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 the 851 Minnesota cities that provided their financial information to the Office of the State Auditor for calendar year 2012.[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.

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 (large cities). The third section provides a detailed overview of the financial operations of cities under 2,500 in population (small cities).[2]

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.[3] 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, 2012, 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 2011 and 2012 unrestricted fund balances in the General and Special Revenue Funds of all cities reporting on a modified accrual basis. Table 19 details the actual unrestricted fund balances and a comparison to 2012 total current expenditures, by city. Table 20 presents the fund balance data sorted by unrestricted fund balance as a percent of total current expenditures.

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[1]The report only provides information on 851 of the cities because 2 cities (Bluffton and Harding) failed to comply with the reporting requirements of Minn. Stat. §§ 6.74-.75 and §§ 471.697-.698. Failure to comply with these reporting requirements results in the Office of the State Auditor not certifying a city as eligible to receive Local Government Aid (LGA). The City of Tenney dissolved and merged with Campbell Township at the end of 2011 resulting in one fewer city in this report than the previous year.

[2]City classifications are designated based on the decennial census. This report uses the class designations based on the 2010 census population figures. Cities over 2,500 in population are designated as first, second, third, and fourth class based on their population. All cities under 2,500 in population are designated as fifth class cities.

[3]Due to rounding, percentages shown for totals may not equal the sum of the individual percentages.

Starting in fiscal year 2011, cities using a modified accrual basis of accounting and reporting on a generally accepted accounting principles (GAAP) basis were required to implement the Governmental Accounting Standards Board's (GASB) Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*. GASB Statement 54 defines the classifications of fund balance based on the focus of the constraints placed on the use of current fund balance. The Statement also identifies the governmental fund type definitions.[4]

Under GASB Statement 54, cities using a modified accrual basis of accounting report separate fund balances for all of their governmental funds and denote the amounts that fall under the following classifications: *nonspendable, restricted, committed, assigned, and unassigned*. (Previously the classifications were *reserved, unreserved designated, and unreserved undesignated*.) The *committed, assigned, and unassigned* classifications are considered the unrestricted portion of the fund balance and replace the unreserved classifications previously used for this analysis. 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 unrestricted fund balance 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.

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: http://www.auditor.state.mn.us/default.aspx?page=ComparisonTools.

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. The modified accrual basis of 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 in population may opt to use a cash basis of accounting. In 2012, 347 of the 626 small cities (55 percent) that reported their financial information opted to use a cash basis of accounting.[5] Cash basis accounting provides for the recording of receipts (revenues) when received in cash and the recording of disbursements (expenditures) when paid in cash.

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[4] For a more detailed discussion of GASB 54, please see Office of the State Auditor's Statement of Position on the topic, *Statement of Position: Fund Balances for Local Governments Based on GASB Statement No. 54*.

[5] There are 628 small cities, but the figure listed here reflects only the 626 cities that provided their 2012 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 totaled $4.82 billion in 2012. This represents an increase of 3 percent over 2011 revenues. Total revenues of cities over 2,500 in population increased 2 percent, and revenues of cities under 2,500 in population increased 6 percent (pg. 5).

- Total expenditures of the governmental funds for all cities totaled $5.40 billion in 2012. This represents an increase of 4 percent from 2011. Total expenditures of cities over 2,500 in population increased 3 percent, while total expenditures for cities under 2,500 in population increased 13 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 22 percent of total expenditures, and public safety accounted for 27 percent. For small cities, streets and highways accounted for 23 percent of total expenditures, and public safety accounted for 21 percent (pg. 5).

- Overall, small cities tend to carry a greater debt burden per capita than large cities. In 2012, small cities carried long-term debt of $1.19 billion, or $3,096 per capita, compared to $8.23 billion, or $2,044 per capita, for large cities (pg. 6).

- In 2012, unrestricted fund balances as a percent of current expenditures averaged 46 percent for large cities, compared to 98 percent for small cities (pg. 6).

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

- In 2012, cities over 2,500 in population, or large cities, had total governmental revenues of $4.38 billion. This represents an increase of 2 percent over 2011 levels. The primary revenue sources for large cities were taxes and state grants, which accounted for 68 percent of all large city revenues. Cities over 2,500 in population expended $4.87 billion from governmental funds to provide city services. This represents an increase of 3 percent over 2011 total governmental expenditures (pgs. 11-12).

- In 2012, cities under 2,500 in population, or small cities, had total governmental revenues of $440.4 million to finance city services. This represents an increase of 6 percent over 2011. Cities under 2,500 expended $525.9 million from governmental funds to provide city services. This represents an increase of 13 percent over 2011 total governmental expenditures (pgs. 18-19).

Ten-Year Trends - All Cities

Governmental Revenues

- Over the ten-year period of 2003 to 2012, an examination of city finances shows that, when adjusted for inflation[6], 2012 revenue levels are below 2003 levels and decreased by 9 percent over that period of time (pg. 7).

- Between 2003 and 2012, actual revenues derived from property taxes grew 78 percent, compared to an increase of 4 percent for revenues derived from intergovernmental sources. Additional analysis of actual intergovernmental revenues shows uneven trends over the ten-year period; federal grants increased 46 percent, state grants decreased 7 percent, and local grants increased 41 percent. When revenues are adjusted for inflation, the ten-year period shows a 29 percent increase in property tax revenues, while intergovernmental revenues decreased 25 percent (pg. 7).

- The proportion of total revenues derived from property taxes grew from 28 percent in 2003 to 39 percent in 2012. During this same time frame, revenues derived from intergovernmental sources decreased from 30 percent of total revenues to 25 percent (pg. 7).

Governmental Expenditures

- Actual total city expenditures grew from \$4.64 billion in 2003 to \$5.40 billion in 2012. This represents an increase of 16 percent. Over the ten-year period of 2003 to 2012, an examination of city finances shows that, when adjusted for inflation, 2012 expenditure levels are below 2003 levels and decreased 16 percent over the ten-year period (pg. 9).

- Over the ten-year period, when adjusted for inflation, total current expenditures declined 3 percent, capital outlays declined 36 percent, and debt service decreased 23 percent (pg. 10).

[6]"Adjusted for inflation" and "constant dollars" refer to data adjusted for inflation using the Implicit Price Deflator for State and Local Governments setting 2003 as the base year (N.I.P.A. Table 1.1.9, February 2014).

Comparison and Overview

2012 Finances for All Minnesota Cities

Revenues

Total revenues of the governmental funds for all Minnesota cities totaled $4.82 billion in 2012. This represents an increase of 3 percent over 2011 revenues. Total revenues of cities over 2,500 in population increased 2 percent, and revenues of cities under 2,500 in population increased 6 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 2012, intergovernmental revenues accounted for 39 percent of total revenues for small cities, compared to 23 percent for large cities. Among all cities, intergovernmental revenues accounted for 25 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, 2012 tax revenue from all sources accounted for 51 percent of large city revenues, compared to 37 percent of small city revenues. Property taxes accounted for 40 percent of large city revenues, compared to 34 percent for small cities.

On a per capita basis, large cities had total revenues of $1,087, and small cities had total revenues of $1,149.

Expenditures

Total expenditures of the governmental funds for all cities totaled $5.40 billion in 2012. This represents an increase of 4 percent from 2011. Total expenditures of cities over 2,500 in population increased 3 percent, while total expenditures for cities under 2,500 in population increased 13 percent.

The spending priorities of cities under 2,500 in population differ from those of cities over 2,500 in population. For example, small cities tend to direct a greater percentage of their resources to general government (15 percent) and less to culture and recreation (7 percent) than cities over 2,500 (10 percent and 11 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 22 percent of total expenditures, and public safety accounted for 27 percent. For small cities, streets and highways accounted for 23 percent of total expenditures, and public safety accounted for 21 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 per capita than large cities. In 2012, small cities carried long-term debt of $1.19 billion, or $3,096 per capita, compared to $8.23 billion, or $2,044 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.

Unrestricted Fund Balances of the General and Special Revenue Funds

A clear difference between the two city types is in the level of unrestricted fund balances. Small cities maintain significantly higher fund balances than large cities. In 2012, unrestricted fund balances as a percent of current expenditures averaged 46 percent for large cities, compared to 98 percent for small cities.

Among the 280 small cities that reported a fund balance in 2012, 140 (50 percent) had an unrestricted fund balance greater than 100 percent of total current expenditures. Among the 225 large cities, 32 cities (14 percent) had an unrestricted fund balance greater than 100 percent of total current expenditures. In 2012, unrestricted fund balances as a percent of total current expenditures among small cities ranged from -25 percent in Red Lake Falls to 634 percent in Thomson. Among large cities, the range was from 4 percent in Saint Michael to 415 percent in Bayport.

The Office of the State Auditor recommends that at year-end, or other key times of the year, local governments that rely significantly on property taxes maintain an unrestricted 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 unrestricted fund balance is less than or greater than this recommendation, the local government should be able to explain the reason for the difference.

The Office of the State Auditor recommends that each local government establish a formal policy on the level of unrestricted fund balance that should be maintained in the General Fund and other significant governmental funds. The policy should be set by the governing body and should provide both a time frame and a specific plan for increasing or decreasing the level of unrestricted fund balance. If the fund balance does not match the policy, a plan should be developed by the governing body that will allow for compliance with the policy. The fund balance policy should include a provision for a regular review of the sufficiency of the minimum fund balance level. The Office of the State Auditor's Statement of Position on Fund balance can be found on our website at: http://www.auditor.state.mn.us/default.aspx?page=statements.

Ten-Year Trends

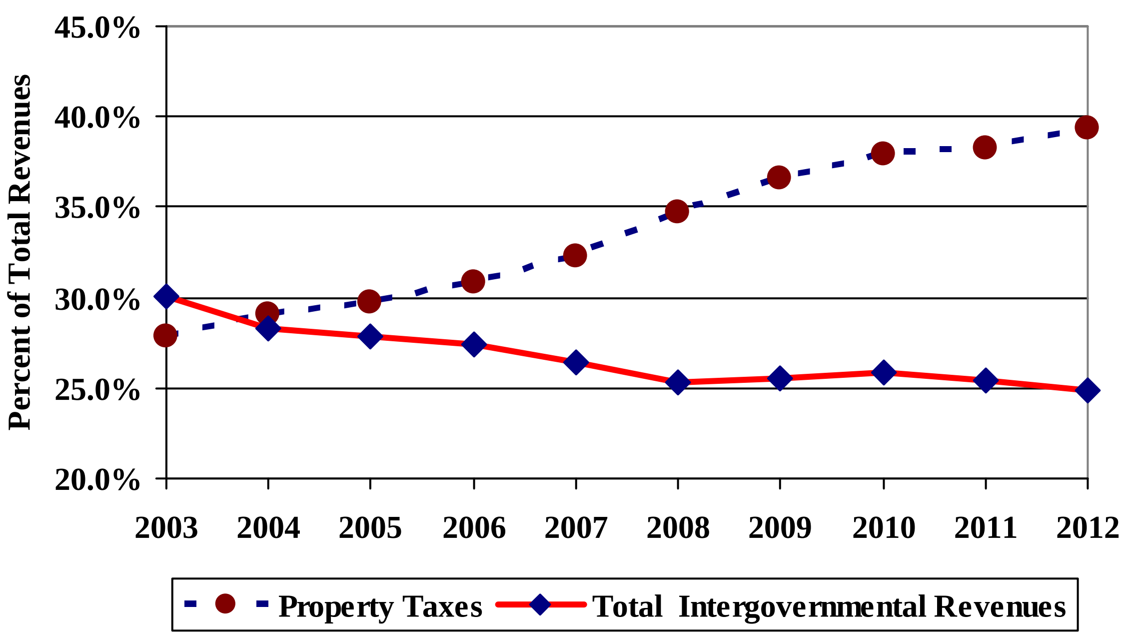
Governmental Revenues

Over the ten-year period of 2003 to 2012, an examination of city finances shows that, when adjusted for inflation[7], 2012 revenue levels are below 2003 levels and decreased by 9 percent over that period of time.

Between 2003 and 2012, actual revenues derived from property taxes grew 78 percent, compared to an increase of 4 percent for revenues derived from intergovernmental sources. Additional analysis of actual intergovernmental revenues shows uneven trends over the ten-year period; federal grants increased 46 percent, state grants decreased 7 percent, and local grants increased 41 percent. When revenues are adjusted for inflation, the ten-year period shows a 29 percent increase in property tax revenues, while intergovernmental revenues decreased 25 percent.

In addition, the proportion of total revenues derived from property taxes grew from 28 percent in 2003 to 39 percent in 2012. During this same time frame, revenues derived from intergovernmental sources decreased from 30 percent of total revenues to 25 percent. Figure 1 below shows that, as intergovernmental revenues to cities have slowed, 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 - 2003 to 2012



[7] "Adjusted for inflation" and "constant dollars" refer to data adjusted for inflation using the Implicit Price Deflator for State and Local Governments setting 2003 as the base year (N.I.P.A. Table 1.1.9, February 2014).

An examination of city revenues from 2003 to 2012 shows that, in actual dollars, revenues grew from $3.84 billion in 2003 to $4.82 billion in 2012, an increase of 25 percent. When adjusted for inflation, 2012 revenues are 9 percent less than in 2003. Figure 2 below illustrates this trend.

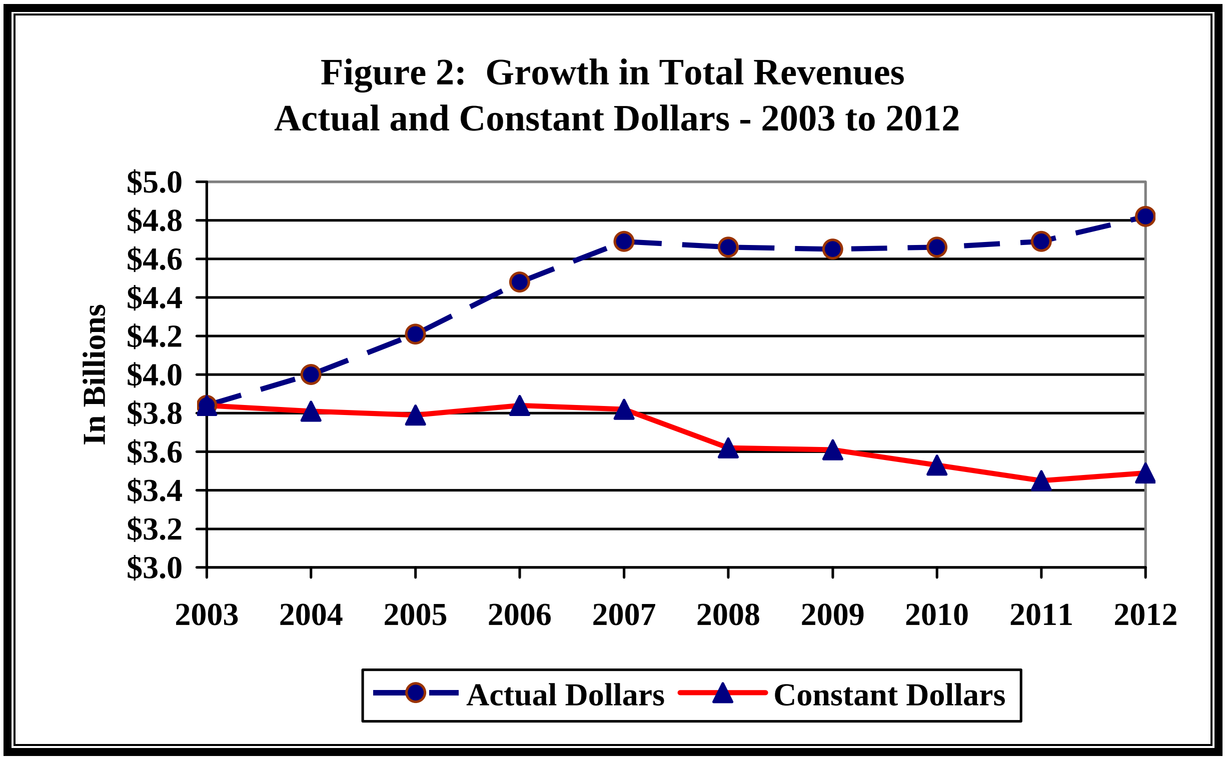


Table 1 on the following page provides a summary of the trend in city revenues from 2003 to 2012 when adjusted for inflation. Taxes, federal grants, and local unit grants were the only sources of revenues to grow over this period, increasing 16, 6, and 2 percent, respectively. All other categories of revenues showed declines over the ten-year period including interest earnings (-52 percent), all other revenues (-44 percent), state grants (-33 percent), special assessments (-30 percent), fines and forfeits (-25 percent), licenses and permits (-25 percent), and charges for services (-5 percent).

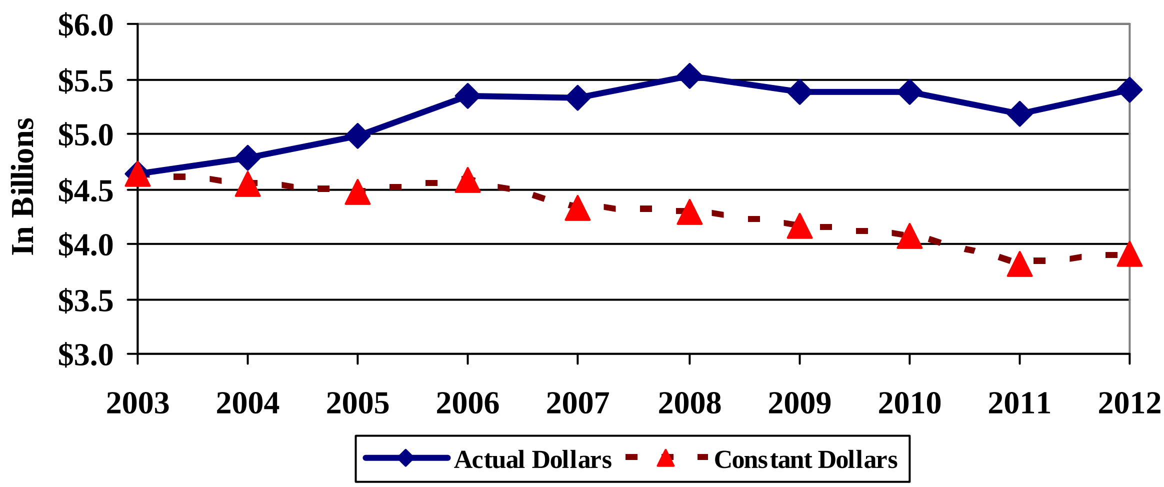
Table 1: Total City Revenues in Constant Dollars

Revenues	2003	2007	2008	2012	2003 - 07 5-Year Change	2008 - 12 5-Year Change	10-Year Change
Taxes	$1,500,939,681	$1,653,199,563	$1,697,842,099	$1,739,720,787	10.1%	2.5%	15.9%
Special Assessments	279,625,302	237,310,160	212,939,914	196,410,747	-15.1%	-7.8%	-29.8%
Licenses and Permits	150,332,607	123,087,876	107,209,749	113,059,761	-18.1%	5.5%	-24.8%
Federal Grants	172,621,264	154,633,701	183,835,970	182,496,504	-10.4%	-0.7%	5.7%
State Grants	914,031,885	780,182,658	660,328,402	613,952,572	-14.6%	-7.0%	-32.8%
Local Unit Grants	68,942,927	72,423,273	70,849,752	70,475,332	5.0%	-0.5%	2.2%
Charges for Services	384,046,379	364,807,201	340,764,944	363,757,023	-5.0%	6.7%	-5.3%
Fines and Forfeits	40,104,036	35,502,280	33,939,866	30,033,404	-11.5%	-11.5%	-25.1%
Interest Earnings	90,364,518	201,093,110	142,594,913	43,789,360	122.5%	-69.3%	-51.5%
All Other Revenues	240,106,087	199,085,721	166,031,558	134,644,779	-17.1%	-18.9%	-43.9%
Total Revenues	**$3,841,114,686**	**$3,821,325,543**	**$3,616,337,167**	**$3,488,340,269**	**-0.5%**	**-3.5%**	**-9.2%**

Governmental Expenditures

Actual total city expenditures grew from $4.64 billion in 2003 to $5.40 billion in 2012. This represents an increase of 16 percent. Over the ten-year period of 2003 to 2012, an examination of city finances shows that, when adjusted for inflation, 2012 expenditure levels are below 2003 levels and decreased 16 percent over the ten-year period. Figure 3 below shows the contrast between expenditures in actual and constant dollars.

Figure 3: Growth in Total Expenditures
Actual and Constant Dollars - 2003 to 2012



The three components of city spending are total current expenditures, total capital outlays, and total debt service. Over the ten-year period, when adjusted for inflation, total current expenditures declined 3 percent, capital outlays declined 36 percent, and debt service decreased 23 percent.

Table 2 below provides a summary of expenditures from 2003 to 2012 in constant dollars. Over this period, only two categories of expenditures grew: conservation of natural resources (28 percent) and public safety (2 percent). All other categories of expenditures decreased over this period.

Table 2: Total City Expenditures in Constant Dollars

Expenditures	2003	2007	2008	2012	2003 - 07 5-Year Change	2008 - 12 5-Year Change	10-Year Change
General Government	$507,439,563	$423,837,581	$423,449,059	$425,456,785	-16.5%	0.5%	-16.2%
Public Safety	1,010,814,441	1,028,104,291	1,091,414,084	1,032,733,034	1.7%	-5.4%	2.2%
Streets and Highways	992,699,168	1,016,277,072	876,839,493	851,418,612	2.4%	-2.9%	-14.2%
Sanitation	17,623,169	18,945,723	21,444,236	15,950,325	7.5%	-25.6%	-9.5%
Health	33,713,691	20,487,968	18,732,767	17,753,559	-39.2%	-5.2%	-47.3%
Culture and Recreation	527,332,670	531,103,514	538,450,808	424,326,730	0.7%	-21.2%	-19.5%
Housing/Economic Development	429,375,577	374,342,136	414,298,004	374,988,171	-12.8%	-9.5%	-12.7%
Conservation of Natural Resources	3,869,892	2,830,014	2,647,291	4,935,963	-26.9%	86.5%	27.5%
Airport	36,958,703	33,123,338	31,200,544	34,466,292	-10.4%	10.5%	-6.7%
All Other Expenditures	253,306,097	188,358,418	181,421,574	93,293,325	-25.6%	-48.6%	-63.2%
Debt Service	825,406,653	694,968,301	685,069,851	635,801,208	-15.8%	-7.2%	-23.0%
Total Expenditures	**$4,638,539,624**	**$4,332,378,356**	**$4,284,967,711**	**$3,911,124,004**	-6.6%	-8.7%	-15.7%
Total Current Expenditures	$2,496,435,799	$2,487,013,710	$2,574,917,786	$2,428,806,207	-0.4%	-5.7%	-2.7%
Total Capital Outlay	1,316,697,172	1,150,396,345	1,024,980,074	846,516,589	-12.6%	-17.4%	-35.7%
Total Debt Service	825,406,653	694,968,301	685,069,851	635,801,208	-15.8%	-7.2%	-23.0%
Total Expenditures	**$4,638,539,624**	**$4,332,378,356**	**$4,284,967,711**	**$3,911,124,004**	-6.6%	-8.7%	-15.7%

Overview of Cities Over 2,500 in Population

Total Governmental Revenues

In 2012, cities over 2,500 in population, or large cities, had total governmental revenues of $4.38 billion. This represents an increase of 2 percent over 2011 levels. The primary revenue sources for large cities were taxes and state grants, which accounted for 68 percent of all large city revenues.

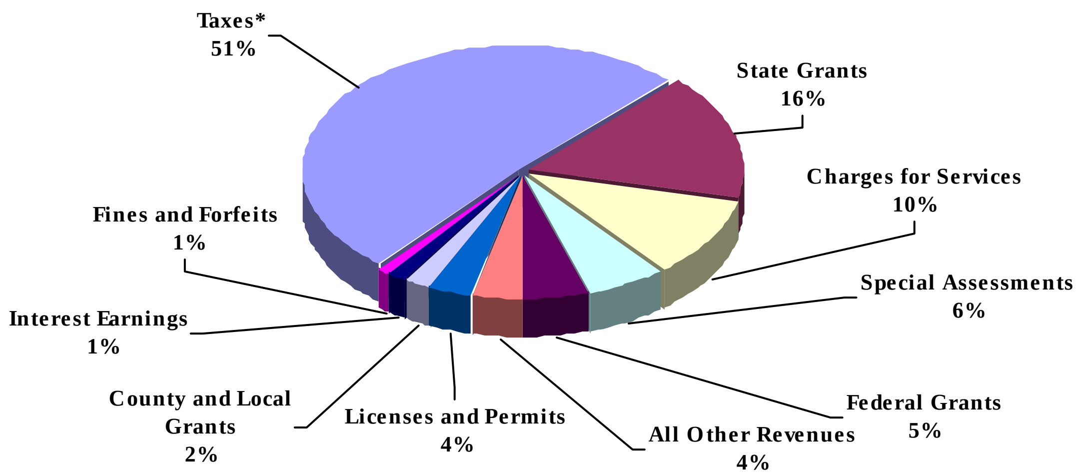
Among the various categories of large city revenues, five showed increases, while five showed decreases between 2011 and 2012. The categories with the largest increases were county and local grants (27 percent), charges for services (14 percent), and licenses and permits (13 percent). Those with the largest decreases were interest earnings (-39 percent), all other revenues (-8 percent), and fines and forfeits (-8 percent).

Although the relative shares of total governmental revenues generally change very little from year to year, an exception over the past several years has been the category of property taxes. Over the past five years, property taxes as a percent of total revenues increased from 35 percent in 2008 to 40 percent in 2012. The increased reliance on property tax revenues has offset decreasing state grants to cities and lower interest earnings over this period.

Figure 4 below shows the relative shares of total governmental revenues by source. Underlying data for this figure, as well as five-year trends can be found in Table 8 on page 28.

Figure 4: 2012 Total Governmental Revenues - Cities Over 2,500 in Population

$4,376,267,398



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

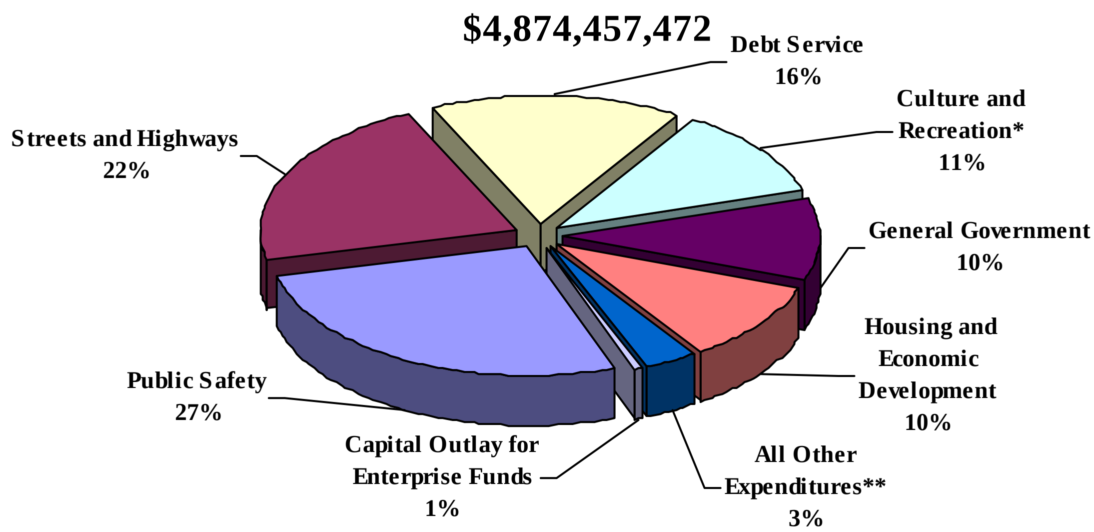
Total Governmental Expenditures

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 2012, cities over 2,500 in population expended $4.87 billion from these various governmental funds to provide city services. This represents an increase of 3 percent over 2011 total governmental expenditures. Total governmental expenditures include current expenditures, capital outlays, and debt service. Current expenditures accounted for 63 percent of total governmental expenditures, while capital outlay accounted for 21 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 outlay expenditure. Public safety accounted for 40 percent of all current expenditure -- more than double that of any other category. Streets and highways accounted for 62 percent of all capital expenditures, over five times greater than any other category of capital outlay.

Figure 5 below 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: 2012 Total Governmental Expenditures - Cities Over 2,500 in Population



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

**This category includes expenditures for airport, cemetery, conservation of natural resources, health, sanitation, transit, unallocated insurance, unallocated pension, and all other unallocated.

Capital Outlay Expenditures

Cities over 2,500 in population expended $1.03 billion on capital investments in 2012. This represents an increase of 7 percent over the level expended in 2011. Capital outlay expenditures 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 amounts for large cities.

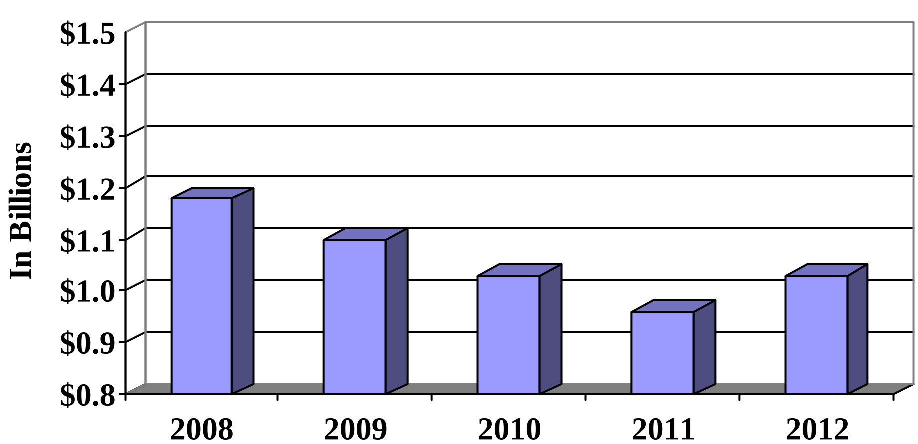
Table 3: Total Capital Outlay Expenditures in Actual Dollars and Per Capita

Year	Total Capital Outlay (actual dollars)	Per Capita*
2008	$1,184,065,833	$303
2009	$1,097,801,667	$280
2010	$1,033,480,751	$261
2011	$ 960,350,132	$241
2012	$1,026,282,677	$255

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

Figure 6 below illustrates the trend in capital outlay expenditures for the years 2008 to 2012.

Figure 6: Capital Outlay Expenditures
Cities Over 2,500 in Population - 2008 to 2012

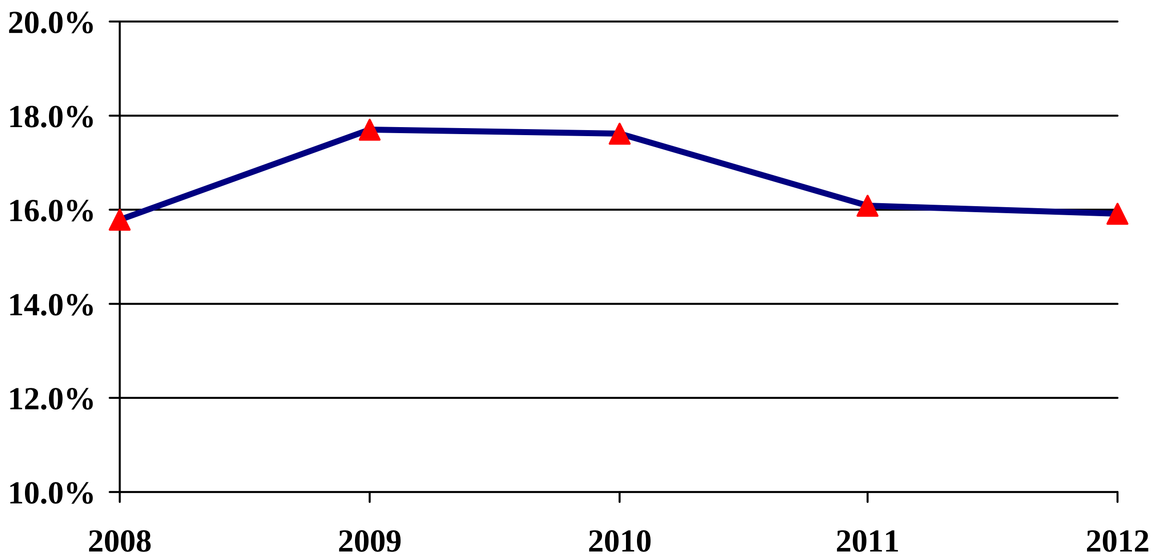


Debt Service

In 2012, large cities expended a total of $773.0 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 2011 and 2012, large city debt service expenditures increased $14.0 million, or 2 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 - 2008 to 2012

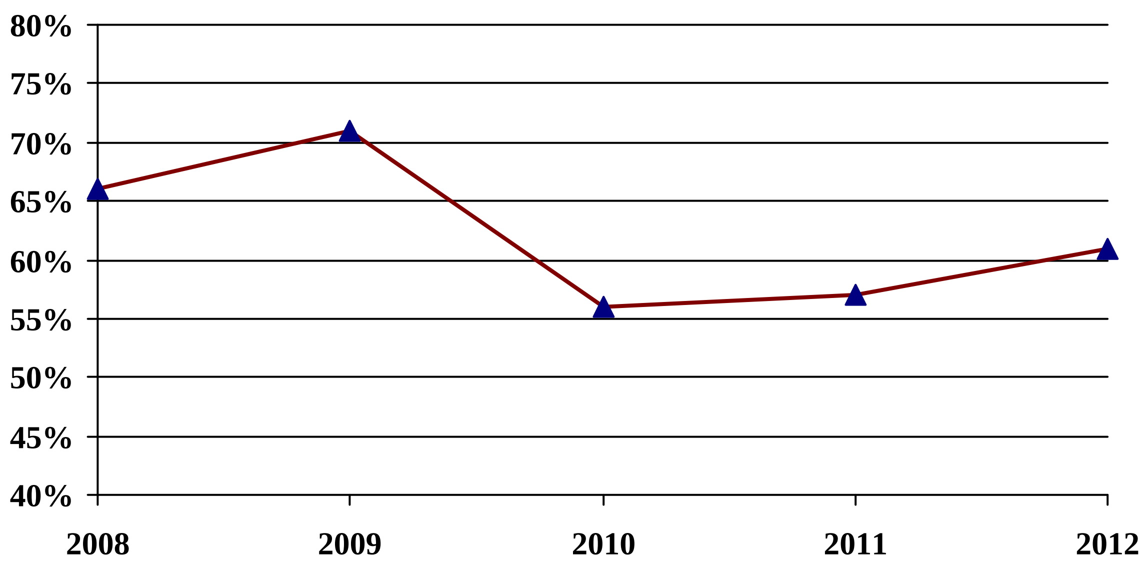


Municipal Enterprises

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.

In aggregate, large city municipal enterprises reported a net income of $183.4 million and net transfers (transfers out minus transfers in) of $112.4 million in 2012. This represents a decrease of 10 percent in net income and a 4 percent decrease 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 represented 61 percent of net profits among large city enterprises. Figure 8 below 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 - 2008 to 2012



Outstanding Long-Term Indebtedness

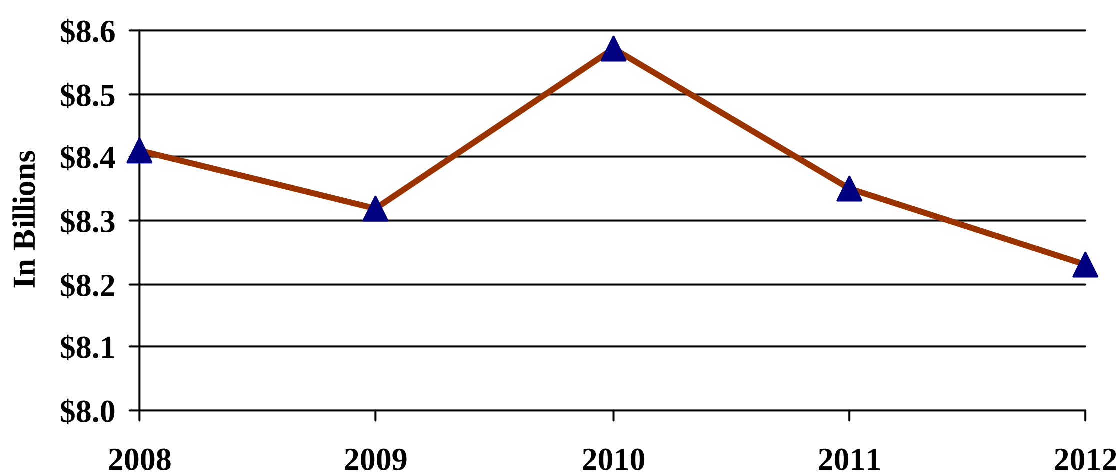
Cities over 2,500 in population carried long-term debt of $8.23 billion, or $2,044 per capita, at the end of 2012. This represents a decrease of 1 percent from the 2011 level. Cities incur long-term debt through various ways such as the issuance of bonds and notes, certificates of indebtedness, and tax 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 expenditures. The amount of outstanding debt affects a city's expenditures because cities must make principal and interest payments to service the debt. Table 4 below shows the outstanding bonded indebtedness for 2011 and 2012.

Table 4: Two-Year Summary of Outstanding Bonded Indebtedness

	2011 Amount	2012 Amount
General Obligation	$1,724,561,687	$1,883,395,437
General Obligation Tax Increment	483,029,367	416,667,133
Revenue Tax Increment	59,254,175	51,468,322
Special Assessment	2,030,278,932	1,969,411,470
General Obligation Revenue	1,396,107,365	1,342,250,291
Revenue	1,076,186,192	1,100,181,292
All Other	99,708,061	58,631,444
Total Bonded Indebtedness	**$6,869,125,779**	**$6,822,005,389**

Figure 9 below 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 - 2008 to 2012



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

Unrestricted Fund Balances of the General and Special Revenue Funds

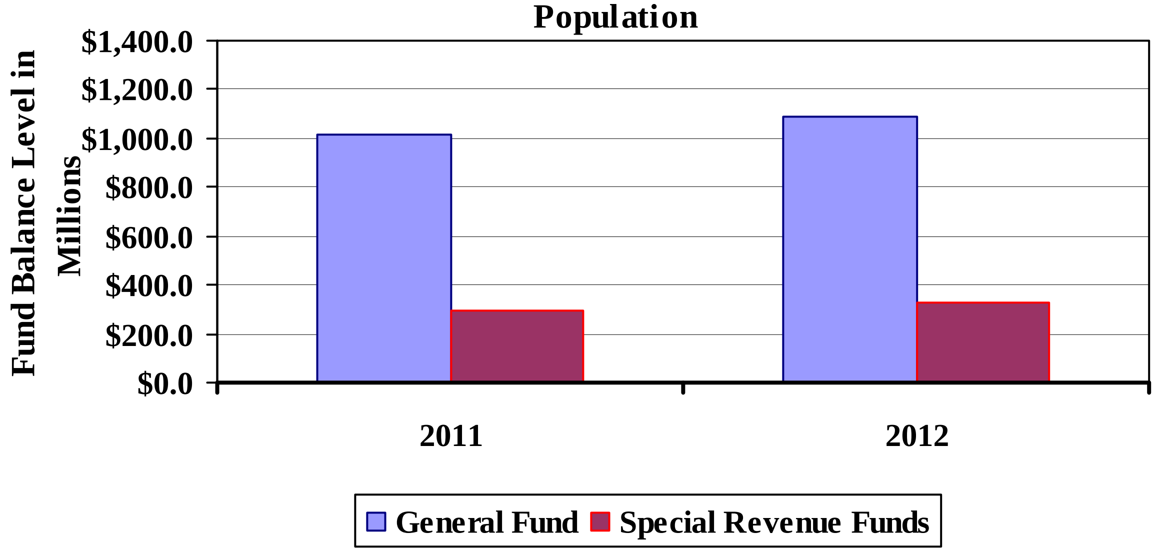
The unrestricted fund balances of large cities' General and Special Revenue Funds totaled $1.41 billion in 2012. This was an increase of 8 percent over 2011. Cities should have relatively large fund balances at the end of the year (December 31) because they must rely on them to meet expenditures during the first five months of the next fiscal year until they receive the first property tax and state aid payments.

Large city unrestricted fund balances as a percent of total current expenditures averaged 46 percent in 2012, compared to 44 percent for unrestricted fund balances in 2011. Larger cities tend to have lower unrestricted fund balances as a percent of current expenditures than small cities. Unrestricted fund balances as a percent of current expenditures averaged 27 percent for cities of the first class, compared to 74 percent for fourth class cities.

As discussed earlier, cities were required to implement GASB Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*, in 2011. This statement changed the classifications of fund balances. Under GASB 54, cities classify fund balances for each fund as *nonspendable, restricted, committed, assigned, or unassigned*. The last three of these classifications are considered the unrestricted portion of the fund balance and replace the unreserved classifications previously used for this analysis. Appendix A (pg. 311) provides a more detailed discussion of fund balances and GASB 54.

Figure 10 below shows the unrestricted fund balances for the General and Special Revenue Funds by type.

Figure 10: 2011 and 2012 Unrestricted Fund Balances of the General and Special Revenue Funds for Cities Over 2,500 in Population



Overview of Cities Under 2,500 in Population

Total Governmental Revenues

In 2012, cities under 2,500 in population, or small cities, had total governmental revenues of $440.4 million to finance city services. This represents an increase of 6 percent over 2011.

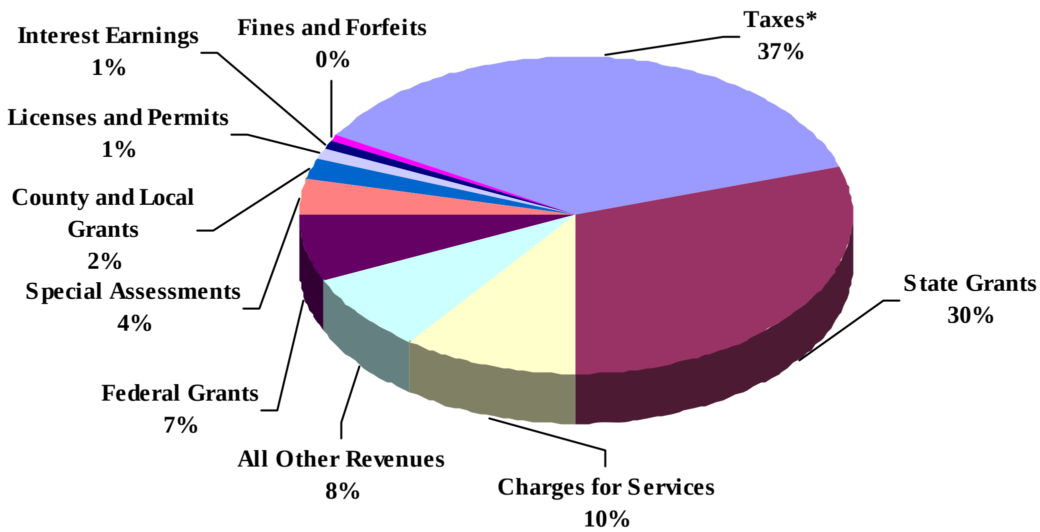
Two sources of revenues showed double-digit increases between 2011 and 2012: federal grants (43 percent) and taxes (11 percent). The increases in these two categories offset decreases in interest earnings (-23 percent), county grants (-13), and special assessments (-5 percent).

The main sources of revenues for small cities in 2012 were state grants and taxes, which together accounted for 67 percent of all revenues.

Figure 11 below 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: 2012 Total Governmental Revenues - Cities Under 2,500 in Population

$440,363,079



*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 2012, cities under 2,500 in population expended $525.9 million from governmental funds to provide city services. This represents an increase of 13 percent over 2011 total governmental expenditures.

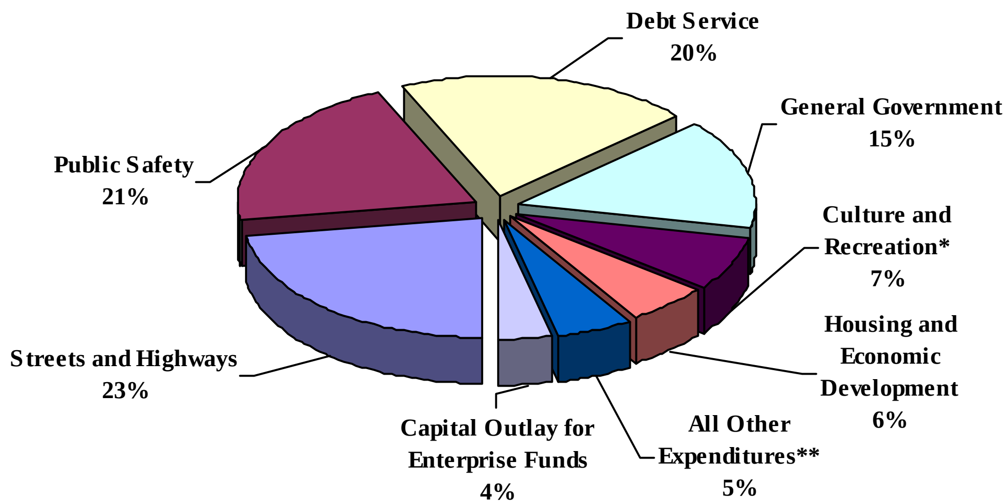
Between 2011 and 2012, several categories showed double and even triple-digit increases, including capital outlay for enterprise funds (111 percent), airports (75 percent), sanitation (62 percent), debt service (43 percent) and housing and economic development (22 percent). Three categories of expenditures decreased between 2011 and 2012, including all other expenditures (-39 percent), libraries (-14 percent), and parks and recreation (-6 percent).

In 2012, 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 78 percent of all expenditures.

Figure 12 below 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: 2012 Total Governmental Expenditures - Cities Under 2,500 in Population***

$525,944,330



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

**This category includes expenditures for airport, cemetery, conservation of natural resources, health, sanitation, transit, unallocated insurance, unallocated pension, and all other unallocated.

***Due to rounding, the sum of the percentages is greater than 100 percent.

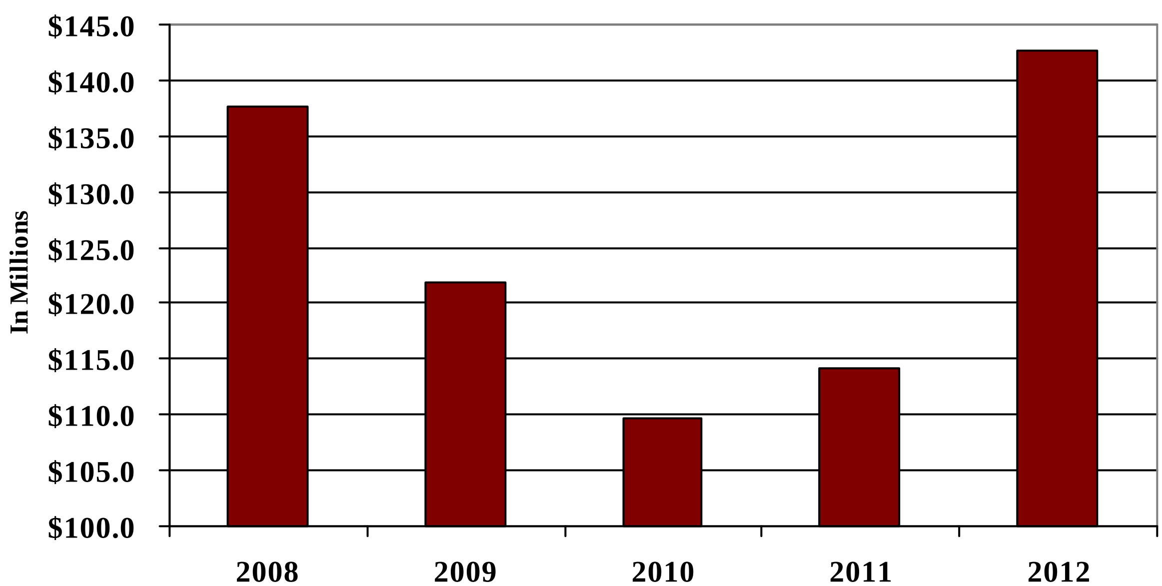
Capital Outlay Expenditures

Capital outlay expenditures account for the purchase, construction, or permanent improvements of buildings, equipment, machinery, and land. Small cities expended $142.6 million on capital outlay in 2012. This represents an increase of 25 percent over the level expended in 2011.

Capital outlay expenditures 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 below illustrates the trend in capital outlay expenditures of small cities for the years 2008 through 2012.

Figure 13: Total Capital Outlay Expenditures
Cities Under 2,500 in Population - 2008 to 2012

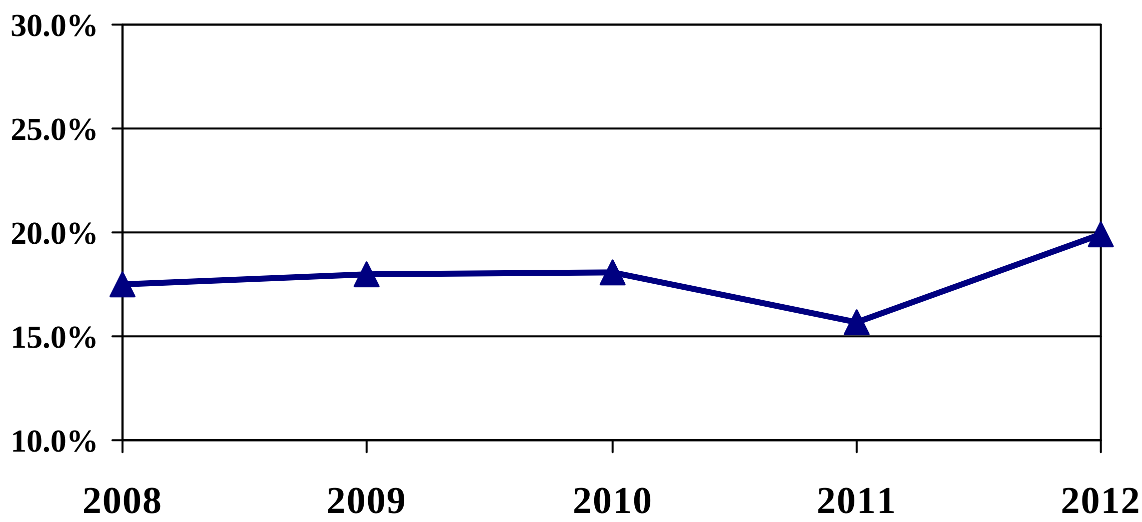


Debt Service

Debt service includes expenditures for the principal and interest payments on debt incurred by cities. In 2012, small cities expended a total of $104.9 million on debt service. This represented an increase of 43 percent over 2011. Overall, debt service expenditures accounted for 20 percent of total expenditures for small cities.

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

Figure 14: Debt Service as a Percent of Total Expenditures - Cities Under 2,500 in Population - 2008 to 2012

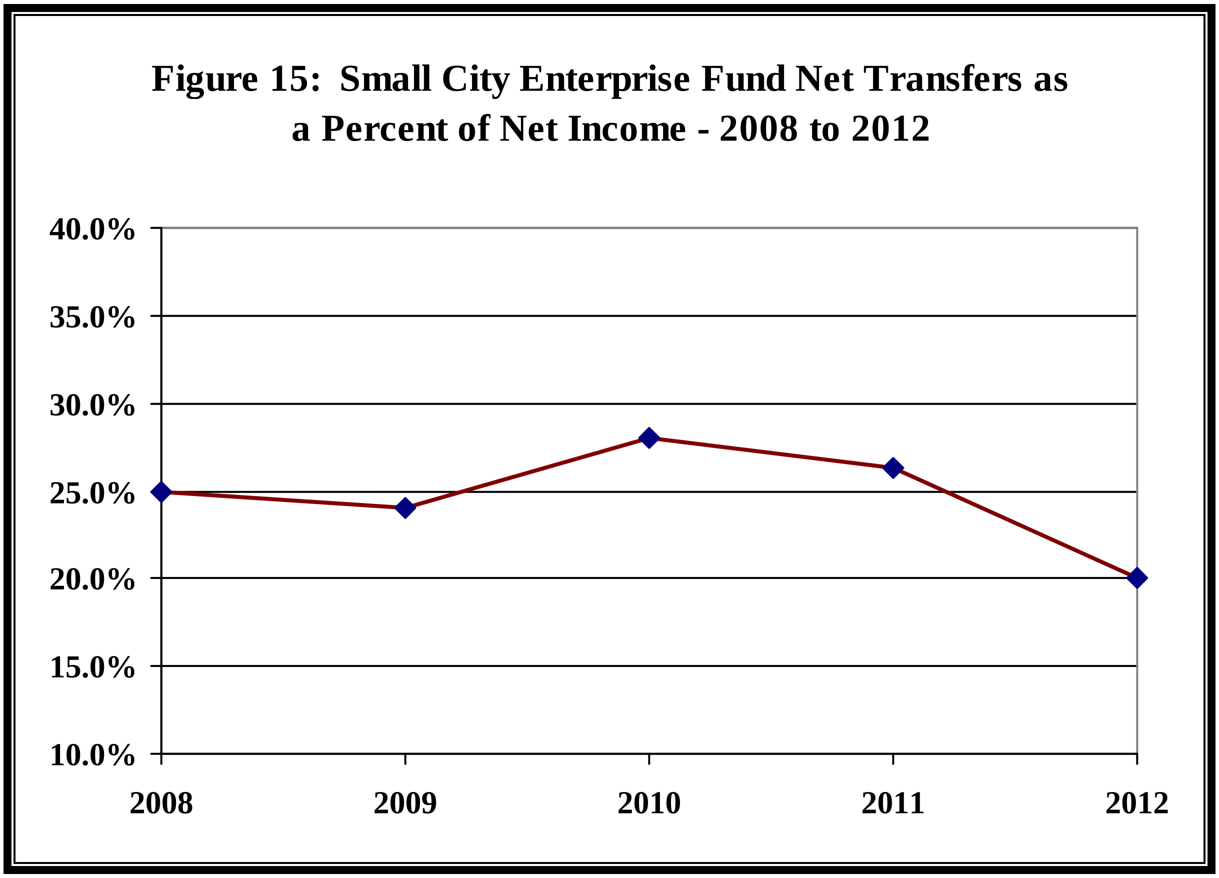


Municipal Enterprises

The total net income of small city enterprises in 2012 was $50.9 million, and the net amount transferred to other funds was $10.2 million. This represents an increase in net income of 34 percent and an increase in net transfers (transfers out minus transfers in) of 2 percent between 2011 and 2012.

In 2012, the municipal enterprises of small cities transferred 20 percent of their net income to other funds, compared to 26 percent in 2011.

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



Outstanding Long-Term Indebtedness

Cities under 2,500 in population carried long-term debt totaling $1.19 billion at the close of 2012. This represents a 2 percent increase over the level in 2011. On a per capita basis, small cities carried $3,096 in long-term debt, compared to $2,044 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.

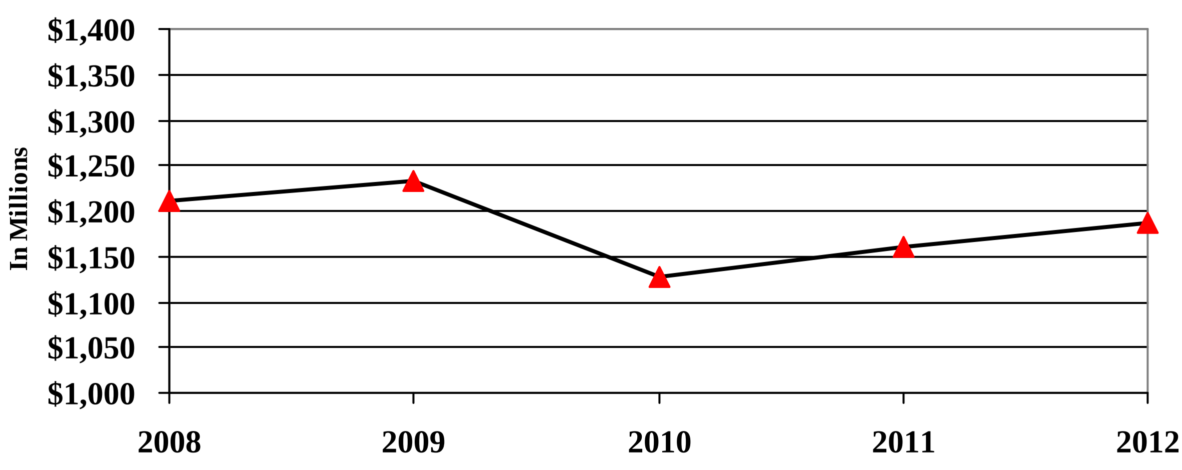
Table 5 below looks at outstanding bonded indebtedness for 2011 and 2012.

Table 5: Two-Year Summary of Outstanding Bonded Indebtedness

	2011 Amount	2012 Amount
General Obligation	$121,350,948	$165,649,915
General Obligation Tax Increment	23,395,054	19,922,843
Revenue Tax Increment	1,751,073	319,763
Special Assessment	270,671,421	250,521,523
General Obligation Revenue	339,972,565	351,375,898
Revenue	89,473,918	79,838,280
All Other	2,408,524	2,154,694
Total Bonded Indebtedness	**$849,023,503**	**$869,782,916**

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

Figure 16: Outstanding Long-Term Indebtedness for Cities Under 2,500 in Population - 2008 to 2012*



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