

CITY OF LAKEVILLE, MINNESOTA
EXECUTIVE AUDIT SUMMARY
YEAR ENDED DECEMBER 31, 2016

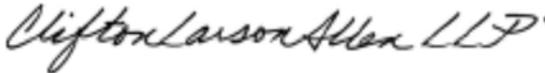
June 5, 2017
To the City Council and Management
City of Lakeville, Minnesota

We have prepared this management report in conjunction with our audit of the City of Lakeville, Minnesota's (the City) financial statements for the year ended December 31, 2016. The purpose of this report is to provide comments resulting from our audit process and to communicate information relevant to city finances in Minnesota. We have organized this report into the following sections:

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

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

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



CliftonLarsonAllen LLP

Minneapolis, Minnesota
June 5, 2017

AUDIT SUMMARY

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

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

We have audited the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City as of and for the year ended December 31, 2016, and the related notes to the financial statements. Professional standards require that we provide you with information about our responsibilities under auditing standards generally accepted in the United States of America and *Government Auditing Standards*, as well as certain information related to the planned scope and timing of our audit. We have communicated such information to you verbally, in our Governance Communication Letter, and in our audit engagement letter. Professional standards also require that we communicate the following information related to our audit.

PLANNED SCOPE AND TIMING OF THE AUDIT

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

AUDIT OPINION AND FINDINGS

Based on our audit of the City's financial statements for the year ended December 31, 2016:

- We issued an **unmodified** opinion on the City's basic financial statements. Our report included a paragraph emphasizing that the City changed its accounting policy related to the valuation of certain General Fund inventories, specifically related to snow-removing chemicals, from the consumption method to the purchase method, during the year ended December 31, 2016. Our opinion was not modified with respect to this matter.
- We reported no deficiencies in the City's internal control over financial reporting that we considered to be material weaknesses or significant deficiencies.
- The results of our testing disclosed no instances of noncompliance required to be reported under *Government Auditing Standards*.
- We reported no findings based on our testing of the City's compliance with Minnesota laws and regulations.

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

GOVERNMENTAL FUNDS OVERVIEW

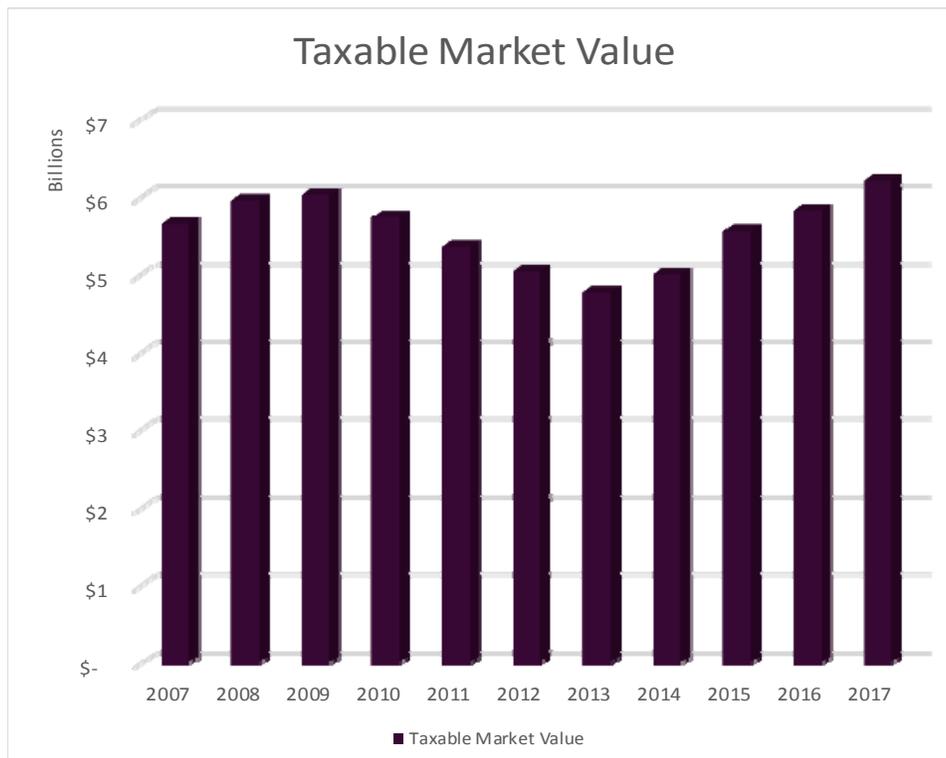
This section of the report provides you with an overview of the financial trends and activities of the City's governmental funds, which include the General, special revenue, debt service, and capital project funds. These funds are used to account for the basic services the City provides to all of its citizens, which are financed primarily with property taxes. The governmental fund information in the City's financial statements focuses on budgetary compliance, and the sufficiency of each governmental fund's current assets to finance its current liabilities.

PROPERTY TAXES

Minnesota cities rely heavily on local property tax levies to support their governmental fund activities. For the 2015 fiscal year, local ad valorem property tax levies provided 39.7 percent of the total governmental fund revenues for cities over 2,500 in population, and 35.5 percent for cities under 2,500 in population. Property tax levies certified by Minnesota cities for 2016 increased about 5.5 percent over 2015, compared to an increase of 4.0 percent the prior year. Levy limits were not in place for 2015 or 2016.

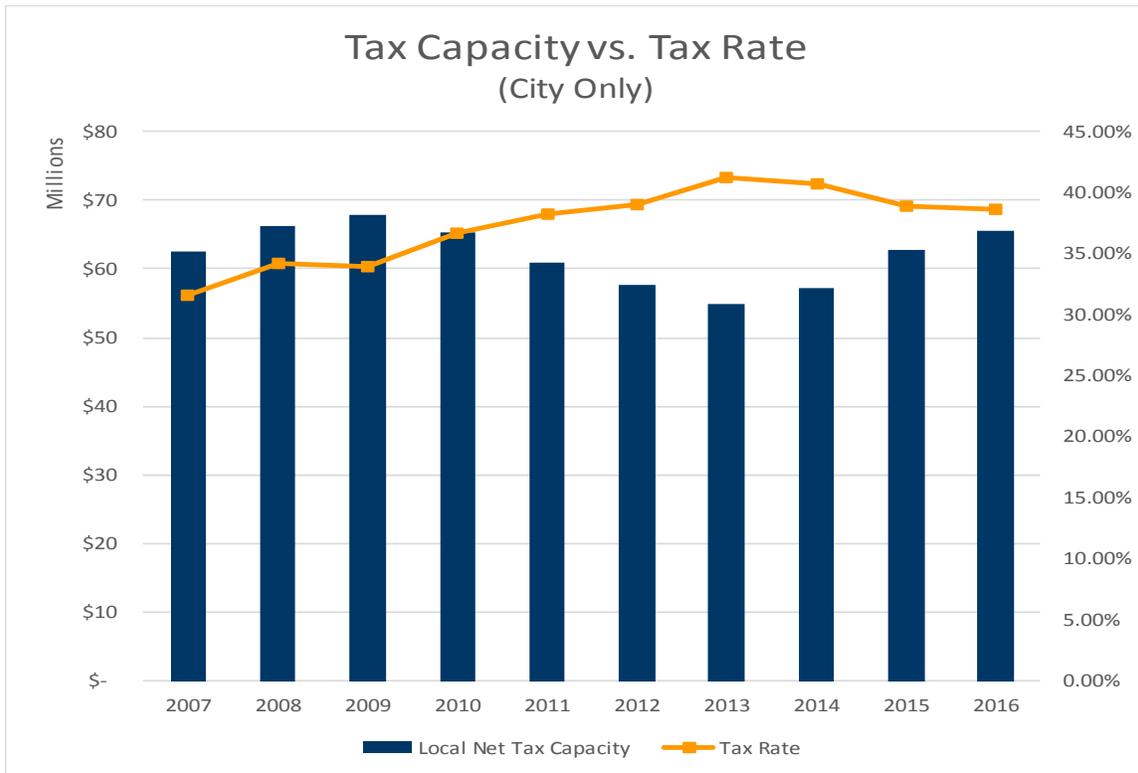
The total market value of property in Minnesota cities increased about 5.7 percent for the 2016 levy year, following an increase of 8.5 percent for levy year 2015, a slight increase 1.1 percent for 2014 and a four-year trend of declining market values for levy years 2010 through 2013. Market values showed increases across all property categories for 2016, with gains in the market values of residential homestead properties (5.0 percent) and non-homestead residential properties (9.1 percent) outpacing the market value gain of commercial/industrial properties (4.9 percent). Because the assessed valuation used for levying property taxes is based on values from the previous fiscal year (e.g., the market value for taxes payable in 2016 is based on estimated values as of January 1, 2015), market value improvement has lagged behind recent upturns in the housing market and the economy in general.

The City's taxable market value increased 11.2 percent for taxes payable in 2015 and 4.9 percent for taxes payable in 2016. The following graph shows the City's changes in taxable market value over the past 11 years:



Tax capacity is considered the actual base available for taxation. It is calculated by applying the state’s property classification system to each property’s market value. Each property classification, such as commercial or residential, has a different calculation and uses different rates. Consequently, a city’s total tax capacity will change at a different rate than its total market value, as tax capacity is affected by the proportion of the City’s tax base that is in each property classification from year-to-year, as well as legislative changes to tax rates and exemptions. The City’s tax capacity increased 9.9 percent and 4.5 percent for taxes payable in 2015 and 2016, respectively.

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



The improvement in property tax capacities contributed to decreases to the overall state-wide and metro area tax rates for 2016. The following table presents the average tax rates applied to city residents for each of the last two levy years, along with comparative state-wide and metro area rates:

*Rates Expressed as a percentage of net tax capacity						
	All Cities State-Wide		Seven-County Metro Area		City of Lakeville	
	2015	2016	2015	2016	2015	2016
	Average Tax Rate					
City	46.9	46.5	43.4	43.0	39.0	38.7
County	44.7	44.1	42.9	42.3	29.6	28.6
School	27.1	27.5	28.3	28.6	32.2	39.1
Special Taxing	6.9	6.9	8.8	8.7	4.9	4.8
Total	125.6	125.1	123.4	122.6	105.7	111.2

Both the total tax rate applied to Lakeville taxpayers and the City's tax rate have been well below both the state-wide and metro averages in recent years. The City's tax rate for 2016 was lower than the previous year, despite a 3.8 percent increase in the City's certified tax levy, due to the improvement in tax capacity as discussed above.

The school tax rate for the City represents an average of Independent School District (ISD) No. 192, Farmington; ISD No. 194, Lakeville; and ISD No. 196, Rosemount – Apple Valley – Eagan.

GOVERNMENTAL FUND BALANCES

The following table summarizes the changes in the fund balances of the City's governmental funds during the year ended December 31, 2016, presented both by fund balance classification and by fund:

	Fund Balance		Increase (Decrease)
	As of December 31,		
	2016	2015	
Fund Balances of Governmental Funds			
Total by Classification			
Nonspendable	\$ 695,830	\$ 447,284	\$ 248,546
Restricted	37,947,697	35,659,756	2,287,941
Committed	21,651,118	17,982,431	3,668,687
Assigned	1,478,522	-	1,478,522
Unassigned	12,175,467	8,390,255	3,785,212
Total governmental funds	\$ 73,948,634	\$ 62,479,726	\$ 11,468,908
Total by Fund			
General	\$ 15,076,500	\$ 12,374,928	\$ 2,701,572
General Obligation Debt Service	14,903,538	17,450,559	(2,547,021)
G.O. Improvement Debt Service	7,037,315	5,274,675	1,762,640
Building Capital Projects	808,425	497,062	311,363
Improvement Construction Capital Projects	1,450,488	2,242,797	(792,309)
Nonmajor Funds	34,672,368	24,639,705	10,032,663
Total governmental funds.	\$ 73,948,634	\$ 62,479,726	\$ 11,468,908

In total, the fund balances of the City's governmental funds increased \$11,468,908 during the year ended December 31, 2016.

The majority of the increase was in committed and unassigned fund balances, which increased \$3.7 million and \$3.8 million, respectively, from the prior year. The increase in the committed balance was primarily related to the collection of water trunk fees in the water capital projects fund in addition with the fund starting in a negative position after 2015, the issuance of \$8 million of bonds, the fund was able to recover the deficit and make the fund whole again. This was partially offset by a \$2.2 million decrease in the committed fund balance of the Equipment Fund resulting from capital expenditures in excess of revenues.

The increase in unassigned fund balance was also partially due to the increase in the Water Capital Project fund balance as it had a negative \$3.1 million fund balance in the prior year which is required to be shown as unassigned. The General Fund also had a \$1 million increase in unassigned fund balance as a result of revenues in excess of expenditures.

GOVERNMENTAL FUNDS REVENUE AND EXPENDITURES

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

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

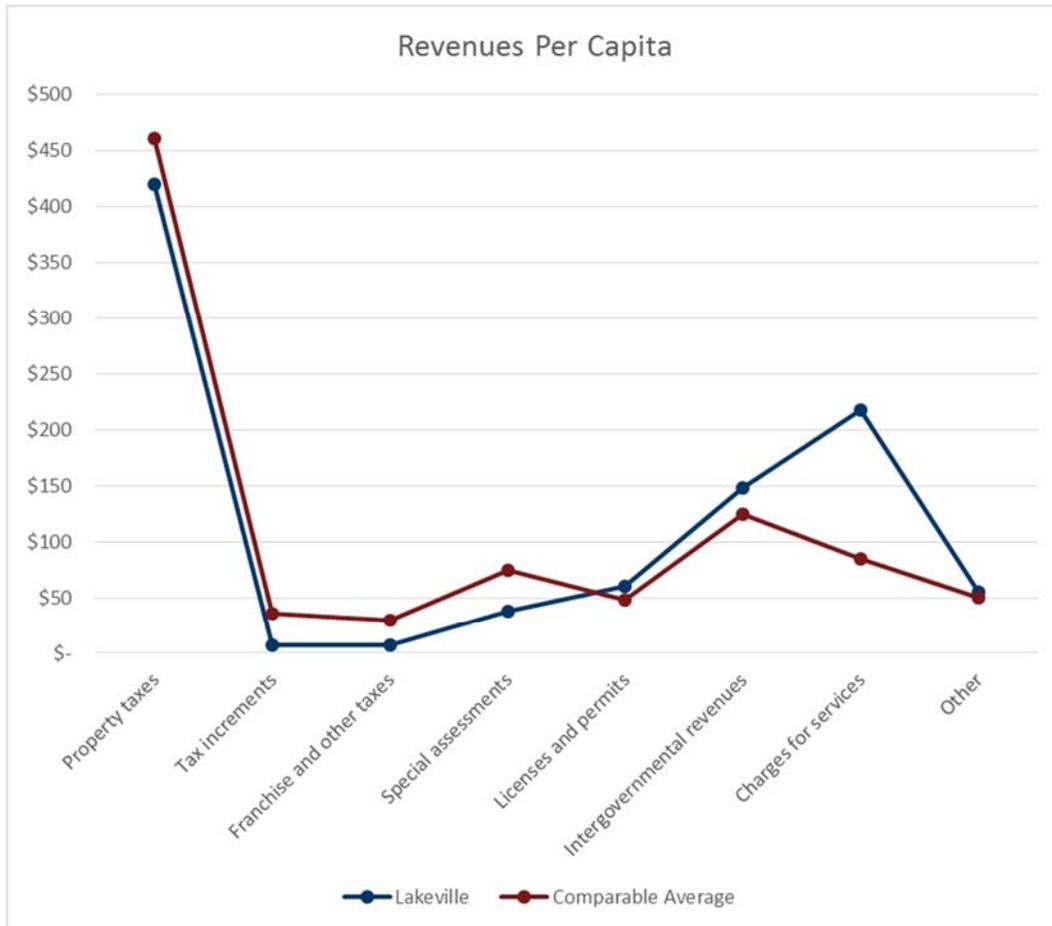
We have designed this section of our management report using per capita data in order to better identify unique or unusual trends and activities of your city. We intend for this type of comparative and trend information to complement, rather than duplicate, information in the Management's Discussion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

Governmental Funds Revenue per Capita With State-Wide Averages by Population Class				
Year	State-Wide	City of Lakeville		
	December 31, 2015	2014	2015	2016
Population	20,000 - 100,000	59,361	59,991	60,965
Property taxes	\$ 443	\$ 399	\$ 414	\$ 421
Tax increments	37	14	7	7
Franchise and other taxes	25	11	11	7
Special assessments	59	28	29	38
Licenses and permits	43	36	55	61
Intergovernmental revenues	156	84	87	148
Charges for services	94	142	196	218
Other	58	71	31	29
Total Revenue	915	785	830	929

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

Total governmental funds revenues were \$56.6 million in 2016, about \$6.8 million (13.7 percent) more than the prior year. On a per capita basis, governmental fund revenue for 2016 was \$99 higher than the prior year. Property tax revenue was \$7 per capita higher than the previous year due to a levy increase and excess tax increment distribution. Licenses and permits revenue was \$6 per capita higher than last year due to increased development activity. Intergovernmental revenues were \$61 per capita higher than last year due to an increase in municipal state-aid revenue for several large capital projects. Charges for services were also \$22 per capita higher than last year due to increased development activity, resulting in additional connection and area charges, park dedication fees, and engineering charges. Revenue in the "other" category shown above decreased \$2 per capita.

Below is a table of the City of Lakeville's 2016 governmental funds revenue per capita as compared to the average per capita revenues for the governmental funds of several comparable cities for the year 2015. The comparable cities included in the average below (and in any other instances of a comparable city average included in this report) are Apple Valley, Blaine, Bloomington, Chanhassen, Eagan, Eden Prairie, Inver Grove Heights, Maple Grove, Plymouth, Prior Lake, Savage, Shakopee, and Woodbury.



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

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

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

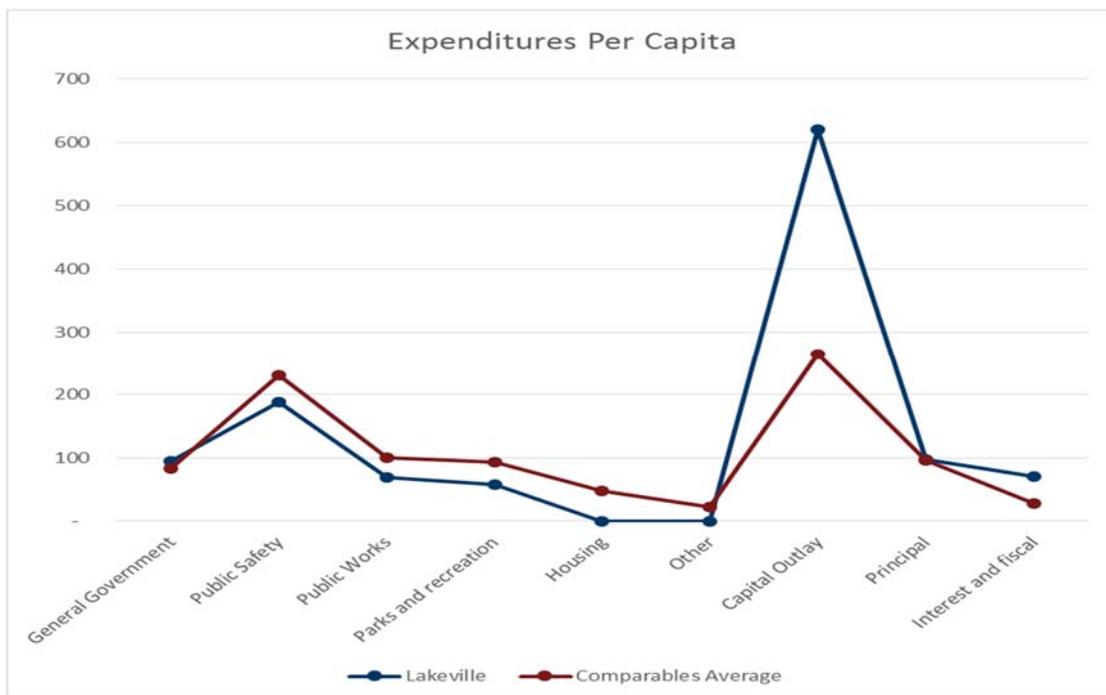
Debt Service – Although the expenditures for debt service may be relatively consistent over the term of the respective debt, the funding source is the important factor. Some debt may be repaid through specific sources such as special assessments or redevelopment funding, while other debt may be repaid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

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

Governmental Fund Expenditures per Capita With State-Wide Averages by Population Class				
Year	State-Wide	City of Lakeville		
	December 31, 2015	2014	2015	2016
Population	20,000 - 100,000	59,361	59,991	60,965
Current				
General Government	\$ 89	\$ 96	\$ 87	\$ 95
Public Safety	261	174	182	189
Public Works	96	64	64	70
Parks and recreation	90	56	59	57
	<u>536</u>	<u>390</u>	<u>392</u>	<u>411</u>
Capital Outlay				
And construction	286	361	528	622
Debt Service				
Principal	117	101	123	97
Interest and fiscal	33	65	63	70
	<u>149</u>	<u>166</u>	<u>186</u>	<u>168</u>
Total Expenditures	<u><u>971</u></u>	<u><u>917</u></u>	<u><u>1,106</u></u>	<u><u>1,201</u></u>

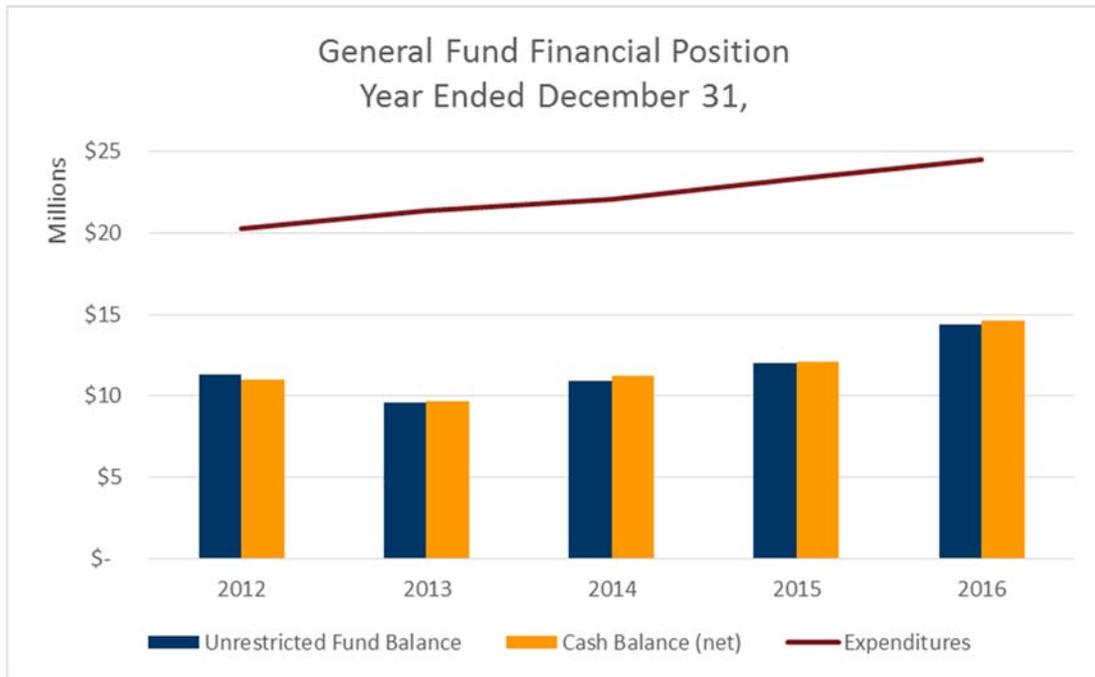
Total expenditures in the City's governmental funds for 2016 were \$73.2 million, an increase of \$6.9 million (10.4 percent) from the previous year, or \$95 per capita. The increase was mainly in capital outlay, which was \$94 per capita higher than the previous year, primarily due to several large street and utility improvement projects. Scheduled debt service principal and interest costs were also \$18 lower per capita than the prior year.

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



GENERAL FUND

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



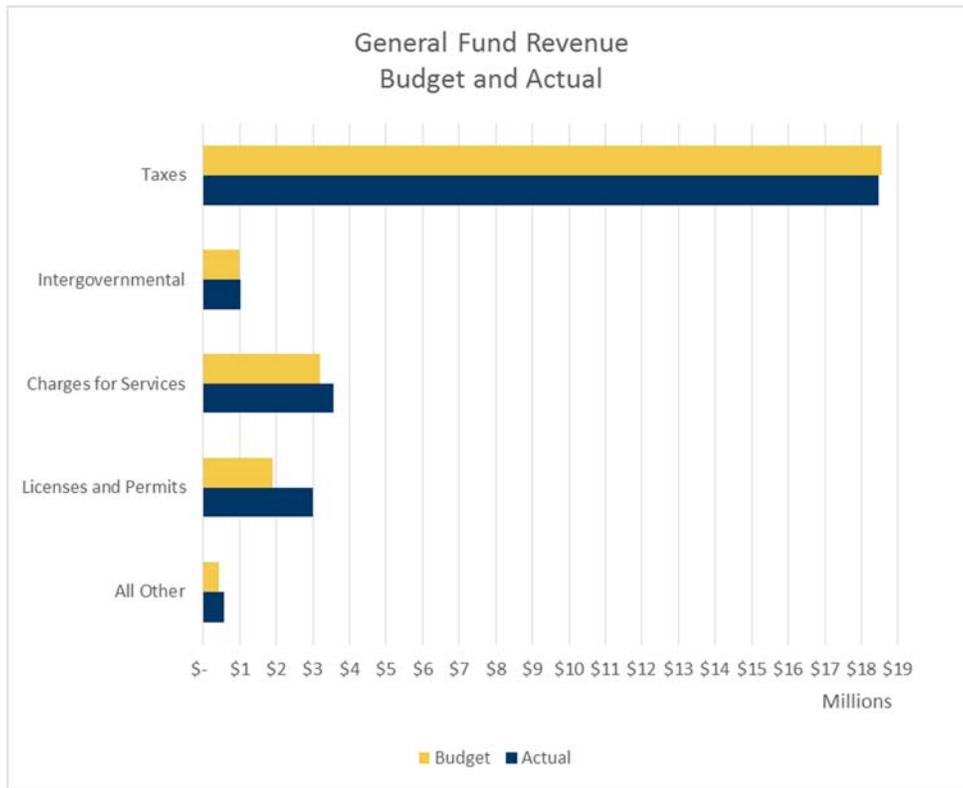
The City's General Fund cash and investments balance at December 31, 2016 was \$14,610,871, an increase of \$2,544,514. Total fund balance at December 31, 2016 was \$15,076,500, which is an increase of \$2,393,104 from the prior year, and \$2,650,167 higher than projected in the City's final budget.

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

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

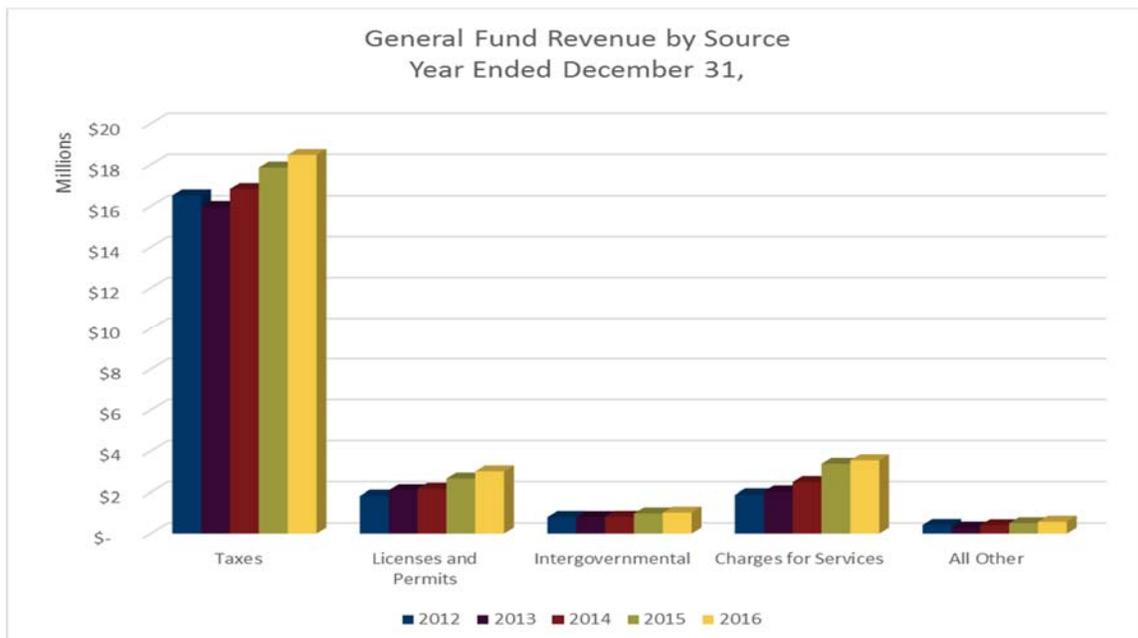
The City's General Fund's unrestricted fund balance at the end of the 2016 fiscal year represents approximately 58.8 percent of annual expenditures based on 2016 levels, compared to 51.3 percent at the end of the previous year.

The following graph reflects the City's General Fund revenue sources for 2016 compared to budget:



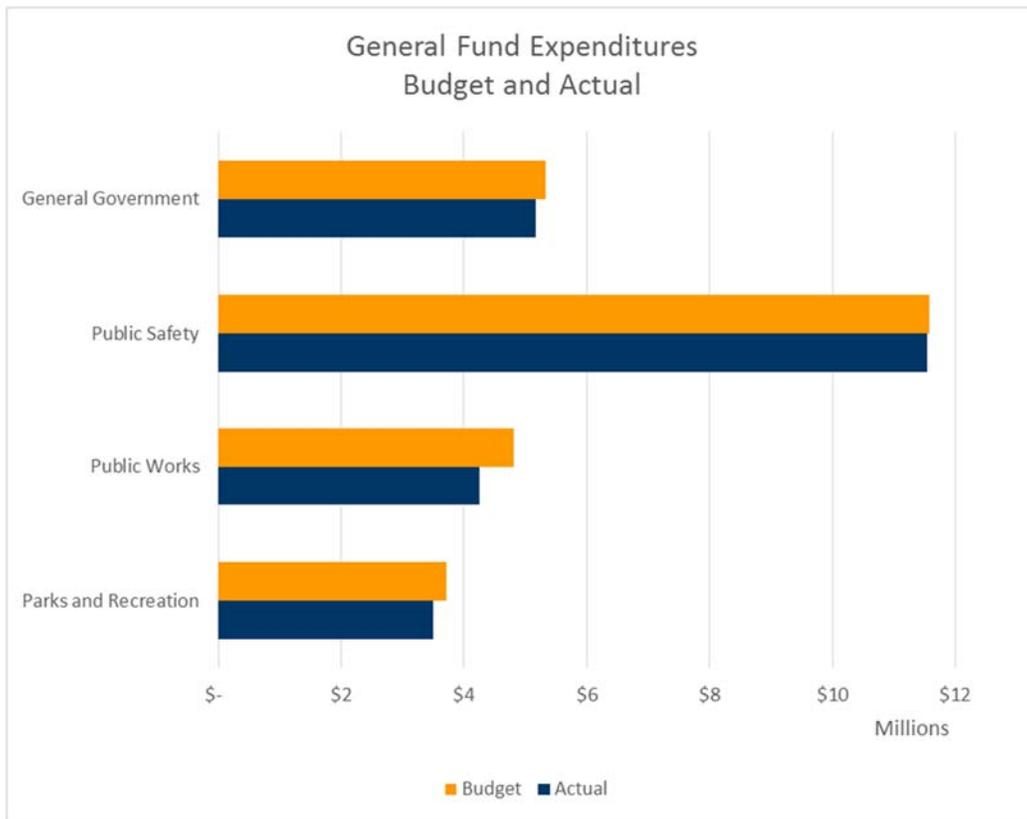
General Fund revenue for 2016 was \$26,632,181, which was \$1,562,088 (6.2 percent) more than budget. Charges for services were \$356,306 over budget, mostly due to engineering fees charged to construction projects. Licenses and permits revenue was over budget by \$1,102,522, primarily due to the number of residential building and construction related permits issued.

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



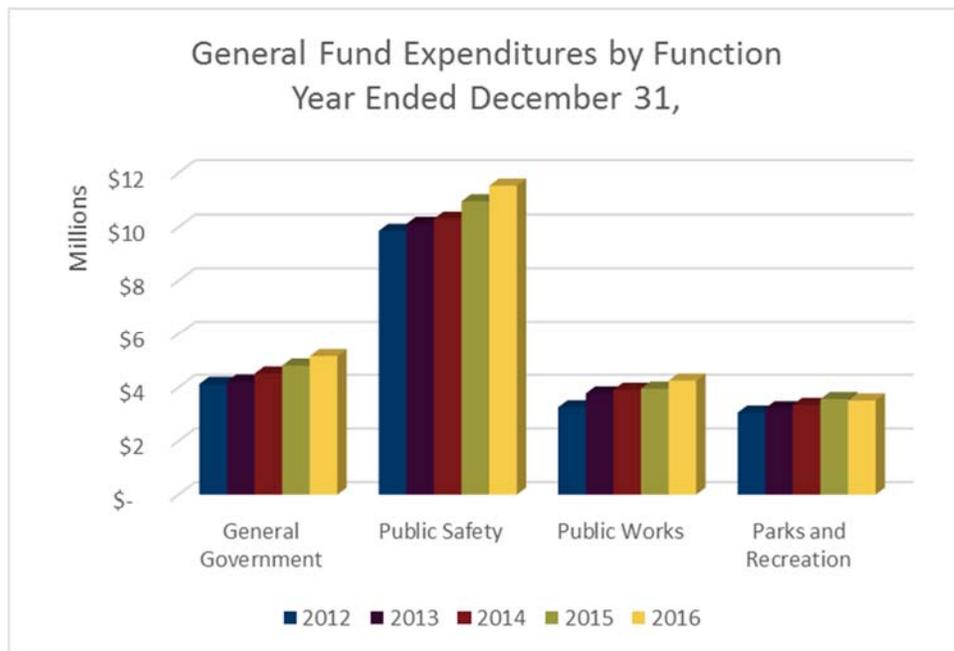
Overall, General Fund revenues increased \$1,259,064 (5.0 percent) from the previous year. Property tax revenue was \$620,760 more than last year due to a 3.85 percent increase in the property tax levy. Intergovernmental revenue increased \$41,933 due to county grants received. Revenue from charges for services (up \$171,932) and licenses and permits (up \$352,177) were both higher than last year due to increased development activity. Finally, revenue in the “all other” category as shown above was \$72,262 higher than last year, mainly due to an increase in revenue from fines and forfeitures and fluctuation in interest returns.

The following graph illustrates the components of General Fund spending for 2016 compared to budget:



Total General Fund expenditures for 2016 were \$24,450,590, which was \$1,088,079 (4.3 percent) under the final budget. General Fund expenditures were under budget in every functional area, as shown in the graph above. General government expenditures were \$165,356 under budget, with the largest savings in finance, human resources, information systems, and legal counsel. Public safety expenditures were \$33,677 under budget, primarily in police other charges and services. Public works expenditures were \$565,312 under budget, mainly in operations and maintenance and street maintenance personnel and commodities costs. Parks and recreation costs were under budget by \$203,963, mainly in park personnel, maintenance charges and services.

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



Total General Fund expenditures for 2016 were \$1,182,697 (5.1 percent) higher than the previous year, with the increase spread across all program areas with the exception of parks and recreation which decreased slightly (\$52,699). The majority of the increase was in personnel costs, which were due to contractual wage increases, inflationary benefit cost increases, and the addition of about seven full-time employees compared to the prior year.

ENTERPRISE FUNDS OVERVIEW

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

ENTERPRISE FUNDS FINANCIAL POSITION

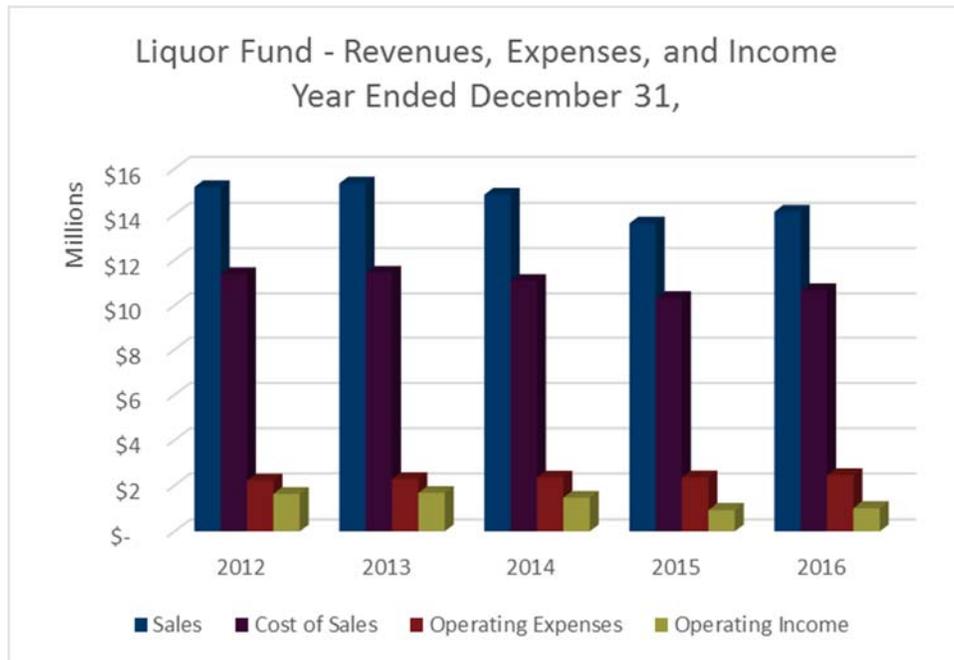
The following table summarizes the changes in the financial position of the City's enterprise funds during the years ended December 31, 2016 and 2015, presented both by classification and by fund:

Enterprise Funds Change in Financial Position			
	Net Position		Increase (Decrease)
	As of December 31,		
	2016	2015	
Net Position of enterprise funds			
Total by classification			
Net Investment in capital assets	\$ 129,086,090	\$ 116,288,771	\$ 12,797,319
Restricted for Debt Service	\$ 323,875	\$ 323,875	\$ -
Unrestricted	\$ 9,584,936	\$ 8,196,986	\$ 1,387,950
Total Enterprise Funds	\$ 138,994,901	\$ 124,809,632	\$ 14,185,269
Total by Fund			
Liquor	\$ 3,942,455	\$ 4,135,906	\$ (193,451)
Utility	\$ 135,052,446	\$ 120,673,726	\$ 14,378,720
Total Enterprise Funds	\$ 138,994,901	\$ 124,809,632	\$ 14,185,269

In total, the net position of the City's enterprise funds increased by \$14,185,269 during the year ended December 31, 2016. The Liquor Fund net position decreased by \$193,451, due mostly to transfers of almost \$1.1 million to governmental funds to provide funding for debt service requirements, various capital projects, and general overhead costs. The increases in both the net investment in capital assets and the net position of the Utility Enterprise Fund were primarily due to capital infrastructure contributions of \$17.9 million received from developers, other government agencies, and the City's governmental funds.

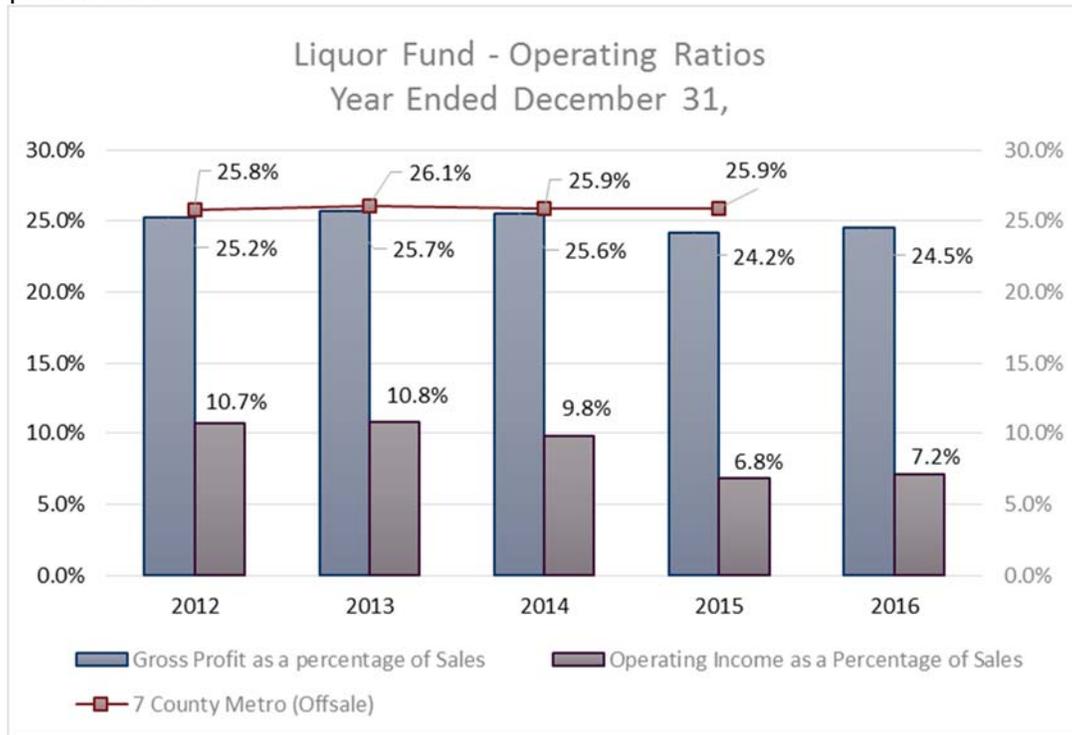
LIQUOR FUND

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



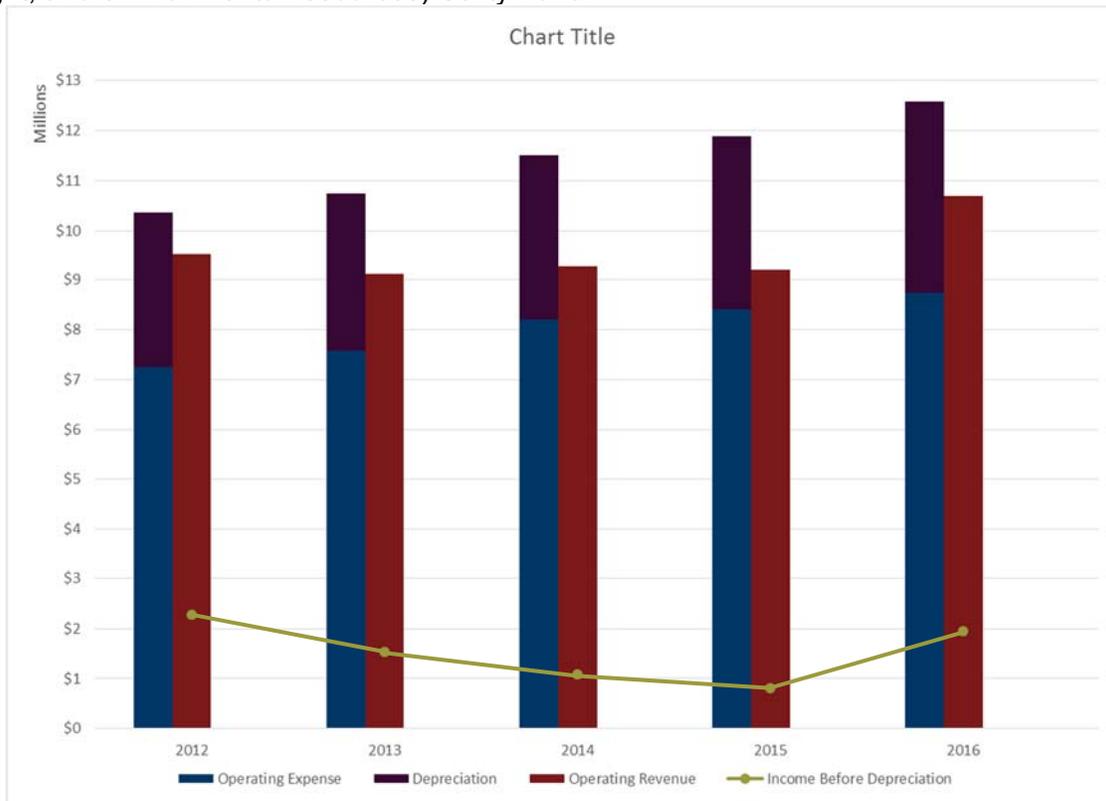
The Liquor Fund ended 2016 with a net position of \$3,942,455, a decrease of \$193,451 from current year operations. Of this, \$3,433,113 represents net investment in capital assets and \$323,875 is restricted in accordance with revenue bond covenants, leaving \$185,467 of unrestricted net position.

Gross liquor sales for 2016 were \$14,130,830, an increase of \$519,536 (3.8 percent) from 2015. The Liquor Fund generated a gross profit of \$3,464,143 in 2016, or about 24.5 percent, of gross sales. Operating expenses for 2016 were \$2,453,328, an increase of \$95,079 (4.0 percent) from the prior year. Net operating income for 2016 was \$1,010,815, or about 7.2 percent, of gross sales. The increase in gross sales and the resulting increase in the two operating ratios shown below were primarily attributable stabilization during 2016 as the City has faced significant increases to competition in previous years. The Liquor Fund also made transfers out of \$1,074,318 to support the General Fund, for debt service, and for various capital needs.



UTILITY FUND

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



The Utility Fund ended 2016 with net position of \$135,052,446, an increase of \$14,378,720 from current year operations. Of the net position balance, \$125,652,977 represents the City's net investment in utility capital assets, leaving \$9,399,469 of unrestricted net position.

Utility Fund operating revenue was \$10,692,185 for 2016, an increase of \$79,655 (16.0 percent), mainly due to increase in water usage and sewer discharge coupled with increase in rates.

Operating expenses (including depreciation of \$3,847,385) were \$12,581,506, which represents an increase of \$700,053 (5.9 percent). The increase was primarily attributable to increases in personnel costs and purchased services related to maintenance and depreciation.

The Utility Fund also received capital contributions of \$17,879,600 in 2016 from developers, other governmental agencies, and the City's governmental funds.

GOVERNMENT-WIDE FINANCIAL STATEMENTS

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

STATEMENT OF NET POSITION

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

The following table presents the components of City's net position as of December 31, 2016 and 2015, for governmental activities and business-type activities:

	As of December 31,		Increase (Decrease)
	2016	2015	
Net Position			
Governmental Activities			
Net Investment in capital assets	\$ 148,684,068	\$ 141,868,136	\$ 6,815,932
Restricted	38,516,463	33,860,946	4,655,517
Unrestricted	2,134,179	(4,929,168)	7,063,347
Total governmental activities	<u>\$ 189,334,710</u>	<u>\$ 170,799,914</u>	<u>\$ 18,534,796</u>
Business-type activities			
Net Investment in capital assets	\$ 129,086,090	\$ 116,288,771	\$ 12,797,319
Restricted	323,875	323,875	-
Unrestricted	9,757,400	8,420,410	1,336,990
Total business-type activities	<u>139,167,365</u>	<u>125,033,056</u>	<u>14,134,309</u>
Total net position	<u><u>\$ 328,502,075</u></u>	<u><u>\$ 295,832,970</u></u>	<u><u>\$ 32,669,105</u></u>

The total net position of the City increased \$32.7 million during the 2016 fiscal year. Of the increase, \$18.5 million came from governmental activities and \$14.2 million from business-type activities. One of the primary reasons for the increases in both the governmental and business-type activities was the amount of infrastructure contributed by developers and others during 2016, which totaled about \$37.5 million.

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

STATEMENT OF ACTIVITIES

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

The following table presents the change in the net position of the City for the years ended December 31, 2016 and 2015:

	2016			2015
	Expenses	Program Revenues	Net Change	Net Change
Net (expense) revenue				
Governmental activities				
General government	\$ 8,028,316	\$ 5,005,889	\$ (3,022,427)	\$ (2,078,781)
Public safety	16,369,670	1,952,237	(14,417,433)	(10,329,933)
Public works	17,711,240	36,948,865	19,237,625	9,793,113
Parks and recreation	5,626,149	6,709,683	1,083,534	(873,267)
Interest on long-term debt	3,930,168	-	(3,930,168)	(3,296,665)
Business-type activities				
Liquor	2,601,732	3,467,905	866,173	762,076
Utility	13,558,839	19,777,037	6,218,198	3,364,514
Total net (expense) revenue	<u>\$ 67,826,114</u>	<u>\$ 73,861,616</u>	6,035,502	(2,658,943)
General Revenues				
Property taxes and tax increments			26,173,822	25,338,778
Investment earnings			459,781	420,693
Total general revenues			<u>26,633,603</u>	<u>25,759,471</u>
Change in net position			<u>32,669,105</u>	<u>23,100,528</u>
Net position, beginning			<u>295,832,970</u>	<u>272,732,442</u>
Net position - ending			<u>\$ 328,502,075</u>	<u>\$ 295,832,970</u>

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

The difference in public works is mainly the result of increased capital contributions, utility connection charges and special assessments of \$10.9 million during 2016.

LEGISLATIVE UPDATES

Despite the 2017 legislative session ending with a projected budget excess of \$743 million for the 2016–2017 biennium and projected surplus of \$1.65 billion for the 2018-2019 biennium, the most favorable budget forecast in over a decade, some progress was made but not everything was accomplished that the Governor and Legislators were hoping to complete.

The following is a summary of recent legislation affecting Minnesota cities in 2016 and into the future:

Local Government Aid (LGA) – The Legislature completely overhauled the LGA formula for fiscal year 2014 and thereafter, creating a three-tiered formula that includes separate “need factor” calculations for cities with populations under 2,500, between 2,500 and 10,000, or over 10,000. The new formula simplified the LGA calculation, and reduced the volatility of the LGA distribution by limiting the amount it may decline in a given year. Beginning in 2015, any reduction to a city’s calculated LGA distribution will be limited to the lesser of \$10 per capita, or 5 percent of their previous year net tax levy. For cities that gain under the new formula, the increases will be distributed proportionate to their unmet need, as determined by the new “need factor” calculations. The state-wide LGA appropriation was \$516.9 million for fiscal 2016 and 2017, and is \$534.4 million for fiscal 2018 and thereafter. The \$15 million increase in LGA for fiscal year 2018 is a permanent increase which was approved by the omnibus tax bill signed by Governor Dayton. The omnibus tax bill also corrected a formula error affecting 20 cities.

Sales Tax Exemption – Cities (both home-rule and statutory) were exempted from paying sales tax on qualifying purchases, effective for purchases made on or after January 1, 2014. Purchases of goods or services by an exempt local government for a publicly-provided liquor store, gas or electric utility, golf course, marina, campground, café, laundromat, solid waste hauling or recycling operation, or landfill will remain taxable.

The 2014 Legislature extended the definition of tax exempt local government to include all special district; city, county, or township instrumentalities; economic development authorities; housing and redevelopment authorities; and all joint power boards or organizations. However, the effective date of this expanded exemption list was delayed until January 1, 2017 by the 2015 Legislature.

Sunday Liquor Sales – Starting Sunday July 2, 2017 Minnesota liquor are now able to allow of-sale intoxicating liquor sales on Sundays. In preparation for this cities should be reviewing liquor ordinances to ensure the change in State Statutes do not contradict city ordinances. Some city ordinances specifically restrict sales on Sundays. To remain compliance with city ordinances and State Statutes, this should be reviewed and amended as necessary.

Omnibus Bonding Bill – The Legislature approved a Omnibus Bonding Bill during the special session, authorizing approximately \$851 million in capital improvements. This includes \$136 million in waste water, drinking water, and storm water infrastructure improvements; \$116 million in spending for local roads; \$49 million in bridge projects; and \$71 million in rail safety projects.

REAL ID Bill – The REAL ID Bill was also passed during the most recent session. This creates three options for driver’s license. These include the REAL ID which will meet all federal requirements to allow access to federal buildings and airports; the standard license as it is currently established; and the enhanced ID that is also currently an option. Options 1 and 2 will be the same price for individuals. Under the Bill’s passage it provided a compliance exemption to 2020.

Small Cities Assistance Account – A one-time appropriation of \$12.5 million was provided to create a new Small Cities Assistance Account to assist with construction and maintenance of roads located within eligible cities, defined as a statutory or home-rule charter city that does not receive municipal state aid street financing (generally those with a population under 5,000). The aid will be distributed to eligible cities biannually in each year funds are available based on the following formula: 5 percent equally to all eligible cities; 35 percent allocated proportionately on each city's share of lane miles to the total for all eligible cities; 35 percent allocated proportionately on each city's population to the total for all eligible cities; and 25 percent allocated proportionately on each city's state-aid adjustment factor to the total for all eligible cities.

Automated License Plate Reader (ALPR) Policy – Law enforcement agencies that utilize ALPRs are required to establish policies governing their use that are consistent with statutory guidelines. The Legislature placed limitations on the type of data that can be collected using ALPRs, and clarified the circumstances under which that data is considered public or private. A limitation of 60 days was established for the retention of data collected by ALPR not related to an active criminal investigation. Standards were established for the sharing of ALPR data between law enforcement agencies. Independent audits will be required starting after August 1, 2017.

Elections – The Elections Omnibus Bill made numerous changes to elections administration laws, including timeline clarification for entities that switch from odd to even election years; changes to requirements for canvassing primary results; establish uniform special election dates, requirements to establish polling places by December 31st each year for the subsequent year by resolution; disclosure of election judge party affiliations; and allows political parties to provide a list of election judges willing to travel outside of their jurisdiction.

Charitable Gambling – Changes to the State's charitable gambling laws will now require cities and counties who have a 10 percent contribution requirement to acknowledge the organization contributing the money. This can be completed at the time of receipt or when the funds are disbursed.

Omnibus Tax Bill – The Omnibus Tax Bill included the provisions to increase LGA funding by \$15 million and fix the LGA formula error. IT also adjusted income limits for entities with affordable housing tax increment financing districts. The Bill also gave authorization to municipalities for workforce housing tax increment financing districts. Not included in this Bill was the exemption to exclude construction materials from sales tax requirements for local governments.

Proposed Ordinance Notification – The State amended Chapter 77 to require cities to provide at least 10 days notice for most proposed ordinances. New ordinances and amendments to existing ordinances are affected. Notification must be completed as follows: via e-mail if a city has an electronic notification system in place; post the ordinance in a public location; and update the city's website if ordinances are posted to a city's website.

Pensions – Governor Dayton vetoed the pension bill that was sent to his desk. This Bill would have focused on the Police and Fire Fund sustainability.

ACCOUNTING AND AUDITING UPDATES

GASB Statement No. 74, “Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans” – the objective of this statement is to improve the usefulness of information about postemployment benefits other than pensions (other postemployment benefits or OPEB) included in the general purpose external financial reports of state and local governmental OPEB plans for making decisions and assessing accountability. The provisions of Statement No 74 are effective for fiscal periods beginning after June 15, 2016.

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

GASB Statement No. 80, “Blending Requirement for Certain Component Units – an amendment of GASB No. 14” – the objective of this Statement is to improve financial reporting by clarifying the financial statement presentation requirements for certain component units. The provisions of Statement No. 80 are effective for periods beginning after June 15, 2016 and should be applied retroactively.

GASB Statement No. 81, “Irrevocable Split-Interest Agreements” – the primary objective of this Statement is to improve accounting and financial reporting by establishing recognition and measurement requirements for irrevocable split-interest agreements. Another objective of this Statement is to enhance the transparency and decision-usefulness of general purpose external financial reports, and their value for assessing accountability, by more clearly identifying resources that are available to a government. The provisions of Statement No. 79 are effective for periods beginning after December 15, 2016 and should be applied retroactively.

GASB Statement No. 82, “Pension Issues, an amendment of GASB Statements No. 67, No. 68, and No. 73” – the objective of this Statement is to improve consistency in the application of pension accounting and financial reporting requirements by addressing certain issues that have been raised with respect to Statements No. 67, Financial Reporting for Pension Plans, No. 68, Accounting and Financial Reporting for Pensions, and No. 73, Accounting and Financial Reporting for Pensions and Related Assets That Are Not within the Scope of GASB Statement 68, and Amendments to Certain Provisions of GASB Statements 67 and 68. The provisions of Statement No. 79 are effective for periods beginning after June 15, 2016, except for the requirement of paragraph 7 in a circumstance in which an employer’s pension liability is measured as of a date other than the employer’s most recent fiscal year-end. In that circumstance, the requirements of paragraph 7 are effective for that employer in the first reporting period in which the measurement date of the pension liability is on or after June 15, 2017.

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

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

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