Scope and Methodology

This publication is intended to help local government officials, policy makers, and the public understand city financial operations. The report summarizes, through data tables and charts, the financial operations of Minnesota cities for calendar year 2007.[1] Minnesota cities are required to submit annual financial reports to the Office of the State Auditor pursuant to Minn. Stat. §§ 6.74-.75 and §§ 471.697-.698.[2]

The data tables presented in this report are divided into governmental funds and proprietary funds. The governmental funds consist of the General, Special Revenue, Capital Projects, Permanent, and Debt Service Funds. The first section of the report provides an overview of all cities and compares cities over and under 2,500 in population. The second section of the report presents a detailed overview of the financial operations of cities over 2,500 in population. The third section provides a detailed overview of the financial operations of cities under 2,500 in population.

Following the overviews, Tables 6 and 7 present a summary of the activities in the governmental funds of all cities. Tables 8 through 11 present a summary of the governmental funds of cities over 2,500 in population. Tables 12 through 14 present a summary of the governmental funds of cities under 2,500 in population. Tables 15 through 17 present the data by individual city.

Table 18 lists the bonded and other long-term debt outstanding as of December 31, 2007, by individual city. Other long-term debt refers to liabilities such as long-term lease agreements, installment purchase contracts, and notes.

Tables 19 and 20 present an analysis of the 2006 and 2007 unreserved fund balances in the General and Special Revenue Funds of all cities reporting on a modified accrual basis. Table 19 details the actual unreserved fund balances, the percent change in unreserved fund balances from 2006 to 2007, and a comparison to 2007 total current expenditures. Table 20 presents the fund balance data sorted by unreserved fund balances as a percent of total current expenditures.

Cities using a modified accrual basis of accounting report separate fund balances for all of their governmental funds and denote the amounts that are reserved and unreserved. Cities using a cash basis of accounting report a single cash balance for all governmental funds at the end of the fiscal year. An analysis of unreserved fund balances for cities using a cash basis of accounting is therefore not appropriate, and is not provided. Appendix A provides a more detailed discussion of fund balances.

Table 21 shows municipal enterprises by city. Minnesota cities operate many types of public service enterprises. These enterprises furnish a variety of services and operate wholly or primarily with revenues derived from the sale of goods or services.

[1] The 2007 report includes two new cities. The Town of New Scandia incorporated as the City of Scandia in 2007; and the cities of Elko and New Market merged to become the City of Elko New Market.
[2] Eight cities failed to comply with the reporting requirements of Minn. Stat. §§ 6.74-.75 and §§ 471.697-.698. The eight cities are: Alexandria, Biscay, Conger, Funkley, McGregor, New Hope, Westport, and Williams.

In addition to this publication, the Office of the State Auditor maintains an interactive database containing several years of data that can be accessed through the website at: www.auditor.state.mn.us.

Accounting Difference for Cities Over and Under 2,500 in Population

For cities in Minnesota, the classification as over or under 2,500 in population helps to determine the type of governmental accounting to which they must adhere. All cities over 2,500 in population must have a financial statement in compliance with generally accepted accounting principles (GAAP), which is a modified accrual basis of accounting. Modified accrual basis accounting recognizes an economic transaction or event as revenues in the operating statement when the revenues are both measurable and available to liquidate liabilities of the current period. Available means collectible in the current period or soon enough thereafter to be used to pay liabilities of the current period. Similarly, expenditures are generally recognized when an event or transaction is expected to draw on current expendable resources.

Cities under 2,500 may opt to use a cash basis of accounting. In 2007, 355 of the 636 small cities (56 percent) opted to use a cash basis of accounting.[3] Cash basis accounting provides for the recording of receipts (revenues) when received in cash and the recording of disbursements (expenditures) when paid in cash.

[3] There are 642 small cities but the figure listed here reflects only the 636 cities that provided their 2007 financial information to the Office of the State Auditor.

Executive Summary

Current Trends – All Cities

- Total revenues of the governmental funds for all Minnesota cities amounted to $4.69 billion in 2007. This represents an increase of 4.7 percent over 2006 revenues. Total revenues of cities over 2,500 in population increased 4.9 percent, while revenues of cities under 2,500 in population increased 3.1 percent (pg. 5).

- Total expenditures of the governmental funds for all cities totaled $5.32 billion in 2007. This represents a decrease of 0.7 percent from 2006. Total expenditures of cities over 2,500 in population decreased 0.4 percent, while total expenditures for cities under 2,500 decreased 3.1 percent (pg. 5).

- The largest expenditure categories for both groups of cities are streets and highways and public safety. For large cities, streets and highways accounted for 23 percent of total expenditures, and public safety accounted for 24 percent. For small cities, streets and highways accounted for 26 percent of total expenditures, and public safety accounted for 20 percent (pgs. 5-6).

- The unreserved fund balances of large cities' General and Special Revenue Funds totaled $1.32 billion in 2007. This represents an increase of 0.4 percent over the level reported in 2006. Large city unreserved fund balances as a percent of total current expenditures averaged 48 percent in 2007, compared to 50 percent in 2006 (pg. 17).

Current Trends – Cities Over and Under 2,500 in Population

- Among large cities, the sources of revenue that grew at the greatest rate between 2006 and 2007 were: local unit grants (35 percent), interest earnings (30 percent), tax increments (17 percent), and fines and forfeits (11 percent). Those sources of revenue showing the greatest decreases were: franchise taxes (-25 percent), gravel and gambling taxes (-19 percent), and licenses and permits (-10 percent) (pg. 11).

- For small cities, the sources of revenue that grew at the fastest rate between 2006 and 2007 were: local unit grants (77 percent), interest earnings (17 percent), county grants (9 percent) and taxes (6 percent). County and local unit grants are generally contributions from local government partners in large capital projects. The categories showing the greatest decrease between 2006 and 2007 were: licenses and permits (-16 percent), federal grants (-8 percent), and all other revenues (-5 percent) (pg. 18).

- Cities under 2,500 carried long-term debt totaling $1.20 billion at the close of 2007. This represents an 8 percent increase over the level in 2006. On a per capita basis, small cities carried $2,927 in long-term debt, compared to $2,152 for large cities (pg. 23).

Ten-Year Trends – All Cities

Governmental Revenues

- While cities appear to have ended 2007 in good financial condition with revenues growing 5 percent and expenditures decreasing 1 percent, an examination of city finances between 1998 and 2007 reveal a noteworthy trend. In particular, when adjusted for inflation[4], 2007 revenue and expenditure levels are below 1998 levels. Inflation-adjusted total city revenues decreased 3 percent between 1998 and 2007, while total city expenditures, when adjusted for inflation, decreased 4 percent through the same period (pg. 7).

- Between 1998 and 2007, actual revenues derived from property taxes grew 98 percent, compared to 14 percent for revenues derived from intergovernmental sources. When revenues are adjusted for inflation, the ten-year period shows a 37 percent increase in property tax revenues, while intergovernmental revenues decreased 21 percent. When put into constant dollars, the level of revenues in 2007 was less than in 1998 (pg. 7).

- As federal and state governments have reduced the amount of aid to cities, the result has been a greater reliance on revenues derived from property taxes. The proportion of total revenues derived from property taxes grew from 23 percent in 1998 to 32 percent in 2007. During this same time frame, revenues derived from intergovernmental sources decreased from 33 percent of total revenues to 26 percent (pg. 7).

Governmental Expenditures

- Total city expenditures grew from \$3.83 billion in 1998 to \$5.32 billion in 2007. This represents an increase of 39 percent. When adjusted for inflation, total expenditures decreased 4 percent (pg. 9).

- When the three components of city spending (total current expenditures, total capital outlays, and total debt service) are looked at individually, only total current expenditures showed growth when adjusted for inflation. Over the ten-year period, when adjusted for inflation, total current expenditures grew 10 percent, while total capital outlays decreased 16 percent, and total debt service decreased 21 percent (pg. 10).

[4]"Adjusted for inflation" and "constant dollars" refer to data adjusted for inflation using the Implicit Price Deflator for State and Local Governments setting 1998 as the base year (N.I.P.A. Table 1.1.9, December 2008).

Comparison and Overview

2007 Finances for All Minnesota Cities

Revenues

Total revenues of the governmental funds for all Minnesota cities amounted to $4.69 billion in 2007. This represents an increase of 4.7 percent over 2006 revenues. Total revenues of cities over 2,500 in population increased 4.9 percent, while revenues of cities under 2,500 in population increased 3.1 percent.

There are two central differences between cities over and under 2,500 in population as to how they fund services. Cities under 2,500 in population (small cities) are much more dependent on intergovernmental revenues than cities over 2,500 (large cities). In 2007, intergovernmental revenues accounted for 40 percent of total revenues for small cities, compared to 25 percent for large cities. Among all cities, intergovernmental revenues accounted for 26 percent of total revenues.

The second difference is the reliance on tax revenues. Because large cities receive a much smaller portion of their revenues from intergovernmental sources, they more commonly utilize tax revenue streams such as tax increments, franchise, lodging, and local sales taxes. As a whole, tax revenue from all sources accounted for 45 percent of large city revenues, compared to 31 percent of small city revenues in 2007. Large cities also utilize tax increment financing to a greater extent than small cities. Revenue derived from tax increment accounted for 3 percent of small city total revenues, compared to 7 percent for large cities.

Property taxes account for a similar share of total revenues for these two groups of cities. For large cities, property taxes accounted for 33 percent of total revenues, compared to 28 percent for small cities. For all cities, property taxes accounted for 32 percent of total revenues.

On a per capita basis, large cities had total revenues of $1,109, while small cities had total revenues of $1,059.

Expenditures

Total expenditures of the governmental funds for all cities totaled $5.32 billion in 2007. This represents a decrease of 0.7 percent from 2006. Total expenditures of cities over 2,500 in population decreased 0.4 percent, while total expenditures for cities under 2,500 decreased 3.1 percent.

The spending priorities of cities under 2,500 in population differ from those cities over 2,500 in population. For example, small cities tend to direct a greater percentage of their resources to general government (16 percent) and less to culture and recreation (8 percent) than cities over 2,500 (9 percent and 13 percent, respectively). The largest expenditure categories for both groups of cities are streets and highways and public safety. For large cities, streets and highways accounted for 23 percent of total expenditures, and public safety accounted for 24 percent. For small cities, streets and highways accounted for 26 percent of total expenditures, and public safety accounted for 20 percent.

Long-Term Debt

Another area where small and large cities (under and over 2,500 in population) differ is in their use of debt. Overall, small cities tend to carry a greater debt burden than large cities. In 2007, small cities carried long-term debt of $1.20 billion, or $2,927 per capita, compared to $8.26 billion, or $2,152 per capita, for large cities. While there is no single reason for the higher level of indebtedness per capita among the smaller cities, a primary reason is that the high costs of projects such as wastewater treatment facilities and water and sewer line replacement are spread across fewer people.

Unreserved Fund Balances of the General and Special Revenue Funds

A clear difference between the two city types is in the level of unreserved fund balances. Small cities maintain significantly higher fund balances than large cities. In 2007, unreserved fund balances as a percent of current expenditures averaged 98 percent for small cities, compared to 48 percent for large cities. The percentage for small cities is up from 93 percent in 2006, but the percentage is down from 50 percent for large cities in 2006.

Among the 281 small cities that reported on a GAAP basis in 2007, 142 (51 percent) had an unreserved fund balance greater than 100 percent of total current expenditures. Among the 210 large cities, 40 cities (19 percent) had an unreserved fund balance greater than 100 percent of total current expenditures.[5] In 2007, unreserved fund balances as a percent of total current expenditures among small cities ranged from -117 percent in Bigelow to 766 percent in Buffalo Lake. Among large cities, the range was from -16 percent in Rogers to 240 percent in Bayport.

The Office of the State Auditor recommends that at year-end, local governments maintain an unreserved fund balance in their General Fund and Special Revenue Funds of approximately 35 to 50 percent of operating revenues, or no less than five months of operating expenditures. If the local government's unreserved fund balance is less than or greater than this recommendation, the local government should be able to explain the reason for the difference.

[5] There are 212 large cities. The cities of Alexandria and New Hope are not included in this figure because they did not comply with the reporting requirements.

Ten-Year Trends

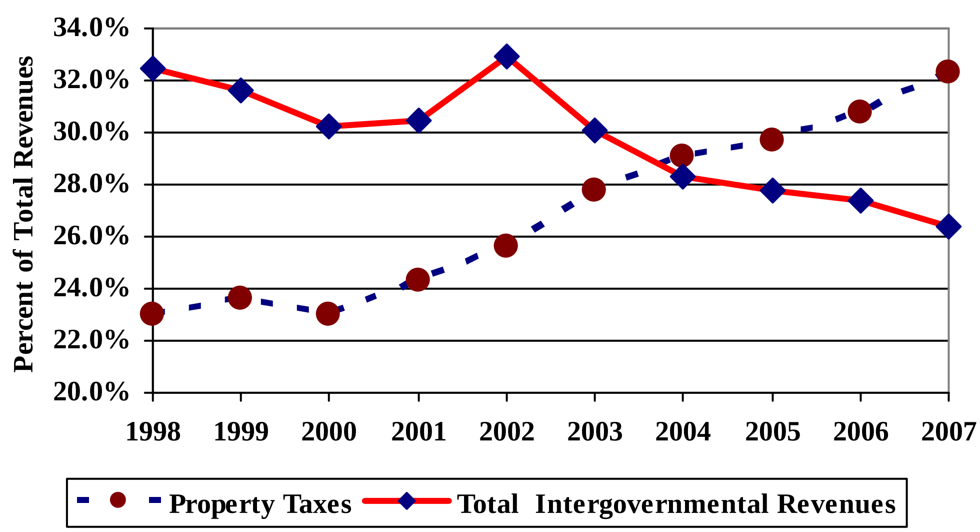
Governmental Revenues

While cities appear to have ended 2007 in good financial condition with revenues growing 5 percent and expenditures decreasing 1 percent, an examination of city finances between 1998 and 2007 reveals a noteworthy trend. In particular, when adjusted for inflation[6], 2007 revenue and expenditure levels are below 1998 levels. Inflation-adjusted total city revenues decreased 3 percent between 1998 and 2007, while total city expenditures, when adjusted for inflation, decreased 4 percent through the same period.

Between 1998 and 2007, actual revenues derived from property taxes grew 98 percent, compared to 14 percent for revenues derived from intergovernmental sources. When revenues are adjusted for inflation, the ten-year period shows a 37 percent increase in property tax revenues, while intergovernmental revenues decreased 21 percent.

In addition, the proportion of total revenues derived from property taxes grew from 23 percent in 1998 to 32 percent in 2007. During this same time frame, revenues derived from intergovernmental sources decreased from 33 percent of total revenues to 26 percent. Figure 1 below shows that as Federal and State governments have reduced the amount of aid to cities, the result has been a greater reliance on revenues derived from property taxes.

Figure 1: Primary Sources of City Revenues as a Percent of Total Revenues - 1998 to 2007



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[6]"Adjusted for inflation" and "constant dollars" refer to data adjusted for inflation using the Implicit Price Deflator for State and Local Governments setting 1998 as the base year (N.I.P.A. Table 1.1.9, December 2008).

An examination of city revenues from 1998 to 2007 shows that in actual dollars, revenues grew from $3.34 billion in 1998 to $4.69 billion in 2007, an increase of 41 percent. Between 2002 and 2003, there was an actual decrease in city revenues. When put into constant dollars, the level of revenues in 2007 was less than in 1998. Figure 2 below illustrates this trend.

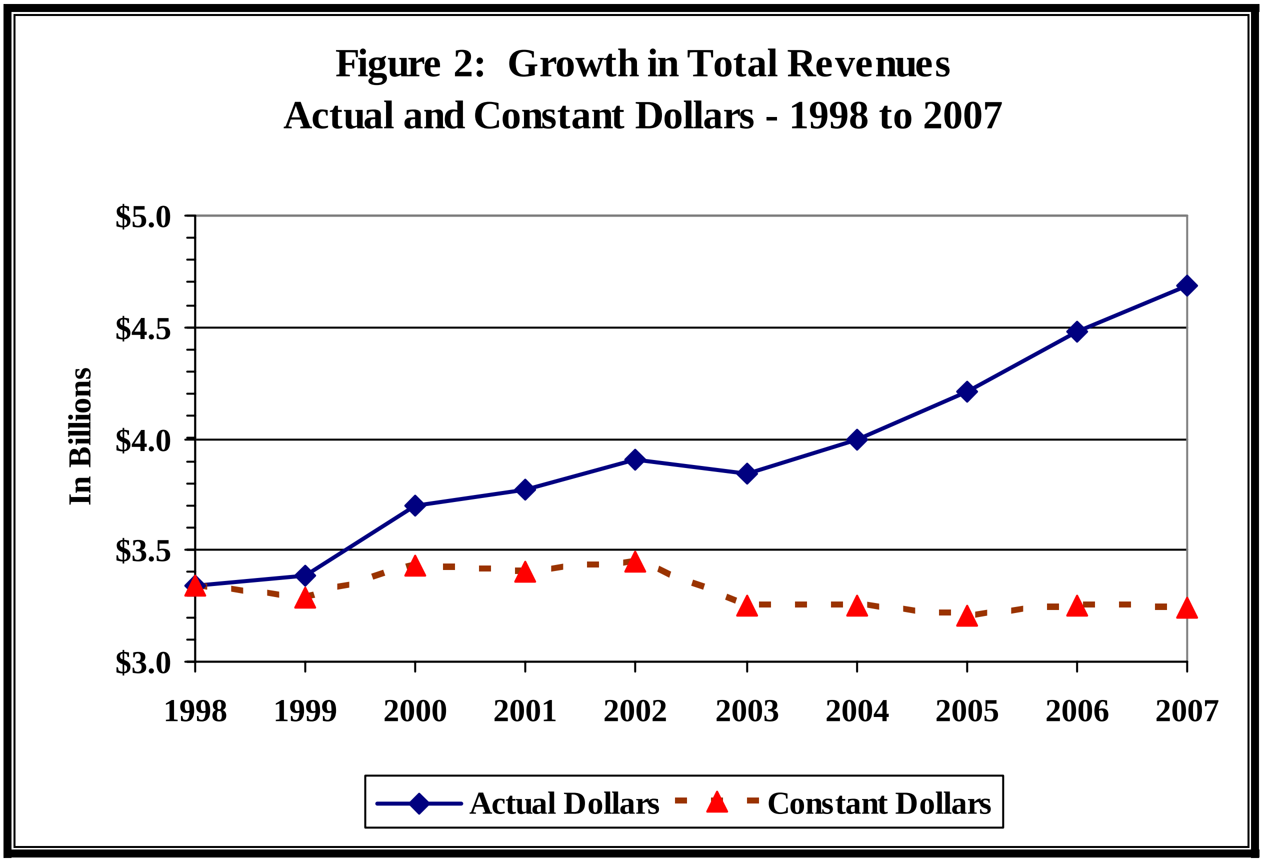


Table 1 on the following page provides a summary of the trend in city revenues from 1998 to 2007 when adjusted for inflation. During the five-year period of 2003 to 2007, there was a significant slowdown in the growth of revenues as compared to the 1998 to 2001 period. This was in part due to the State's fiscal crises in 2002 and 2003 when budget cuts were made in state aid to cities. While property taxes and other sources of revenues were increased to counter the cuts, revenues did not grow at a rate to keep up with inflation.

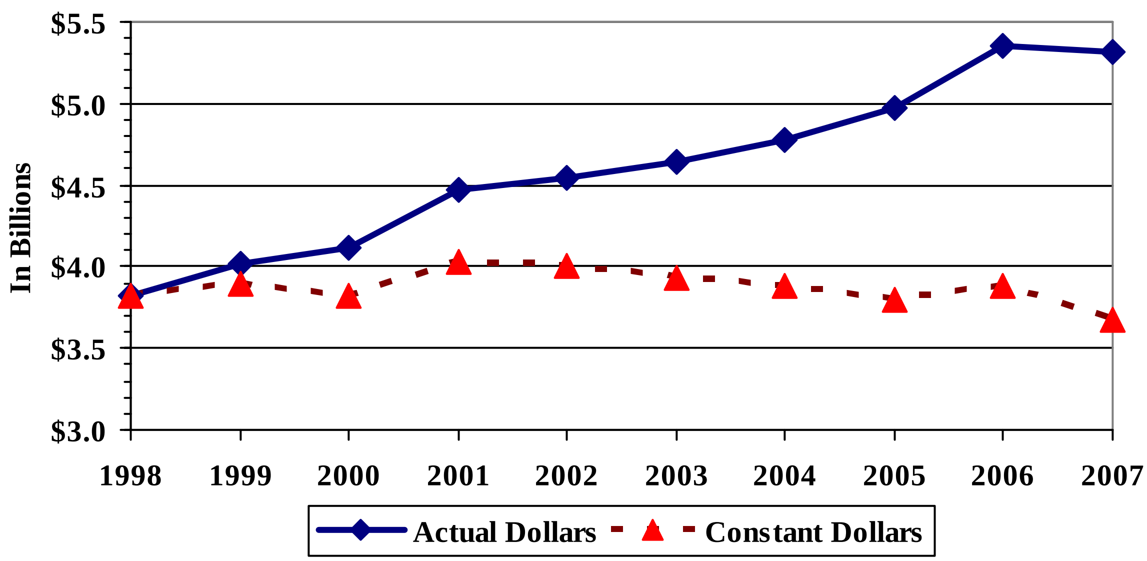
Table 1: Total City Revenues in Constant Dollars

Revenues	1998	2002	2003	2007	1998 - 02 5-Year Change	2003 - 07 5-Year Change	10-Year Change
Taxes	$1,183,172,698	$1,234,719,267	$1,271,418,185	$1,400,023,262	4.4%	10.1%	18.3%
Special Assessments	239,042,593	223,777,051	236,865,411	200,967,718	-6.4%	-15.2%	-15.9%
Licenses and Permits	105,800,897	123,420,983	127,343,965	104,237,803	16.7%	-18.1%	-1.5%
Federal Grants	178,114,460	121,058,795	146,224,273	130,952,598	-32.0%	-10.4%	-26.5%
State Grants	861,370,819	951,810,657	774,259,469	660,702,975	10.5%	-14.7%	-23.3%
Local Unit Grants	44,191,720	60,340,676	58,400,276	61,332,140	36.5%	5.0%	38.8%
Charges for Services	260,100,255	324,781,273	325,318,570	308,939,452	24.9%	-5.0%	18.8%
Fines and Forfeits	31,398,546	32,806,380	33,971,386	30,065,347	4.5%	-11.5%	-4.2%
Interest Earnings	204,201,542	135,875,058	76,546,108	170,297,064	-33.5%	122.5%	-16.6%
All Other Revenues	229,605,353	236,687,200	203,389,416	168,597,093	3.1%	-17.1%	-26.6%
Total Revenues	**$3,336,998,883**	**$3,445,277,340**	**$3,253,737,057**	**$3,236,115,452**	**3.2%**	**-0.5%**	**-3.0%**

Governmental Expenditures

Total city expenditures grew from $3.83 billion in 1998 to $5.32 billion in 2007. This represents an increase of 39 percent. When adjusted for inflation, total expenditures decreased 4 percent. Figure 3 below shows the contrast between expenditures in actual and constant dollars.

Figure 3: Growth in Total Expenditures
Actual and Constant Dollars - 1998 to 2007



When the three components of city spending (total current expenditures, total capital outlays, and total debt service) are looked at individually, only total current expenditures showed growth when adjusted for inflation. Over the ten-year period, when adjusted for inflation, total current expenditures grew 10 percent, while total capital outlays decreased 16 percent, and total debt service decreased 21 percent.

Table 2 below provides a summary of expenditures from 1998 to 2007 in constant dollars. Those categories showing the greatest growth were streets and highways (13 percent), airports (12 percent), and public safety (11 percent), while those showing the greatest decreases were conservation of natural resources (-56 percent), health (-45 percent), and all other expenditures (-29 percent).

Table 2: Total City Expenditures in Constant Dollars

Expenditures	1998	2002	2003	2007	1998 - 02 5-Year Change	2003 - 07 5-Year Change	10-Year Change
General Government	$358,696,030	$403,747,142	$429,842,649	$358,929,730	12.6%	-16.5%	0.1%
Public Safety	782,872,349	852,272,744	856,242,178	870,657,091	8.9%	1.7%	11.2%
Streets and Highways	764,228,757	831,593,261	840,897,066	860,641,130	8.8%	2.3%	12.6%
Sanitation	16,996,711	16,990,809	14,928,260	16,044,314	0.0%	7.5%	-5.6%
Health	31,299,365	33,050,671	28,558,243	17,350,375	5.6%	-39.2%	-44.6%
Culture and Recreation	435,082,991	474,608,456	446,693,731	449,768,612	9.1%	0.7%	3.4%
Housing/Economic Development	435,547,494	400,728,622	363,716,093	317,014,177	-8.0%	-12.8%	-27.2%
Conservation of Natural Resources	5,380,017	2,562,317	3,278,114	2,396,616	-52.4%	-26.9%	-55.5%
Airport	24,951,684	25,423,054	31,307,032	28,050,724	1.9%	-10.4%	12.4%
All Other Expenditures	224,990,268	216,382,892	214,570,900	159,512,604	-3.8%	-25.7%	-29.1%
Debt Service	746,373,125	751,371,333	699,186,677	588,538,619	0.7%	-15.8%	-21.1%
Total Expenditures	**$3,826,418,791**	**$4,008,731,301**	**$3,929,220,943**	**$3,668,903,991**	**4.8%**	**-6.6%**	**-4.1%**
Total Current Expenditures	$1,921,489,583	$2,125,400,989	$2,114,684,495	$2,106,144,426	10.6%	-0.4%	9.6%
Total Capital Outlay	1,158,556,083	1,131,958,979	1,115,349,770	974,220,947	-2.3%	-12.7%	-15.9%
Total Debt Service	746,373,125	751,371,333	699,186,677	588,538,619	0.7%	-15.8%	-21.1%
Total Expenditures	**$3,826,418,791**	**$4,008,731,301**	**$3,929,220,943**	**$3,668,903,991**	**4.8%**	**-6.6%**	**-4.1%**

Overview of Cities Over 2,500 in Population

Total Governmental Revenues

In 2007, cities over 2,500 in population, or large cities, had total governmental revenues of $4.26 billion. This represents an increase of 4.9 percent from the amount raised in 2006 to finance city services. The primary funding sources for cities were taxes and state aid. These two sources accounted for 64 percent of all city revenues.

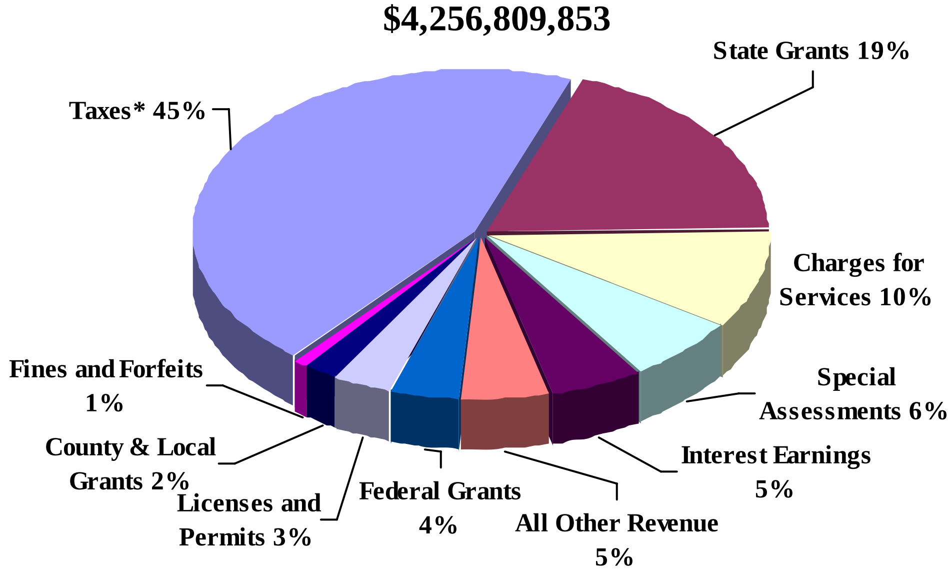
The sources of revenue that grew at the greatest rate between 2006 and 2007 were: local unit grants (35 percent), interest earnings (30 percent), tax increments (17 percent), and fines and forfeits (11 percent). Those sources of revenue showing the greatest decreases were: franchise taxes (-25 percent), gravel and gambling taxes (-19 percent), and licenses and permits (-10 percent).

The shares of total governmental revenues generally change very little from year to year. The two categories that have shown change are property taxes and intergovernmental revenues. Over the past five years, property taxes as a percent of total revenues increased from 28 percent in 2003 to 33 percent in 2007 and intergovernmental revenues, which decreased from 29 percent in 2003 to 25 percent in 2007. To examine five-year trends in revenues, see Table 8 on page 28.

Figure 4 shows the relative shares of total governmental revenues by source. Underlying data for this figure is detailed in Table 8 on page 28.

Figure 4: 2007 Total Governmental Revenues - Cities Over 2,500 in Population

$4,256,809,853



* This category includes property, hotel/motel, sales, franchise, gravel, and gambling taxes, as well as tax increments.

Total Governmental Expenditures

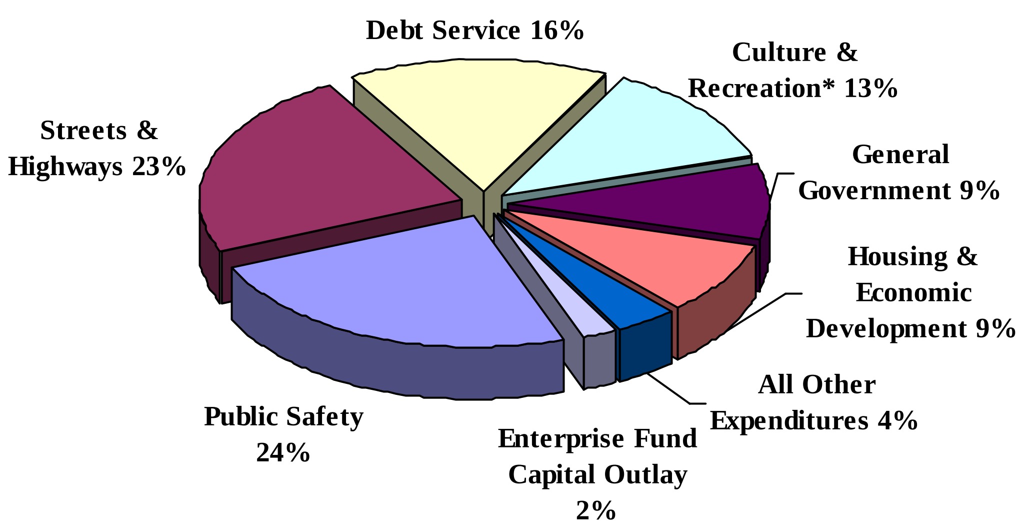
Cities provide a variety of services. Most expenditures related to these services are accounted for in governmental funds. The governmental funds are classified as the General, Special Revenue, Capital Projects, Permanent, and Debt Service Funds. In 2007, cities over 2,500 in population expended $4.78 billion from these various governmental funds to provide city services. This represents a decrease of 0.4 percent from 2006 total governmental expenditures. Total governmental expenditures include current expenditures, capital outlays, and debt service. Current expenditures accounted for 58 percent of total government expenditures, while capital outlay accounted for 26 percent, and debt service accounted for 16 percent.

The largest category of current expenditures for cities over 2,500 in population was public safety, while streets and highways was the largest capital outlays expenditure. Public safety accounted for 39 percent of all current expenditures--more than double that of any other category. Streets and highways accounted for 58 percent of all capital expenditures, over five times greater than any other category of capital outlay.

Two areas showed very large changes in 2007. Capital outlays related to general government decreased by 47 percent, resulting from the completion of large capital projects in the cities of Prior Lake (city hall) and Ramsey (parking ramp and municipal building).

Figure 5 shows the relative shares of total governmental expenditures by function. The underlying data for this figure is detailed in Table 9 on page 29.

Figure 5: 2007 Total Governmental Expenditures - Cities Over 2,500 in Population $4,795,881,669



* This category represents expenditures for libraries and parks and recreation.

Capital Outlay Expenditures

Cities over 2,500 in population expended $1.26 billion on capital investments in 2007. This represents a decrease of 11.3 percent from the level expended in 2006. While no one particular city was responsible for the decrease, the ten cities with the largest decreases in capital outlays accounted for 70 percent of the total decrease. Capital outlays are more likely than current expenditures to vary significantly from one year to the next. The reason for this is that capital projects tend to be large in size, but the associated costs are short-term. Table 3 below shows total capital outlays in actual dollars and per capita for large cities.

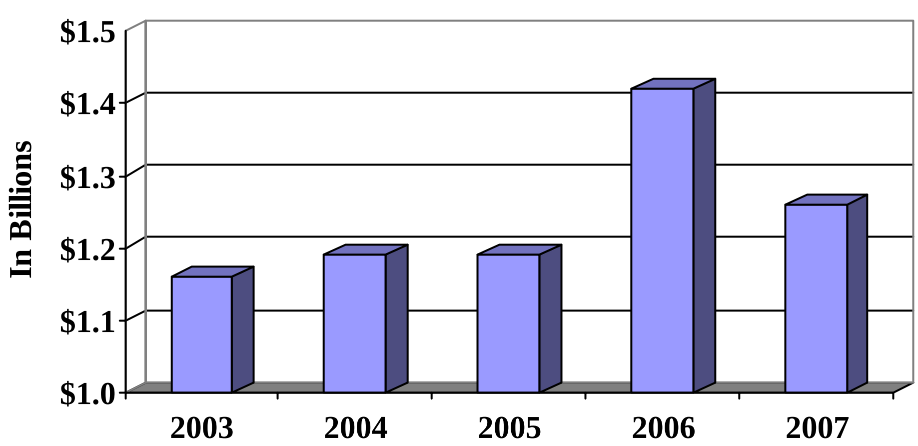
Table 3: Total Capital Outlay Expenditures in Actual Dollars and Per Capita

Year	Total Capital Outlay (actual dollars)	Per Capita*
2003	$1,163,674,824	$315
2004	$1,198,430,759	$320
2005	$1,194,717,585	$315
2006	$1,418,495,255	$371
2007	$1,258,328,908	$328

* Per capita amounts are based on the total population of cities with over 2,500 in population that reported their financial information.

Figure 6 illustrates the trend in capital spending for the years 2003 through 2007.

Figure 6: Capital Outlay Expenditures
Cities Over 2,500 in Population - 2003 to 2007

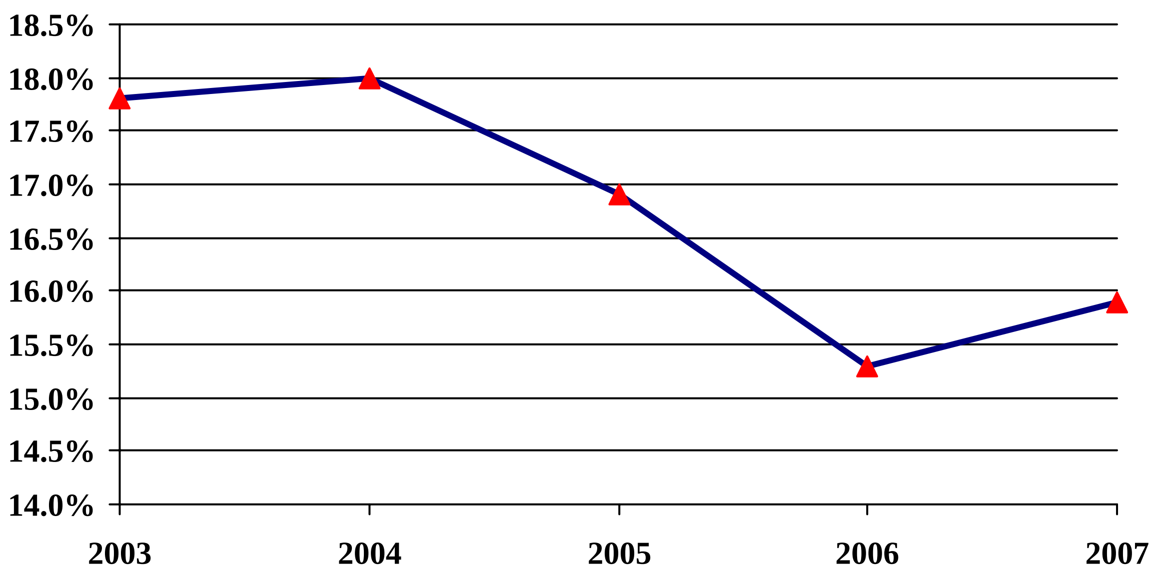


Debt Service

In 2007, large cities expended a total of $764.4 million on debt service, which represented 16 percent of total expenditures. Debt service includes expenditures for the principal and interest payments of debt incurred by cities. Between 2006 and 2007, large city debt service expenditures increased $26.1 million, or 4 percent. The increase is primarily attributable to the City of St. Paul, which increased debt service expenditures by $33.7 million, or 54 percent.

Figure 7 below shows the trend in the percentage of total expenditures allocated to debt service.

Figure 7: Debt Service as a Percentage of Total Expenditures - Cities Over 2,500 in Population

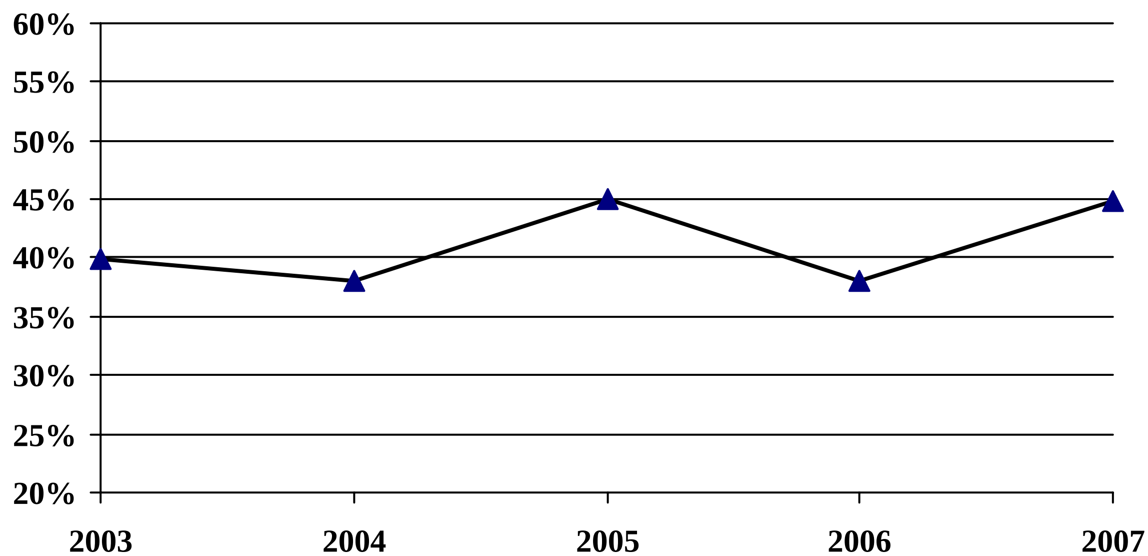


Municipal Enterprises

In addition to governmental funds, many cities establish enterprise funds to account for services that are financed and operated in a manner similar to private business enterprises. These enterprises generally are intended to be self-sustaining through fees and user charges. Although some enterprises may earn a net profit, most have the objective of breaking even. However, some municipalities choose to subsidize an enterprise that benefits the community as a whole. Enterprise fund accounting is also used to provide more detailed financial information on operations where there are public policy, accountability, management control, and other concerns. The most common enterprises created by large cities are for recreation, sewer, and water activities.[7]

In aggregate, large city municipal enterprises reported a net income of $269.8 million and net transfers (transfers out minus transfers in) of $121.1 million in 2007. This represents a decrease of 10 percent in net income and a 6 percent increase in net transfers. An example of this type of transfer is when city officials transfer excess reserves from the Water Utility Enterprise Fund to the General Fund. Overall, net transfers were 45 percent of net profits among large city enterprises. Figure 8 examines the five-year trend for large cities in net transfers from enterprise funds as a percent of their net income.

Figure 8: Large City Enterprise Fund Net Transfers as a Percent of Net Income - 2003 to 2007



[7] The Office of the State Auditor issues a separate report for municipal liquor stores entitled, “Analysis of Municipal Liquor Store Operations.” The most recent report was issued in April 2008.

Outstanding Long-Term Indebtedness

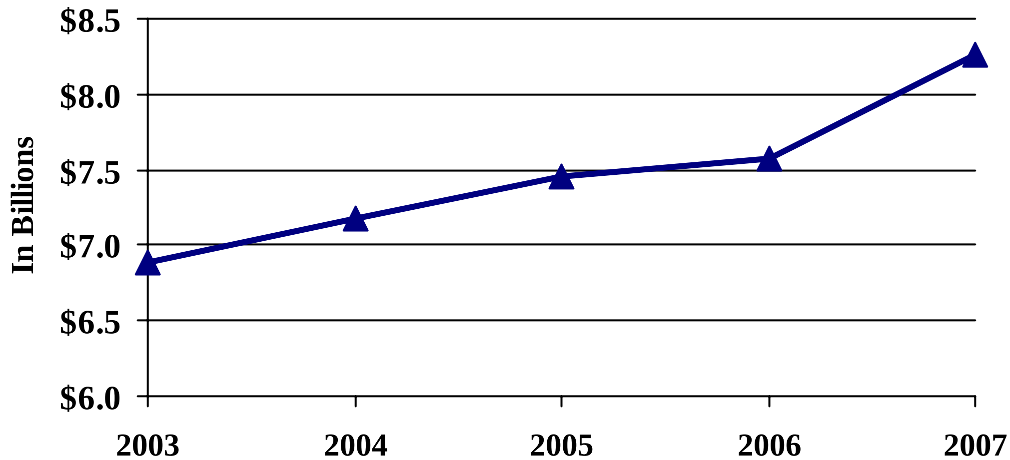
Cities over 2,500 carried long-term debt of $8.26 billion, or $2,152 per capita, at the end of 2007. This represents an increase of 9 percent over the 2006 level. Cities incur long-term debt through various ways such as the issuance of bonds and notes, certificates of indebtedness, and tax anticipation certificates. Long-term lease agreements are also classified as long-term debt. Cities may only borrow to finance capital projects and purchases but are restricted by law from borrowing for current expenses. The amount of outstanding debt affects a city's current expenditures because cities must make principal and interest payments to service the debt. Table 4 below shows the outstanding bonded indebtedness for 2006 and 2007.

Table 4: Two-Year Summary of Outstanding Bonded Indebtedness

	2006 Amount	2007 Amount
General Obligation	$1,115,964,338	$1,106,265,767
G.O. Tax Increment	724,234,565	769,892,452
Revenue Tax Increment	182,174,411	182,826,742
Special Assessment	1,755,289,709	1,938,205,505
G.O. Revenue	1,946,839,231	2,057,732,032
Revenue	1,022,403,209	1,262,683,092
All Other	54,033,410	79,620,745
Total Bonded Indebtedness	**$6,800,938,873**	**$7,397,226,335**

Figure 9 shows the five-year trend of outstanding long-term debt for cities over 2,500 in population.

Figure 9: Outstanding Long-Term Indebtedness* for Cities Over 2,500 in Population



*Includes bonds and other types of debt such as certificates of indebtedness, long-term leases, and notes.

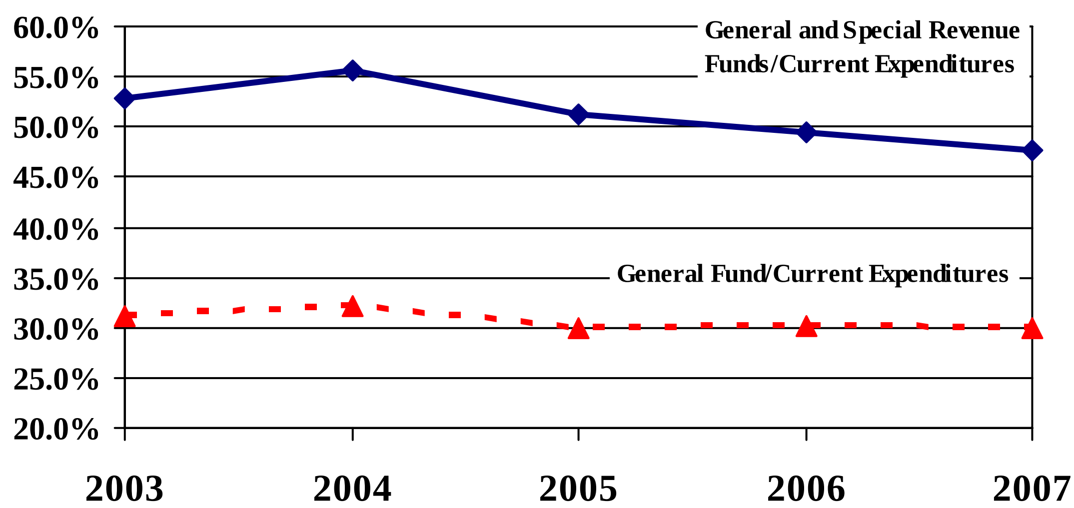
Unreserved Fund Balances of the General and Special Revenue Funds

The unreserved fund balances of large cities' General and Special Revenue Funds totaled $1.32 billion in 2007. This represents an increase of 0.4 percent over the level reported in 2006. Cities should have relatively large fund balances at the end of the year (December 31) because they must rely on them to meet expenditures during the first five months of the next fiscal year, until they receive the first property tax and state aid payments. Appendix A on page 315 provides an in-depth discussion of city fund balances.

Comparing cities' unreserved fund balances to their total current expenditures helps put the fund balances into perspective and provides insight on the relative financial health of Minnesota's cities. Large city unreserved fund balances as a percent of total current expenditures averaged 48 percent in 2007, compared to 50 percent in 2006. The decrease in the ratio of unreserved fund balances to total current expenditures reflects flat growth in fund balances combined with stronger growth in current expenditures. If cities in this category are divided into their class number, it is interesting to note that as population decreases, the average increases. Class 1 (first class) cities average 27 percent of their unreserved fund balances as a percent of total current expenditures, while class 4 cities (populations 2,500 to 10,000) average 74 percent.

Figure 10 below shows the five-year trend of the unreserved fund balances as a percent of total current expenditures for large cities. One line shows the combined unreserved fund balance of the General and Special Revenue Funds, and the other shows only the unreserved fund balance of the General Fund.

Figure 10: Unreserved Fund Balances of the General and Special Revenue Funds as a Percent of Total Current Expenditures for Cities Over 2,500 in Population



Overview of Cities Under 2,500 in Population

Total Governmental Revenues

In 2007, cities under 2,500 in population, or small cities, had total governmental revenues of $432.6 million to finance city services. This represents an increase of 3 percent over the amount raised in 2006.

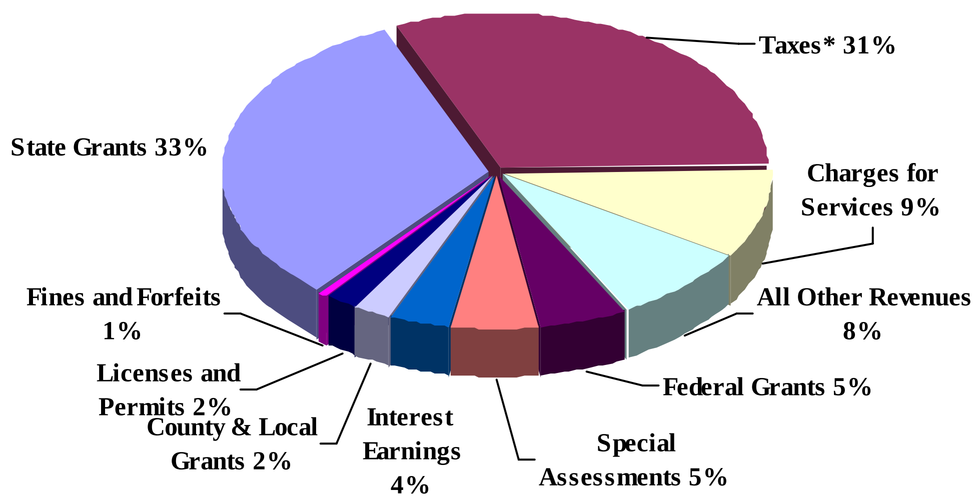
The sources of revenue that grew at the fastest rate between 2006 and 2007 were: local unit grants (77 percent), interest earnings (17 percent), county grants (9 percent) and taxes (6 percent). County and local unit grants are generally contributions from local government partners in large capital projects. The categories showing the greatest decrease between 2006 and 2007 were: licenses and permits (-16 percent), federal grants (-8 percent), and all other revenues (-5 percent).

The main sources of revenues for small cities in 2007 were state grants and taxes, which together accounted for 64 percent of all revenues, up from 63 percent in 2006. Both taxes and state grants increased at a rate greater than overall revenues, which resulted in their share of total revenues increasing relative to other revenue sources.

Figure 11 shows the relative shares of total governmental revenues by source. The underlying data for this figure is in Table 12 on page 33.

Figure 11: 2007 Total Governmental Revenues - Cities Under 2,500 in Population

$432,606,215



* This category includes property, hotel/motel, sales, franchise, gravel, and gambling taxes, as well as tax increments.

Total Governmental Expenditures

Most city services are accounted for in governmental funds. The governmental funds are made up of the General, Special Revenue, Capital Projects, Permanent, and Debt Service Funds. In 2007, cities under 2,500 in population expended $520.7 million from governmental funds to provide city services. This represents a decrease of 3 percent from 2006 total governmental expenditures.

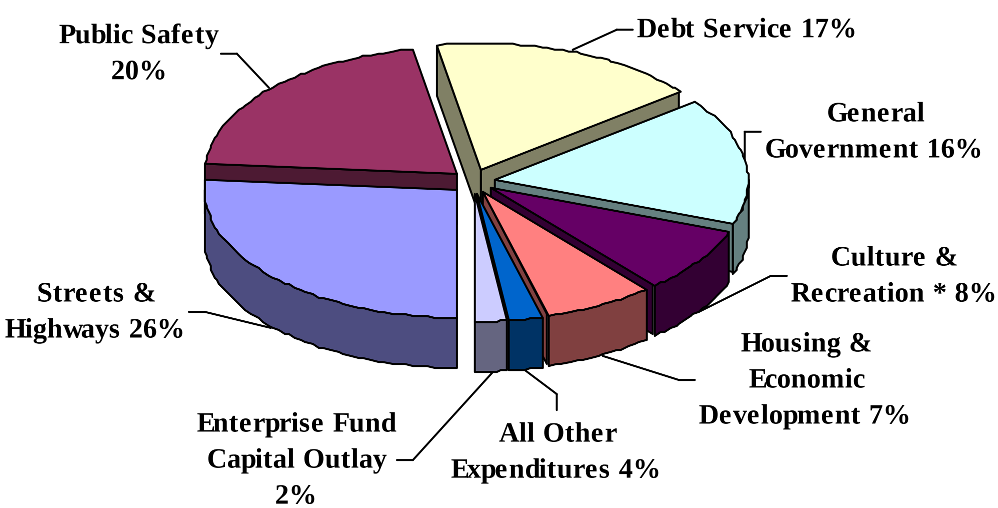
Between 2006 and 2007, the categories of expenditures that grew at the fastest rate were: debt service (12 percent), libraries (10 percent), and streets and highways (4 percent). The categories showing the greatest decreases were: sanitation (-69 percent), capital outlay for enterprise funds (-60 percent), health (-49 percent), and all other expenditures (-20 percent).

In 2007, the four largest expenditure categories for cities under 2,500 in population were streets and highways, public safety, debt service, and general government. These four categories together accounted for 79 percent of all expenditures in 2007.

Figure 12 shows the relative shares of total governmental expenditures of small cities by function. The underlying data for this figure is in Table 12 on page 33.

Figure 12: 2007 Total Governmental Expenditures - Cities Under 2,500 in Population

$520,683,078



* This category represents expenditures for libraries and parks and recreation.

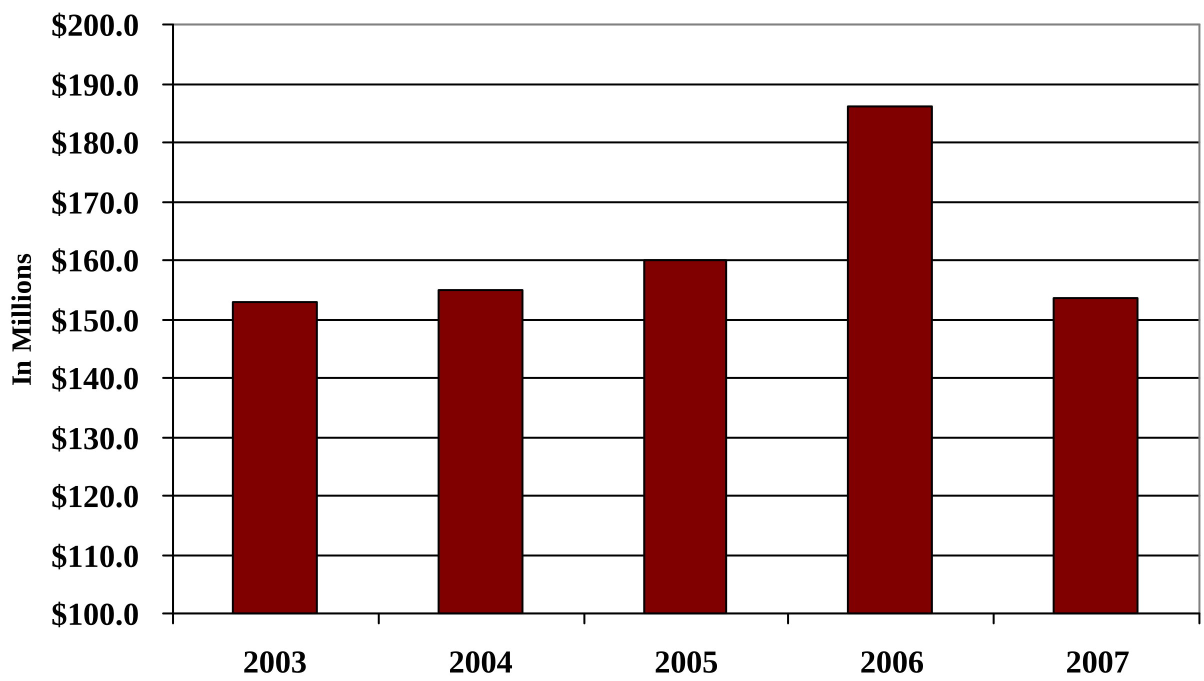
Capital Outlay Expenditures

Capital outlay expenditures account for the purchase, construction, or permanent improvements of buildings, equipment, machinery, and land. Small cities expended $153.4 million on capital outlay in 2007. This represents a decrease of 18 percent from the level expended in 2006.

Capital outlays are more likely than current expenditures to vary significantly from one year to the next. The reason for this is that capital projects tend to be large in size, but the associated costs are short-term. Some of the factors that influence the level of capital investments include: demands for public meeting places and facilities; the need to replace aging infrastructure; public safety concerns; infrastructure improvements for new developments; and damage to public facilities caused by fire, floods, and storms.

Figure 13 illustrates the trend in capital outlays of small cities for the years 2003 through 2007.

Figure 13: Total Capital Outlay Expenditures
Cities Under 2,500 in Population

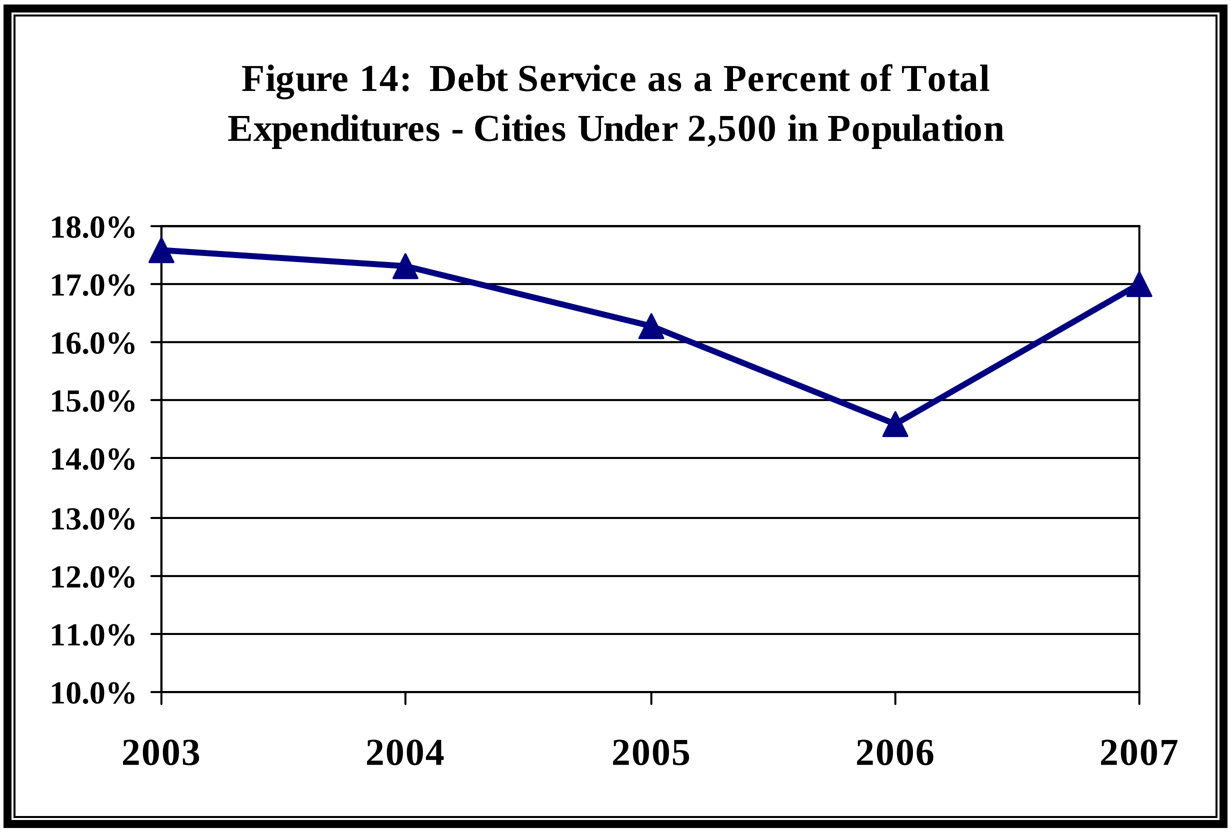


Debt Service

Debt service includes expenditures for the principal and interest payments on debt incurred by cities. In 2007, small cities expended a total of $88.5 million on debt service. This represented an increase of 12 percent from 2006. Overall, debt service expenditures accounted for 17 percent of total expenditures for small cities.

Debt service expenditures as a percent of total expenditures declined yearly between 2003 and 2006 but increased in 2007. The percentage increased because debt service expenditures increased, while total expenditures decreased.

Figure 14 shows the five-year trend in the percent of total expenditures allocated to debt service.



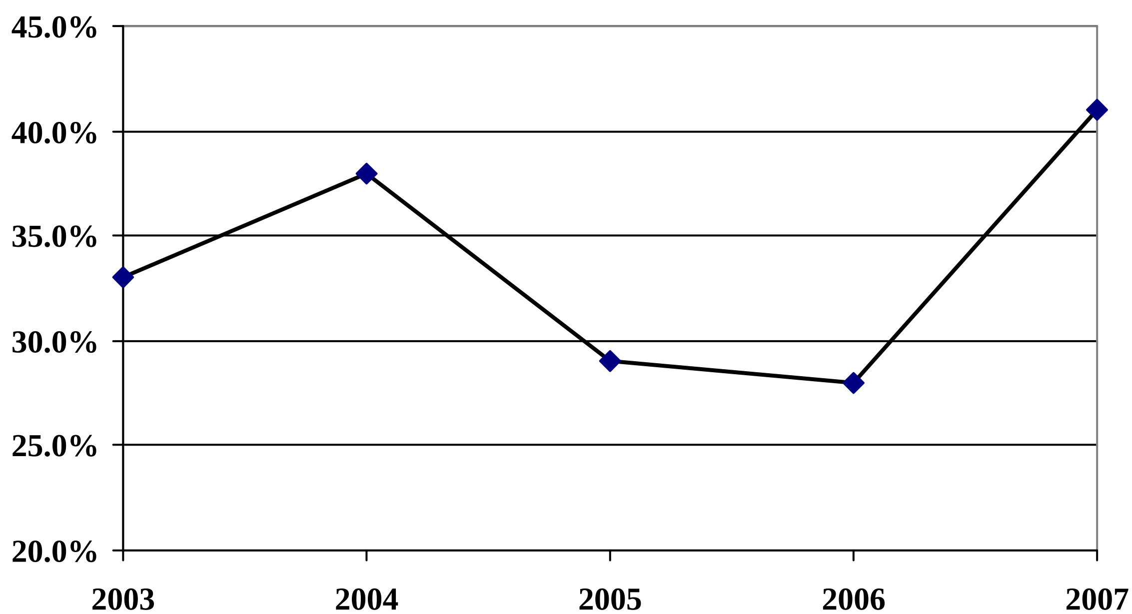
Municipal Enterprises

The total net income of small city enterprises in 2007 was $46.4 million and the net amount transferred to other funds was $19.1 million. This represents an increase in net income of 6 percent and an increase in net transfers (transfers out minus transfers in) of 59 percent between 2006 and 2007.

In 2007, the municipal enterprises of small cities transferred 41 percent of their net income to other funds. This was significantly more than the 28 percent transferred in 2006. Transfers in 2007 were affected by the sale of two nursing home facilities in the cities of Gaylord and Lakefield. The proceeds from these sales were transferred to other funds. In addition, because the growth in net income was smaller than the growth in net transfers, there was an increase in net transfers as a percent of net income.

Figure 15 examines the five-year trend in net transfers from enterprise funds as a percent of net income.

Figure 15: Small City Enterprise Fund Net Transfers as a Percent of Net Income - 2003 to 2007



Outstanding Long-Term Indebtedness

Cities under 2,500 carried long-term debt totaling $1.20 billion at the close of 2007. This represents an 8 percent increase over the level in 2006. On a per capita basis, small cities carried $2,927 in long-term debt, compared to $2,152 for large cities. While there is no single reason for the higher level of indebtedness per capita among the smaller cities, a primary reason is that the high costs of projects, such as water and sewer line replacement, are spread across fewer people.

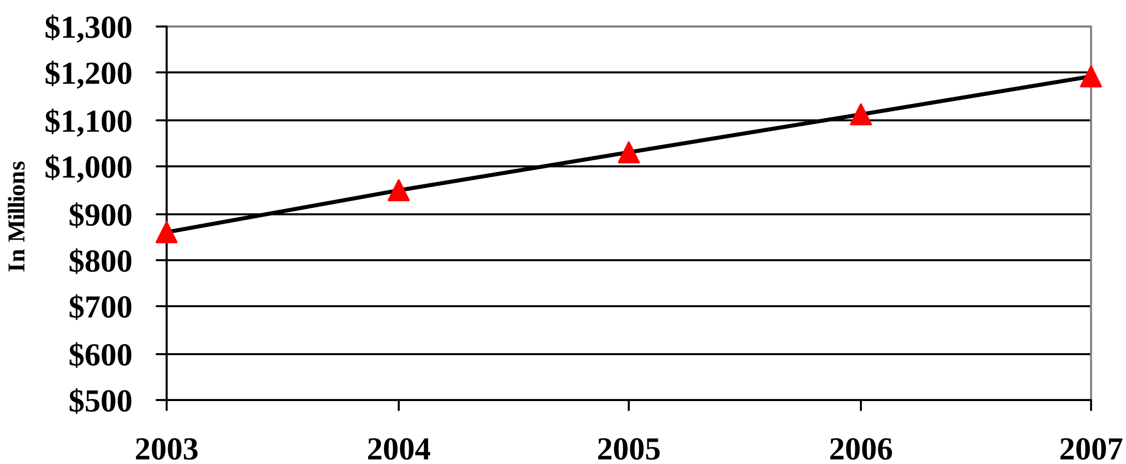
Table 5 looks at outstanding bonded indebtedness for 2006 and 2007.

Table 5: Two-Year Summary of Outstanding Bonded Indebtedness

	2006 Amount	2007 Amount
General Obligation	$114,507,702	$106,894,839
G.O. Tax Increment	34,715,071	34,415,730
Revenue Tax Increment	761,034	820,986
Special Assessment	295,385,856	317,667,102
G.O. Revenue	323,912,684	348,249,691
Revenue	97,709,231	95,086,016
All Other	1,622,287	1,897,209
Total Bonded Indebtedness	**$868,613,865**	**$905,031,573**

Figure 16 shows the five-year trend of outstanding long-term debt for small cities.

Figure 16: 2007 Outstanding Long-Term Indebtedness - Cities Under 2,500 in Population*



* Includes bonds and other types of debt such as certificates of indebtedness, long-term leases, and notes.