment Fund (CIF), temporary or permanent transfers to other capital project funds and special assessment required cash flow. The following reflects current commitments of the SACF:

\$million	Use	Status
\$8.2	Fund balance as of 12/31/2013	
(2.0)	Cash flow for special assessments	Revolving balance
(1.6)	Shady Oak (CR 7-Excel) property	10-yr transfer payback from Devpt Fund*
(1.7)	Ice Arena B improvement project	Transfer payback as afforded from CIF
(2.5)	Cullen-Smith property	Transfer until 2016 open space bonding
\$0.4	Ending Avail Balance until 2016 bonding	
2.5	Open space bonding payback	
<u>\$2.9</u>	Available Cash Balance in 2017	* May be paid back sooner, upon sale

Three options to consider are:

- 1) **A permanent cash transfer** to a capital project fund from the SACF.
- 2) A temporary cash transfer from the SACF to a capital project fund to be repaid over a period of years from incremental increases to the **Housing and Redevelopment Authority (HRA) levy** -- When the money is fully repaid to the SACF, the levy could be reduced or future revenues used for economic development enhancement and affordable housing opportunities.

At the HRA levy's current level of \$175,000 annually, the adopted 2016-20 Economic Improvement Program (EIP) accumulates an estimated uncommitted fund balance of only \$240,000 by the end of 2025. Therefore, a possible scenario is to increase the HRA levy by \$75,000, which equates to a 0.2 percent increase above the city's 2015 levy, in order to pay back the transfer over ten years. The payback period could be shortened with greater or additional HRA levy increases.

- 3) A temporary cash transfer from the SACF to a capital project fund to be repaid over a period of years using revenue derived through the adoption of a **new natural gas franchise fee** -- After the money is fully repaid, revenue from the franchise agreement might be used to finance a more comprehensive trails and sidewalk improvement plan. Many cities, including Edina, St. Louis Park and Plymouth, currently use this source of revenue for

street improvements, sidewalks and trails. Staff would more fully explore this option, if it is the council's preference.

The option of bonding for the contribution was reviewed and is not recommended since the issue would be too costly for its small size and scope. Staff has dismissed alternative 1 because of the limiting effect it would have on the SACF for other unforeseen needs. Although option 3 shows promise, the demand for trail and sidewalk improvements is more imminent, and if supported by the council in the future, this financing tool provides a dedicated funding stream to meet connectivity and walkability goals.

Therefore, staff **recommends option 2 to increase the HRA levy by 0.2 percent or an additional \$75,000**. The city council has consistently stated that the HRA levy should only increase when a known project is at hand. For years the council has been a strong supporter of the SWLRT project. Use of the HRA levy presents an opportunity for a specific use at a minimal increase to the overall HRA levy. Further, the owner of a median valued home in Minnetonka would continue to see a decrease in the city share of 2016 property taxes even with such a levy increase.

Discussion Question:

- ***Does the council support the recommended combination financing strategy for the city's \$2 million commitment to SWLRT?***

HRA LEVY

The city's first levy for housing and redevelopment began in 2009. State law limits levies, and the maximum rate is 0.0185 percent of a city's taxable market value. This equals approximately \$1.52 million in Minnetonka. The 2009 levy rate of 0.00117 percent raised \$100,000 and was solely dedicated to WHAHLT (West Hennepin Affordable Housing Land Trust). Beginning in 2010, the annual levy increased to \$175,000 (0.00212 percent) and has remained at that dollar level to accommodate village center master planning, housing programs, and marketing efforts.

The Economic Development Advisory Commission (EDAC) reviewed the HRA budget at its August 13 meeting and, on a unanimous vote, recommended adopting **a preliminary HRA levy of \$175,000**. The budget would be for comprehensive planning, housing rehab loans, and a small amount for a business survey. The EDAC was informed about the council's potential discussion of the light rail funding and how this may or may not change the HRA levy request.

Staff recommends adopting the EDAC's recommendation **plus an additional increase in the HRA levy of \$75,000** to begin a 10-year payback to the SACF for the city's

commitment to the SWLRT project. The additional amount would result in an estimated \$3 less savings in property taxes for the median-valued home (\$317,800 in 2015) in Minnetonka.

Discussion Question:

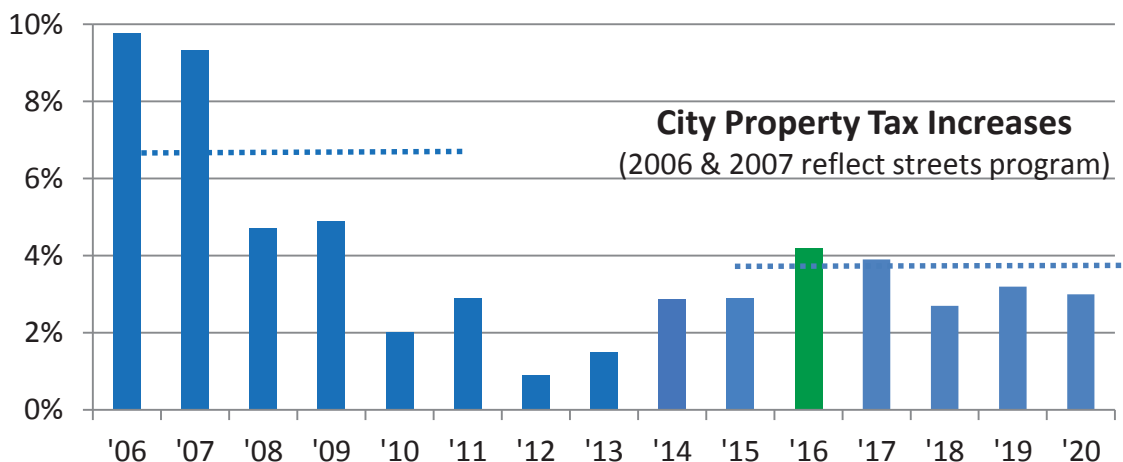
- **Does the council agree that \$250,000 should be certified as the HRA preliminary levy for 2016?**

2016 PRELIMINARY LEVY

The 2016 proposed operating and adopted capital budgets plus the HRA budget will require an **increase in the city property tax of 4.2 percent**. Of this overall increase, 2.0 percent is associated with financing the first year of the city’s 2016-20 capital budget, which was adopted by the city council in May 2015, 2.0 percent is associated with the General Fund operating budget, and 0.2 percent is the proposed HRA levy increase.

Operating budget	2.0%
Capital program	2.0
SWLRT - HRA levy	0.2
Total levy increase	4.2%

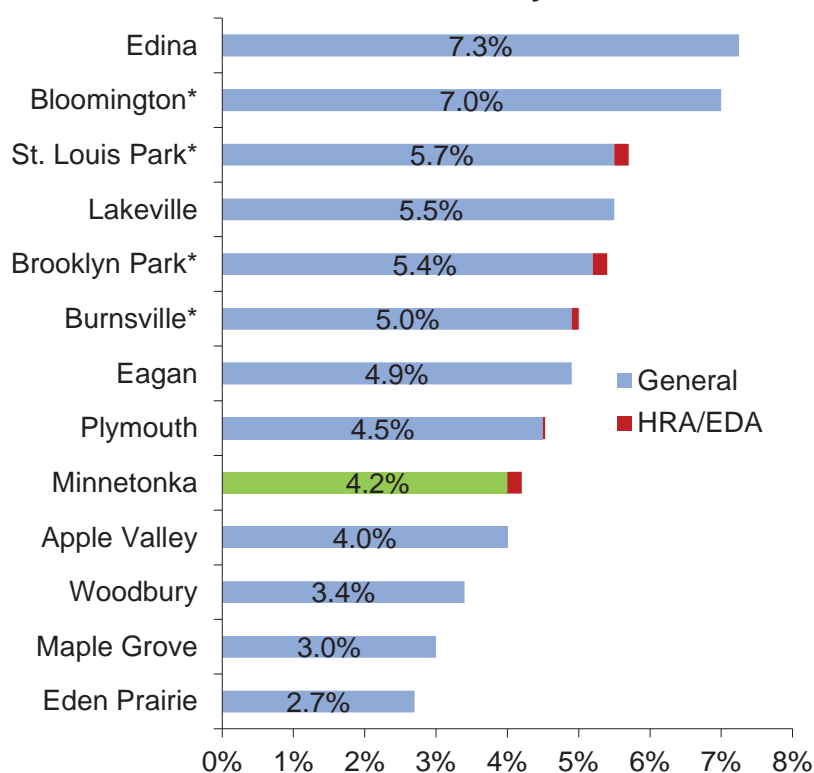
Overall inflation is exceptionally low this year, currently 0.4 percent nationwide, 0.5 percent in the Midwest, and this has significantly helped to keep the city’s projected operating costs low for 2016. Almost all of the proposed budget and levy increase is associated with the requested new positions and keeping up with streetscaping and landscaping care as outlined above. A significant decrease in the price of fuel is forecasted to continue into 2016, and therefore meaningful savings are garnered with reductions in the city’s budget for those costs across all programs, which will serve to offset the increases.



As a result the city's 2016 tax increase of 4.2 percent is in keeping with our recent history of increases *below historic averages*. Included in these projections are the new tax abatement levy for Ridgedale Mall to begin in 2016 at \$26,000, which is offset by an increase in tax capacity, and in 2017, the referendum debt levy for the final \$2.5 million referendum bonding for the Cullen-Smith open space property purchase.

Comparisons with Other Cities. The proposed 2016 city levy increase is likely to place Minnetonka in the middle of comparable cities. The levy variable changes amongst these communities is related to a diversity of reasons including new or retiring debt, additional staffing, reductions in liquor store revenues, and capital needs.

Potential 2016 Preliminary Tax Increases



* Denotes comparable cities that receive Local Government Aid (LGA).

Further, four of the comparable cities listed continue to receive an allocation of LGA, which began in 2014. As has been the case for over a decade, Minnetonka does not and will not receive LGA in 2016. Equally important, unlike many of these other cities, the city does not rely upon special assessments to fund street reconstruction and maintenance.

Homeowner Impacts. New development and redevelopment in the city significantly increased the city's property tax base last year as reported in March by the city assessor. Overall the city's assessed market value increased by 5.8 percent, a

significant proportion of which was the consequence of actual improved real estate as opposed to market forces alone.

In addition, commercial property values improved at a greater rate than did residential properties during the period. As a result, ***city property taxes for the median-valued home in Minnetonka (\$317,800 in 2015) will more than offset the proposed levy increase and will decrease by around 4 percent.*** This is an early estimate with some data not yet finalized by Hennepin County, and a more certain estimate will be provided when the information becomes available.

Discussion Question:

- ***Does the council agree that \$34,088,440, plus \$26,000 for Ridgedale tax abatement (overall 4.0 percent increase) should be certified as the city's preliminary general levy for 2016?***

Summary

Responsible long-term financial planning has continued to position the city of Minnetonka to accommodate the slow economic recovery and federal and state political uncertainties, while appropriately providing services to city residents and businesses. The preliminary city tax levy will be limited to an overall increase of 4.2 percent for 2016. This increase is around the middle of comparable cities. It ensures our position of fiscal responsibility, preserves our standards of excellence, and encourages innovative and creative thinking.

As always, the city of Minnetonka will continue to provide the excellent services our residents and businesses have come to expect, and at a reasonable price, both in 2016 and well into the future.

Originated by:

Geralyn Barone, City Manager
Merrill King, Finance Director