

Rice Lake Township Assessment

October 2002



Prepared for Rice Lake Township
by the
Duluth-Superior Metropolitan Interstate Committee



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Metropolitan Interstate Committee

*Duluth and Superior urban area communities
cooperating in planning and development through a
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**"Guiding the Future of Transportation
and Planning for the Twin Ports Area"**



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October 3, 2002

This report was prepared by the Duluth-Superior Metropolitan Interstate Committee (MIC) as a result of the Rice Lake Township Board's request for assistance regarding a short-term study of incorporation and annexation issues. Members of the Board were asked by residents to research these issues. The MIC examined some of these issues about 5 years ago; however, recent changes in state legislation required that new research would be necessary to document several other impacts on issues including property tax issues and municipal services.

Section I of this report will examine the changes in state legislation. Section II will provide an overview of the boundary adjustment process. Section III provides a review of urban and non-urban town powers. Section IV will describe Minnesota's complex property tax system and how Rice Lake could be financially affected by incorporating all or parts of the township. Section V will list options and recommendations for Rice Lake.

SECTION I: MUNICIPAL BOUNDARY ADJUSTMENTS

In 2000, the Minnesota Legislature required Minnesota Planning (officially known as the Office of Strategic and Long Range Planning) to prepare a report on the effects of the transfer of duties regarding municipal boundary adjustments. Much of the information in Section I of this report was obtained from Minnesota Planning's report along with interviews with Minnesota Planning staff.

Introduction of State Authority

In 1959, Minnesota became the first state in the country to create a quasi-judicial commission, the Minnesota Municipal Board, to hear and decide local incorporation and boundary adjustment questions.

Prior to this, the Minnesota Legislature was confronted with municipal boundary chaos. The spectacular post-World War II growth in large urban centers marked a distinct departure from the previous patterns of a predominantly agricultural age. In just one decade, in five metropolitan counties, 45 new villages were organized: nearly half of them contained under 1,000 people when incorporated; seven contained under 200; and one contained only 43. By the end of the 1950s, a total of 130 separate municipalities had mushroomed in the seven-county Twin Cities area.

This proliferation of uneconomic villages, which often lacked means to furnish their own police and fire protection or adequate sewage disposal facilities, placed additional burdens on counties and surrounding areas. A 1959 Interim Report to the Legislature complained that "multiplying villages, like rabbits, can outdistance all progress achieved by otherwise intelligent planning." Before 1959, provisions and procedures for incorporation and boundary changes were haphazard, with no public body to provide order and an overview. In some cases, statutory

authority to annex or detach an area, even with the support of everyone affected, was nonexistent. The laws that did exist were scattered and complicated and allowed such abuses as:

- Incorporation for the single purpose of obtaining a liquor license, preempting the tax base created by a new industry, or merely avoiding annexation;
- Gerrymandered municipal boundaries where those seeking annexation or incorporation might bypass entire blocks or residential areas that were unfavorable to their position;
- Islands of unincorporated land surrounded by cities; or
- Bisection of cities by new freeways.

Clearly, it was necessary to stem the tide of imprudent incorporations and end the confusion caused by inadequate legal controls. The Legislature recognized the need for a coherent policy to guide urban growth not only in the metropolitan area but throughout the entire state. So, in 1959, Chapter 414 was passed. It was a comprehensive act codifying all laws on boundary adjustment and providing for administrative review by the Minnesota Municipal Board. The principles that form the basis for the law include:

- Sound urban development and preservation of agricultural land and open spaces through land use planning is essential to the continued economic growth of this state.
- Municipal government most efficiently provides services in areas intensively developed for residential, commercial, industrial, and governmental purposes.
- Township government most efficiently provides services in areas used or developed for agricultural, open space and rural residential purposes.
- The public interest requires that municipalities be formed when there exists or will likely exist the necessary resources to provide for their economical and efficient operation.
- Annexation to existing municipalities of unincorporated areas unable to supply municipal services should be facilitated.
- Consolidation of municipalities should be encouraged.

The Minnesota Municipal Board

The Board was charged with:

- Conducting proceedings and issuing orders to create a municipality, combine 2 or more governmental units, or alter a municipal boundary
- Providing for the extension of municipal government to areas which are developed or are in the process of being developed for intensive use for residential, commercial, industrial, institutional, and governmental purposes, or are needed for such purposes
- Protecting the integrity of land use planning in municipalities and unincorporated areas

Just two years after the Board was created, a report of the Committee on Municipal Laws to the 1961 Legislature stated:

"The purpose underlying the philosophy of the law has been accomplished... (t)he provisions to prevent the multiplication of municipalities have been largely self-executing. We find the establishment of a statewide administrative commission to apply legislative standards in hearing and determining boundary change indispensable to sound

public policy in administering the future urban growth in Minnesota. We have found no expert that disagrees."

During its existence, the Board:

- Strengthened municipal government by providing a means of orderly and intelligent evaluation of proposed incorporations, consolidations, and annexations throughout the state
- Controlled incorporation of uneconomic cities: in the nine years before the Board was created, 62 new cities (averaging only 7.6 square miles) were formed, compared to only 15 new cities (averaging 30 square miles) in the first 20 years after the Board's formation
- Assisted governmental units in addressing the problems and responsibilities that go with development, such as finances, the environment, delivery of services, etc.
- Encouraged communities to work together to reach mutually agreeable solutions at the local level.

Dissolution of the Municipal Board

All of the power and responsibilities of the former Minnesota Municipal Board were transferred to Minnesota Planning on June 1, 1999, with the ultimate authority resting with the director of the agency.

Working in concert with local government associations and others, the agency established an alternative dispute resolution process to handle contested case annexations, detachments and concurrent detachments and annexations. The process strongly encourages local governments to jointly plan for fringe areas. If joint planning efforts fail to resolve disputed issues, the affected parties will enter a mediation process that, if unsuccessful, is followed by a hearing. Minnesota Planning also prepares a fact-finding report on each case.

Municipal Boundary Adjustments (MBA) at Minnesota Planning is the internal team that reviews, processes, and facilitates boundary expansion, contraction, or unification in Minnesota. The vast majority of requests initiating boundary change come from property owners, with the remainder coming from cities and townships. All adjustments affect local government and have the potential for conflict or agreement. MBA works with other state agencies and local governments to make the most efficient use of available resources.

MBA seeks to serve and provide local governments with:

- Assistance in understanding boundary change and incorporation statutes;
- Staff consultations on potential issues and concerns;
- Information on the various statutory factors to be considered, and procedures to be followed, in decisions of contested cases;
- Identification of other data resources;
- Sample documents and other supporting materials to initiate boundary change or incorporation;
- Consultation as to citizens' rights in boundary change proceedings.

Sunset of the Municipal Board

In 1997, the Legislature acted to sunset the Minnesota Municipal Board effective December 31, 1999, transferring its duties to Minnesota Planning.

During the two years prior to the sunset there were clear indications that the arbitration process created to replace the Board was unworkable. The timelines and method of selecting arbitrators conflicted with existing statutory provisions and ignored the reality of multiparty proceedings. Significant legal issues were being raised by legal counsel for both the Municipal Board and for Minnesota Planning. In addition, the cost impact of switching from an appropriation-based model to a fee-for-services model was overlooked. Further confusion was added when the Legislature accelerated the Board's sunset by seven months on the last day of the 1999 session.

Arbitration rejected

Since 1997, the use of arbitration has been available to parties under Chapter 414 as a substitute for a contested hearing. This option has never been exercised by any party. Shortly after the Municipal Board sunset, stakeholders agreed to yet another method of arbitration as a replacement for the Board's decision-making authority in contested matters.

In 1999, the ability of the Director of Minnesota Planning to order parties into arbitration was successfully challenged in court. As a result, the Director has not required arbitration unless all parties agree to use it. Agreement to use arbitration among parties to a contested proceeding has not happened, nor is it likely to in the future. Consequently, contested proceedings are delegated to the Office of Administrative Hearings for assignment of administrative law judges.

Dramatic Differences in Perceptions

The sunset of the Municipal Board has rekindled some long-standing feuds between interested stakeholders. Cities perceived the sunset as a long overdue and necessary change to improving the boundary adjustment process. Overall, feedback from city participants and associations indicates a substantial increase in satisfaction with the current process. In particular, cities are pleased with the use of administrative law judges.

Townships, on the other hand, have made it clear that they are not in a better position since the sunset of the Municipal Board. The creation of a new association devoted to addressing township concerns on annexation issues signals dissatisfaction with the current process. Townships cite the 1992 changes to Minnesota Statutes Chapter 414 (the allowance of cities to annex 60 acres or less abutting the city by ordinance upon petition of 100% of owners without an election), the sunset of the Board and the rising costs of contested proceedings as shrinking their opportunity for meaningful participation in the process. In particular, townships are decidedly against continued use of administrative law judges as final decision-makers.

Mediation Widely Accepted

As divided as individual parties and local government associations are with respect to the current state of contested proceedings, they appear to be united in their support of mediation in the pre-hearing boundary adjustment process. Mediators received high marks; the most sought-after

mediators are former Municipal Board members as parties gravitate towards individuals experienced and knowledgeable in boundary adjustments.

Despite the widespread support for mediation, some concerns have surfaced. As one mediator observed, mediation is a process of compromise which may not produce the best result for a legal issue. Some mediations have resulted in agreements containing terms and conditions not authorized by Chapter 414.

The concern regarding the increase in costs for contested hearings has not surfaced in mediation where the costs are comparatively modest, averaging from \$2,000 to \$4,000 per case, and generally split among the parties.

Administrative Hearing Costs Skyrocket

Costs of contested proceedings have risen significantly since the sunset of the Municipal board. This is largely a result of a difference in funding models between the Board and the Office of Administrative Hearings. Each board member received a \$50 per diem from the state's general fund while the services of administrative law judges are billed on a fee-for-service basis at \$150 per hour. An example of the disparity that results between the two funding structures can be seen in a recent case between St. Cloud and St. Augusta. In this matter, the cost of the administrative law judge was approximately \$29,000. The Municipal Board's estimated costs for the same time would have been \$1,800.

High Costs are a Barrier to Participation

Under the Municipal Board funding structure, costs for the decision-makers were paid by the state. Due to recent amendments to Chapter 414, the costs for administrative law judges are now paid for by the parties. Although costs are allocated proportionately among parties, some cities, most townships and property owner petitioners cannot afford these costs in addition to the cost of preparing and presenting their case. In preparing individual cases for hearing, party spending tends to be consistent with the commitment to the desired outcome. This will remain constant regardless which decision-making model is in place.

High costs have prevented private parties and related groups such as homeowner's associations and watershed districts from participating in this level of the process. Even when Chapter 414 allows for an objection from a township, the high cost of hearings impedes a township's ability to contest annexation, and is perceived as a further limitation of rights.

The overwhelming share of boundary adjustment cases continue to be uncontested as they were before the sunset of the Municipal Board. However, the effect of the high costs of the new process may be causing smaller entities to avoid contesting boundary adjustments even though they may disagree with them. In the 2½ years before the dissolution of the Municipal Board, 475 boundary adjustment cases were proposed. Of this number, 30 (6.3%) were contested. In the 2½ years after the dissolution of the Board, 909 cases were proposed and only 22 (2.4%) were contested. So the rate of contesting the proceedings has dropped by two-thirds.

One court case has already challenged the fairness of assessing costs to private individuals. In this instance, the court rejected the claim but there is every indication that the issue will continue to resurface until the current funding structure is re-examined.

Collection of hearing costs has become an issue for the Office of Administrative Hearings as some parties have refused to pay the costs of the case out of protest. This situation may threaten the Office's ability to continue to provide these services for boundary adjustment proceedings.

Legislative Policy for Chapter 414 Needs Updating

Minnesota Planning believes that more changes are needed to Chapter 414. Establishing a clear statement of legislative policy regarding the relationship between cities and townships is the first step toward a stable environment for municipal growth. Chapter 414 was created to manage and facilitate municipal growth. The legislative policy intent contained in the preamble to Chapter 414 is clear but may not be current. This is the threshold issue the Legislature must address. Absent this policy direction and commitment, other changes to Chapter 414 will fall short.

SECTION II: PROCESS OVERVIEW

The procedures for adjusting municipal boundaries under Minnesota Statutes Chapter 414 were, for the most part, left intact following the sunset of the Minnesota Municipal Board. The sunset had the greatest impact on the contested hearing procedures of Chapter 414 which affect the smallest percentage of total proceedings processes by municipal boundary adjustment staff at Minnesota Planning.

Chapter 414 procedures for hearings are still in place, only with different decision-makers. The Director of Minnesota Planning inherited all of the Municipal Board's decision-making authority and is the only decision-maker for proceedings that are uncontested. In addition, parties have the option to use a single arbitrator to decide the matter or a panel of three arbitrators. Neither arbitration process has ever been used.

For hearing or contested proceedings, the Director of Minnesota Planning has expanded authority to invoke alternative dispute resolution processes, which include mediation and arbitration instead of Chapter 414 procedures. The Director also has the authority to delegate the hearing and final decision-making to the Office of Administrative Hearings.

Statutory Sections

Chapter 414 sets out procedures for nine different ways to adjust a municipal boundary:

§ 414.02 *Municipal Incorporation*

Can be initiated by a resolution of the town board or by a petition of 100 or more property owners. The statute mandates an administrative hearing on the question regardless of whether there is opposition, and sets forth evidentiary factors that must be considered by the decision-maker.

§ 414.031 *Annexation of Unincorporated Property by Board Order*

Can be initiated by a resolution of the annexing municipality; a resolution of the township; a petition of 20 percent of the property owners or 100 property owners, whichever is less; or by a joint resolution of the city and the town. The statute mandates an administrative hearing on the issue and sets forth evidentiary factors that must be considered by the decision-maker.

§ 414.0325 *Orderly Annexations Within a Designated Area*

One or more townships and one or more municipalities, by joint resolution, may designate an unincorporated area as in need of orderly annexation. Thereafter, any signatory or the Director may initiate annexation of any part of the area designated. These annexations still require a hearing unless the joint resolution designating an area provides for conditions for annexation and states that the Director may review and comment but shall order the annexation within 30 days.

§ 414.033 *Annexations by Ordinance*

Provides for six different ways for a municipal council to declare unincorporated land annexed by ordinance. No annexation by ordinance is effective until approved by the Director. Two of the six methods for ordinance annexation allow a 90-day objection period for the township. If objections are raised during that time, the file must go forward for an administrative hearing before final decision.

§ 414.0335 *Ordered Governmental Service Extension: Annexation by Ordinance*

An order by the Pollution Control Agency pursuant to Minnesota Statutes section 115.49 or similar statute triggers annexation by ordinance, regardless of the acreage involved, and bypasses the requirement to consider the 414.031 statutory factors required by an administrative hearing. Municipalities may opt to annex property by ordinance instead of extending services by contract. The Director may review and comment but shall approve the ordinance within 30 days. This section was added in 1997, and has never been used.

§ 414.041 *Consolidation of Municipalities*

Allows two or more abutting municipalities to consolidate. May be initiated by a resolution of each municipality involved, the Director or by resident petition. Provides for a local consolidation commission and a chair to be appointed. The commission has up to two years to study the question of consolidation and must report a recommendation back to the Director. After an administrative hearing on the report and recommendation, any order is not final unless approved by a majority vote of each municipality involved and a majority vote of the residents of each community.

§ 414.051 *Review of Townships According to Population*

After each federal census, the Director may make recommendations to any township with a population that exceeds 2,000. (This section used to provide for a hearing on the question of incorporation of a town with a population that exceeded 2,000.)

§ 414.06 *Detachment of Property From a Municipality*

Property within a city that abuts the municipal boundary and is rural in character and not developed for residential, commercial or industrial uses may be detached. The process can be initiated by a resolution of the municipality or by property owners. (All property owners if the area is less than 40 acres; 75 percent of owners if the area is more than 40 acres.) No hearing is necessary if both a municipal resolution and a petition by all the property owners is received.

§ 414.061 *Concurrent Detachment and Annexation of Incorporated Land*

Property of one municipality which abuts another may be concurrently detached and annexed by joint resolution of both municipalities. Property owners may initiate the process by a petition signed by all the owners together with a resolution of one of the municipalities. An administrative hearing is required if only one city supports the action.

§ 412.091 *Dissolution*

A percentage of voters may petition for a special election on the question of dissolving a city. A hearing is conducted in accordance with section 414.09 prior to the election. Disposition of the land to appropriate townships occurs after an election on the question.

Procedures

Boundary adjustments that require a hearing by statute, or where the right to object is exercised, thereby triggering a hearing, are processed as contested proceedings. Boundary adjustments that are accomplished by ordinance, joint resolutions or by township waiver are processed as uncontested or administrative proceedings. For all docketed files, initiating documents are received and collected according to the statutory requirements. The boundary adjustment staff completes file work-up. Property descriptions are checked for legal compliance and are currently reviewed by the Cartographic Unit at the Minnesota Department of Transportation. Any legal or procedural issues are addressed at this point.

Uncontested Proceedings

Includes any proposed boundary adjustment filed under a section of Minnesota Statutes Chapter 414 that does not provide for a hearing; or where the right to object has been waived, or where a hearing is not necessary due to a joint filing as provided for by law. The Director reviews and approves uncontested proceedings monthly or bimonthly as needed, depending on the volume of petitions received. Expedited review is available when requested for good cause.

Contested Proceedings

Includes proposed boundary adjustments filed under any section of Minnesota Statutes Chapter 414 that requires a hearing, or where a hearing is required upon the receipt of a timely objection as provided for by law. A hearing date is scheduled within 30 to 60 days after receipt of initiating documents filed.

Parties may notify Minnesota Planning in writing of intent to invoke mediation and binding arbitration within 30 days of an initiating document or a timely objection. (This option has been available since May 1997; it has never been used.) If this option is not exercised, then:

Local Meetings, Subdivision 16

The Director reviews the file and considers invoking either Minnesota Statutes section 414.01 subdivision 16, which requires parties to meet locally at least three times during a 60-day period and report back to the Director the results of those meetings or mediation. Extensions of this time period may be obtained, at the discretion of the Director if circumstances warrant. The Municipal Board had frequently used this section of the statute.

Mediation

The Director could invoke mediation at the beginning of a proceeding, or after Minnesota Statutes section 414.01 subdivision 16 meetings prove unsuccessful. If mediation is invoked, the parties have input as to the kind of mediation process chosen. Mediation options include: parties choose their own mediator; a mediator assigned by the Office of Dispute Resolution working with the boundary adjustment staff; or the parties could contract for mediation services provided by the Office of Administrative Hearings.

If parties disagree on preference of mediation, the file is sent to the Office of Dispute Resolution for assignment.

Hearing

The Director may send a file directly to hearing at any time, either at the beginning of a proceeding, or after unsuccessful local meetings or mediation. Again, the parties have input as to which decision-making path they prefer, including arbitration or an administrative hearing pursuant to Chapter 414. If the parties disagree on the type of hearing, the Director or designee will either conduct the hearing, or the matter will be delegated to the Office of Administrative Hearings for assignment of an administrative law judge.

Decisions

Decisions are no longer made in public. The Director, administrative law judges and arbitrators, as individual decision-makers, are not subject to the open meeting law. All hearing processes are still open to the public but the deliberation, or act of deciding a case, is no longer required to be done at a public meeting.

Uncontested proceedings are decided at a staff meeting after review by the Director. Contested proceedings have been decided in private by the presiding decision-maker, whether it be the Director, administrative law judge or arbitrator.

Written approvals or orders are then issued and served on all involved parties and designated recipients.

Appeal

There is a right of appeal following either of the available hearing options. However, depending upon the kind of hearing, the right of appeal differs markedly.

In an appeal from an arbitration under Chapter 572, the grounds for appeal are limited to challenging actions of the arbitrator or the absence of an arbitration agreement, and therefore, the jurisdictional authority of the arbitrator. This is a limited scope of appeal. The underlying evidence upon which the decision is based is not available for challenge in this kind of appeal.

Appeals from an administrative hearing conducted under Chapter 414 may challenge the underlying merits of the decision. The scope of this appeal is very broad. Not only can the result or decision itself be challenged, various aspects of the evidence, as well as the jurisdiction of the decision, may be challenged on appeal. Parties prefer the hearing procedures of Chapter 414, in part because of its broad scope of appeal.

SECTION III: URBAN AND NON-URBAN TOWN POWERS

At the outset of this project, we were informed by the Rice Lake Town Board that its current status is that of an “urban town.” We were asked to explore the differences between urban and non-urban towns. The majority of information in this section was prepared by Peter Tiede and Troy Gilchrist, Attorney, for the Minnesota Association of Townships.

One of the unique aspects of township government is the level of involvement township residents (“electors”) have in the operation of their community. At least once a year the electors are given the opportunity to meet and provide direction to the town board. Even though elector authority is reduced when a town adopts urban town powers, the residents continue to play a significant role in the operation of the township.

For the most part, town boards only have the powers granted them by the legislature. In much the same way, the legislature has indicated when and to what extent the electors are authorized to decide township matters. While in some cases the electors are authorized to actually decide an

issue for the town (e.g., setting the town's levy), elector authority usually takes the form of deciding whether to authorize the board to undertake a particular activity.

The instances when elector authorization is required are specifically mentioned in the statutes granting the town board the power to undertake the particular activities. In a sense, the legislature has installed stoplights on certain powers it gave town boards by requiring elector authorization. Unless a majority of the electors at an annual or special town meeting agree to give the board a green light, the board may not proceed to exercise that power. On the other hand, it is important to realize that authorizing an activity is not the same as mandating an activity. For example, elector authority is needed in a rural township in order for the board to buy grounds for a town cemetery (Minn. Stat. § 365.10, subd. 7). However, if the board is not interested in establishing a cemetery, elector authorization does not obligate the board to buy the grounds.

When a Township elects to become an urban township, it has access to three different types of powers:

- (1) Powers the township had before it became an urban township;
- (2) Powers the township had before it became an urban township but no longer require elector approval;
- (3) New powers that are enjoyed only by an urban township.

As mentioned, elector authority may only be exercised at the annual or a special *town* meeting. Electors are not authorized to make motions or take other actions at regular or special *board* meetings or at town hearings. The public should be given an opportunity to speak at board meetings, but the board controls these meetings and may impose reasonable restrictions on public input (e.g., setting time limits on speaking).

For the most part, what may be done at the annual meeting may also be done at a special town meeting (Minn. Stat. § 365.52, subd. 1). This gives rise to the question of whether a decision made at one town meeting may be changed at a subsequent town meeting. As with board decisions, there is a point where a decision of the electors may not be modified. For instance, the decision may have been relied upon by another, the activity may have already been carried out, or a deadline reached that does not allow further modification. In the meantime, an opportunity may exist for the electors or the board to attempt to change the decision. One area where such changes occasionally occur is in modifying a levy set at the annual meeting.

When the state experienced flooding problems some years ago, a number of townships needed to seek an increase in their levy to adjust for the unexpected drain on township funds. These boards called special town meetings to submit the proposed levy increase to the electors for their approval. Once the increase was approved, the board had until five working days after December 20 to recertify their levy to the county auditor (Minn. Stat. § 275.07, subd. 1).

Because there are no established limits on how often special town meetings may be called, a potential for abuse exists for those on both sides of a controversial issue. Towns have experienced competing attempts to alter decisions made at a previous town meeting. When the dispute eventually ends, it usually leaves behind hard feelings that run very deep among people of the township. Because there are few legal boundaries on attempts to change elector decisions, the only way to avoid potentially disastrous situations is for both the electors and town boards to

refrain from abusing their authority to pursue such changes. No one will argue the township form of government is perfect, but it has worked in this state and these United States since their inception. Furthermore, keep in mind that these disputes would not occur if, as in other forms of government, the residents were not given a say in what occurs in their community.

The following is a chart which compares the three types of powers between urban and non-urban towns. These lists are not exhaustive. We have not tried to inventory all town powers, nor have we tried to find powers that can be combined to create equivalents to powers expressly granted. This chart is intended as a quick reference for attorneys and town officers who are interested in determining the potential benefits of assuming urban town powers, or who wish to find if a certain urban town power is available in their town. Specific legal questions should be directed to your attorney or to the Association of Townships.

I. Similar Powers That Urban Towns And Non-Urban Townships Share

Description	Urban Town Power	Non-Urban Town Power
Acquire Property	1. Has the power to acquire private property within or without its limits by eminent domain for any purpose for which it is authorized by law to take or hold property by purchase or gift. It may also acquire property by eminent domain a right of way for sewerage or drainage purposes, and an outlet for sewerage or drainage within or without its limits. Minn. Stat. § 368.01, subd. 27.	“Any town may exercise the right of eminent domain to acquire private property within or without the limits of the town for the purpose of carrying out the authority provided in this chapter, including obtaining the right of way for sewerage or drainage purposes and an outlet for sewerage or drainage within or without the town limits.” Minn. Stat. § 444.26, subd. (2).
Animals	2. Has the power to regulate the keeping of animals, restraining their running at large. Minn. Stat. § 368.01, subd. 13.	A township board, by ordinance, may license and regulate the presence or keeping of dogs or domestic animal pets. Minn. Stat. § 366.01, subd. (2).
Board of Health	3. Has the power to establish a board of health with all of the powers of a board of health under the general laws. Minn. Stat. § 368.01, subd. 14(5)(b).	The board of health may authorize a township board to establish a board of health and delegate the powers and the duties of the board of health. Minn. Stat. § 145A.07, subd. (2).

Description	Urban Town Power	Non-Urban Town Power
Bonds	4. Issue bonds or other obligations to acquire or better warning systems. Minn. Stat. § 366.095, subd. 2.	Any town may issue bonds for the acquisition and betterment of town halls, town roads and bridges, nursing homes and home for the aged, and for the acquisition of equipment for snow removal, road construction or maintenance, and fire fighting for the acquisition of the development rights in the form of conservation easements under Chapter 84C, and for the acquisition and betterment of any buildings to house and maintain town equipment. Minn. Stat. § 475.52, subd. 4.

Description	Urban Town Power	Non-Urban Town Power
Buildings and building codes	<p>5. Regulate by ordinance the construction of buildings. Minn. Stat. § 368.01, subd. 18.</p>	<p>General zoning authority including “by ordinance regulated on the earth’s surface, in the air space above the surface, and in subsurface areas, the location, height, width, bulk, type of foundation, number of stories, size of buildings and other structures, the percentage of lots which may be occupied, the size of yards, and other open spaces . . . The uses of buildings and structures for trades . . .” Minn. Stat. § 462.357, subd. (1).</p> <p>Further, all Towns may adopt and administer state building code- In Minn. Stat. § 16B.60 the definition of 'municipality' was amended in 2001 legislative session to include towns.</p> <p>Hazardous buildings: Under Minn. Stat. § 463.151 "the governing body of any city or town may remove or raze any hazardous building or remove or correct any hazardous condition of real estate upon obtaining the consent in writing of all owners of record, occupying tenants, and all lien holders of record.... Under 463.16, the governing body of any city or town may order the owner of any hazardous building or property to correct or remove the hazardous condition of the building or property or to raze or remove the building.</p> <p>Under Minn. Stat. § 463.161, the town may correct or remove the hazardous condition or building and the cost of which shall be charged against the real estate as provided in 463.21 -- essentially the 429 process for special assessments.</p>

Description	Urban Town Power	Non-Urban Town Power
Drains	6. Has the power to establish and maintain drains. Minn. Stat. § 368.01, subs. 3(1) and 3(2).	“Has the power of a drainage authority to repair a town drainage system located within the town.” Minn. Stat. § 103E.701, subd. 3.
Entertainment, Gambling	7. Has the power to, by ordinance, prevent license, and regulate circuses, theatrical performances, the keeping of billiard tables and bowling alleys. Minn. Stat. § 368.01, subd. 16(1). License, regulate, or prohibit gambling and gambling devices. Minn. Stat. § 368.01, subd. 16(3). Minn. Stat. § 368.02, subd. 16(2) - Prohibit gambling and gambling devices.	By ordinance, prohibit or license and regulate the keeping of billiard, pool and pigeonhole tables, games of amusement, games of skill,” in addition to “circuses, shows, theatrical performances” Minn. Stat. § 366.01, subd. 2.
Hospital Board	8. Has the power to provide hospitals, and create a hospital board to operate the hospital. Minn. Stat. § 368.01, subd. 8.	Any two or more townships may create a hospital. Minn. Stat. § 447.31, subd. 1. Each hospital district is governed by a hospital board. Minn. Stat. § 447.32, subd. (1).
Purchase Equipment	9. Has the power to issue certificates of indebtedness within debt limits to purchase fire, street construction and street maintenance equipment. Minn. Stat. § 368.01, subd. 23.	Issue bonds for the acquisition and betterment of town roads and bridges, and for the acquisition of equipment for road construction or maintenance and fire fighting. Minn. Stat. § 475.52, subd. 4.

Description	Urban Town Power	Non-Urban Town Power
Sewage	10. Provide for and regulate the disposal of sewage. Minn. Stat. § 368.01, subd. 14(3) [subd. 14(4)]	To acquire, develop, construct, reconstruct, extend, and maintain storm and sanitary sewers and systems, including outlets, holding areas and ponds, treatment plants, pumps, lift stations, service connections, and other appurtenances of a sewer system, within and without the corporate limits. Minn. Stat. § 429.021, subd. (2).
Tourist Camps, Automobile Parking	11. Has the power to acquire, improve and operate tourist camps and automobile parking facilities. Minn. Stat. § 368.01, subd. 7.	“May establish and maintain public tourist camping grounds.” Minn. Stat. § 450.19.
Town Debt	12. The urban township board may issue certificates of indebtedness within debt limits to purchase police and ambulance equipment. Minn. Stat. § 368.01, subd. 23.	Any town may issue bonds for the acquisition and betterment of town halls, town roads and bridges, nursing homes and home for the aged, and for acquisition of equipment for snow removal, road construction or maintenance, and fire fighting for the acquisition of the development rights in the form of conservation easements under Chapter 84C, and for the acquisition and betterment of any buildings to house and maintain town equipment. Minn. Stat. § 475.52, subd. 4. See Also Certificates of Indebtedness - Minn. Stat. § 366.095.

Description	Urban Town Power	Non-Urban Town Power
Violation of Ordinance	13. Has the power to declare that any violation of an ordinance is a penal offense and describe penalties for it, but these penalties may not exceed the penalties of a misdemeanor. Minn. Stat. § 368.01, subd. 22.	“Declare that a violation of an ordinance is a penal offense and prescribe penalties for violations.” Minn. Stat. § 366.01, subd. 10. No penalty shall exceed that of a misdemeanor. <u>Id.</u>

II. Similar Powers That Urban Towns And Non-Urban Townships Share, Except That In The Case Of The Non-Urban Town, The Consent Of The Electors Is Required

Description	Urban Town Power	Non-Urban Town Power
Acquire Structures	1. Has the power to construct or acquire structures for town purposes. Minn. Stat. § 368.01, subd. 2.	“[t]he electors may let the town board buy or build a town hall or other buildings for the use of the town.” Minn. Stat. § 365.10, subd. 6. The township board may enter into contracts that are necessary to buy the building. Minn. Stat. § 365.14.
Cemetery	2. Has the power to acquire cemetery ground and sell lots. Minn. Stat. § 368.01, subd. 5.	“[a] town’s electors may vote to let the town buy, condemn or receive a gift of land within the town to be used as a cemetery.” Minn. Stat. § 365.26, subd. (1). The electors may also let the township board set up a program to sell lots. Minn. Stat. § 365.10 subd. 10.

Description	Urban Town Power	Non-Urban Town Power
Crime	3. Has the power to suppress vice and immorality, prevent crime, protect the public and private property, benefit the residence, trade and commerce, and the promotion of health, safety, order, convenience and general welfare by ordinance that are consistent with the laws of the United States. Minn. Stat. § 368.01, subd. 19.	The electors may grant the town board the authority to provide for: “(b) the suppression of vice and immorality; (c) the prevention of crime; (d) the protection of public and private property; (e) the benefit of residence, trade, and commerce; (f) the promotion of health, safety, order, and convenience, and (g) the general welfare.” Minn. Stat. § 365.10, subd. 17.
Fire Department	4. Has the power to establish a fire department and provide fire apparatus. Minn. Stat. § 368.01, subd. 9.	The electors, at a town meeting, may direct the town board to provide for fire protection and to keep up fire apparatus. Minn. Stat. § 365.15. The board can enter into any contracts to get, operate, and keep up the fire apparatus. Minn. Stat. § 365.16.
Garbage Disposal	5. Has the power to provide for and regulate the disposal of garbage and other refuse. Minn. Stat. § 368.01, subd. 14(4). In fact, urban towns have an obligation to provide solid waste collection services. Minn. Stat. § 115A.941.	“The electors may let the town board find a way to collect and get rid of household wastes and other refuse.” Minn. Stat. § 365.10, subd. 15. A township may issue license to collect solid waste. Minn. Stat. § 115A.93, subd. (2). Towns with populations over 5,000 have an obligation to provide solid waste collection services. Minn. Stat. § 115A.941.

Description	Urban Town Power	Non-Urban Town Power
Parks	6. Has the power to establish, improve, ornament, maintain and manage parks, parkways and recreational facilities. Minn. Stat. § 368.01, subd. 24.	The electors may let the town board buy grounds for a public park, and care for and beautify the parks. Minn. Stat. § 365.10, subd. 8.
Restrain Animals	7. Has the power to restrain animals running at large. Minn. Stat. § 368.01, subd. 13.	The electors may make orders to restrain the running of horses, cattle, sheep, swine, and other domestic animals from running at large on town roads. Minn. Stat. § 365.10, subd. (3). They may also make orders on the impounding of animals that are running at large. <u>Id.</u> In addition, the electors may let the town board pass an ordinance for licensing dogs and cats, keeping them from running at large. Minn. Stat. § 365.10, subd. (13). Finally, the electors may decide to establish a pound and where it will be located. Minn. Stat. § 365.10, subd. 1(a).
Roads	8. Has the power to open, pave, change, widen, grade, repair and maintain roads. Minn. Stat. § 368.01, subd. 3(1).	“[t]he electors may let the town board, by resolution, determine whether to open, or maintain town roads.” Minn. Stat. § 365.10, subd. 11. In addition, “[t]he electors may vote money to repair and build roads and bridges.” Minn. Stat. § 365.10, subd. 4.

Description	Urban Town Power	Non-Urban Town Power
Snow and Ice Removal	9. Has the power to require real estate owners to remove snow and ice. Minn. Stat. § 368.01, subd. 4.	At the annual township election, the board may submit to the electors a vote if they should require property owners to remove snow and ice off an adjacent town road or right of way. Minn. Stat. § 366.016, subd. (1).
Water Supply	10. Regulate, by ordinance, wells and other means of water supply. Minn. Stat. § 368.01, subd. 6.	Any municipality may build, construct, reconstruct, repair, enlarge, improve, or in any other manner obtain (i) waterworks systems . . . Minn. Stat. § 444.075 (also defining towns as municipalities). See also Minn. Stat. § 471.371.

III. Powers That Are New To A Township When A Township Elects To Become An Urban Town

When a town becomes an urban town, the board is given a set of powers that can be exercised without elector approval. Division Of Authority In Urban Towns, Minnesota Association of Townships Handbook, May, 1995. The new powers an urban town can exercise include:

Description	Urban Town Power	Non-Urban Town Power
Canals, Sewers	Establish and maintain canals, and sewers. Minn. Stat. § 368.01, subd. 3(2).	Non-urban townships have power to create sewer systems under Minn. Stat. § 429.021, subd. 1(2).
Dead Bodies	Regulate by ordinance the disposal of dead bodies. Minn. Stat. § 368.01, subd. 5.	
Economic Development	Contributions to regional or local organizations. A home rule or statutory city or town described in section 368.01, subdivision 1 or 1a, may appropriate not more than \$50,000 annually out of the general revenue fund of the jurisdiction to be paid to any incorporated development society or organization of this state for promoting, advertising, improving, or developing the economic and agricultural resources of the city or town. Minn. Stat. § 469.191. Urban Towns may also exercise other economic development authority under Minn. Stat. §469.152 et. seq.	
Nuisances	Define nuisances and provide for their prevention or abatement. Minn. Stat. § 368.01, subd. 15.	

Description	Urban Town Power	Non-Urban Town Power
Protect Foliage	Regulate by ordinance the protection of trees and shrubs in the town. Minn. Stat. § 368.01, subd. 4.	**
Public Utilities and Improvements	Minn. Stat § 429.011, Subd 2 includes urban towns in the list of towns that have full municipal powers.	Note that Minn. Stat. § 429.011 Subd. 2a provides various powers to non-urban towns as well, and, by references to Minn. Stat. § 429.021, incorporates many of the traditional public works projects typically undertaken by towns.
Regulate Grounds	Regulate the street and public grounds by ordinance to prevent encumbrances. Minn. Stat. § 368.01, subd. 3(4).	**
Restrain Merchants	Restrain or license and regulate auctioneers, transient merchants and dealers, hawkers, peddlers, solicitors and canvassers. Minn. Stat. § 368.01, subd. 11.	**
Riding Academies	License and regulate riding academies. Minn. Stat. § 368.01, subd. 13.	**
Sidewalks	Lay, repair or improve sidewalks, paths, and cross walks. Minn. Stat. § 368.01, subd. 3(4).	
Slaughterhouses	By ordinance, regulate slaughterhouses and prevent unwholesome substances from being brought into the township. Minn. Stat. § 368.01, subds. 14(1) and 14(2).	**
Taxicabs	Regulate taxicab drivers by ordinance. Minn. Stat. § 368.01, subd. 12.	**
Town Streets	Rename or renumber the town streets. Minn. Stat. § 368.01, subd. 10.	

**Similar authority may be granted to a non-urban town by the electors at the annual meeting Minn. Stat. §365.10.

Description	Urban Town Power	Non-Urban Town Power
Town Management	Create departments and advisory boards and appoint town officers, employees, and agents for the management of town affairs. Minn. Stat. § 368.01, subd. 20.	General powers to employ are found throughout the statutes. See, for example, Minn. Stat. Chap. 353.
Vacation	By resolution vacate all or part of any street, alley, public ground or way on its own motion or by motion by the majority of the owners of the land abutting the street alley, public grounds, public way, or part or be vacated. Minn. Stat. § 368.01, subd. 25.	Only upon petition (Minn. Stat. §164.07) or abandonment (Minn. Stat. §164.06).
Water Obstructions	Provide for the cleaning and removal of obstructions from waters. Minn. Stat. § 368.01, subd. 14(5).	
Water Courses	Alter, widen, or straighten water courses. Minn. Stat. § 368.01, subd. 3(3).	

SECTION IV: MINNESOTA PROPERTY TAX SYSTEM

Rice Lake officials requested that a section be included in this report that addresses financial impact regarding incorporation and annexation including tax impact, levels of services and related issues. The MIC does not have financial experts on its staff so a detailed discussion of Rice Lake's particular financial situation will not be undertaken. However, the MIC will provide a general overview of the local tax structure in Minnesota and how it relates to services and form of government.

Minnesota's property tax system is one of the most complex in the country. Because of extensive changes in the system it has become even more complicated in the last five years. It is a process that is difficult to explain and understand. Unfortunately, this topic must be addressed because property taxes are a major source of revenue for local governments.

Property tax rates in Minnesota vary considerably between localities. This is because the system treats different types of property and different types of taxpayers differently through a complicated classification system. Many officials and levels of government are involved in its administration and each parcel of property is taxed by multiple jurisdictions. The major taxing bodies are the township or city, school district and county. Other taxing bodies include such entities as mosquito control districts and other special districts. In Minnesota, the county collects all property tax payments and distributes the funds accordingly to each taxing district.

Whether the form of local government is a city or township has only a small impact on property tax rates. The issues that have the most impact on rate changes from year to year are the following:

- Intergovernmental aid;
- The cumulative total of local (city or township), county, school and other tax rates;
- Level of services provided;
- The number of commercial and industrial properties in the jurisdiction;
- Changes in total assessed valuation from year to year.

The Impact of Intergovernmental Aid

A considerable portion of local revenues comes in the form of intergovernmental aid. Data from the State Auditor's office show that in 1996, 30% of cities' and 40% of counties' revenues came from state and federal aid. In 1997, 38% of townships' revenues came from this source. And in 1994, the percentage of school districts' revenues coming from these sources was nearly 70%, although this percentage may have changed significantly because of recent changes in the ways that schools are funded. While intergovernmental aid provides a significant amount of a local unit's revenue, it can fluctuate from year to year depending on decisions made at the state and federal levels. This fact adds more uncertainty each year to how much revenue will need to be raised from property taxes. With the changes in 2002, the property tax will become much more

of a city/township/county tax. Before reform, city, township and county levies made up just over half of the total property tax levy and schools made up about 45 percent. After reform, the city/township/county share of the total levy will rise to 70 percent and the school share will fall to about 25 percent. Moreover, the school levies will reflect local (not state) spending choices.

Local Government Aid

A representative of the Minnesota Department of Revenue (DR) was consulted regarding local government aid (LGA). According to this person, recent changes in legislation have resulted in the fact that townships will no longer receive state aid. The representative stated that in 2001, Rice Lake Township received approximately \$95,000 in state aid. The DR uses a complex formula for computing aid levels. The general rule of thumb is that the poorer a city is, the more aid it will receive from the state. The DR representative performed a rough calculation to approximate how much aid Rice Lake would receive in 2002 if it were a city. One of the larger factors for determining the level of aid is the percentage of homes built before 1940. At the time of our discussion, the 2000 census numbers for this factor were not available, so 40% was used as an example. Based on this percentage, Rice Lake would have received *roughly* \$68,000 in 2002 if it were a city. If the percentage of homes built before 1940 is less than 40%, this amount would go down, and vice-versa.

Calculating Property Tax

In Minnesota, a business property not only pays more property taxes than a residential property because of its value, but it also pays at a much higher *rate*. To illustrate how important commercial and industrial properties are to a local tax base, we can run through a couple of examples.

Step 1: Assess the property

The county assessor establishes a value for the property. This is the assessor's estimate of the property's selling price. Each spring, property owners receive a "notice of valuation" in the mail for each piece of property they own.

We will compare the amount of property tax paid on an \$86,000 home and a \$1,000,000 big box commercial property such as a Wal-Mart or Best Buy.

Step 2: Classify the property

The use of ownership of the property determines its "property tax classification." Each class of property (i.e., home, apartment, cabin, farm, or business) is taxed at a different percentage of its value. This percentage—or "class rate"—is set by state law. The estimated market value is multiplied by the appropriate percentage (class rate) to determine the home's "tax capacity."

Most single-family homes in Minnesota are categorized as a "residential homestead." The class rates used for our example house are:

First \$500,000 = 1%
 Over \$500,000 = 1.25%

Calculate tax capacity as follows:

Value x Class Rate = Tax Capacity
 \$86,000 x .01 = \$860

Most commercial and industrial property have the following class rates:

First \$150,000 = 1.5%
 Over \$150,000 = 2%

As above,
 \$150,000 x .015 = \$2,250
 + (1,000,000-150,000) x .02 = \$17,000
 Tax Capacity = \$19,250

Step 3: Prepare a Local Budget

During the first half of the year, local officials prepare a budget for the coming year. As part of the budget process, local elected officials estimate the cost of services they intend to provide. This budget must be approved by the city council for cities, the town board for urban towns and by the voters for non-urban townships. (A township cannot spend more than its approved budget in a given year while there are methods for city administrations to do so in certain cases.)

The proposed *tax levy* (total dollars to be raised with property taxes) is computed by subtracting estimates of state aid and revenue from other sources (i.e., building permits, user fees, interest income, fines, etc.) from estimated budget needs.

The net *tax rate* for a local unit is computed by dividing the tax levy by the total net tax capacity of all properties in the jurisdiction. Each individual's tax bill is equal to the property's tax capacity times the tax capacity rate. The local tax rate is the percentage charged to the property owner and will reflect the combined tax levies of all jurisdictions governing each piece of property.

As an illustration of step 3, consider Anywhere City and our two property owners. Anywhere City's council determines that to provide the services they want at the desired level, they will spend \$100,000. State aid and other revenue (fines, user fees, interest income, etc.) for their city totals \$25,000, leaving them with \$75,000 to raise through local property taxes (tax levy):

Budget	\$100,000
State Aids and revenues	<u>-\$25,000</u>
Tax Levy	\$75,000

In Anywhere City, the total tax capacity for all the properties in the city is \$250,000. The tax rate is then calculated by dividing the tax levy by the tax capacity to obtain a percentage.

Calculate tax rate as follows:

$$\begin{array}{lcl} \text{Tax Levy/City's Tax Capacity} & = & \text{Tax Rate} \\ 75,000/250,000 & = & .30 \text{ (a tax capacity rate of 30\%)} \end{array}$$

Once the tax rate is calculated, each property in the city is taxed at that percentage of its tax capacity. So, for our example house, the property tax for Anywhere City would be calculated by multiplying the house's tax capacity times the tax rate.

Calculate property tax as follows:

$$\begin{array}{lcl} \text{House owner Tax Capacity (\$860) x Tax Rate (.30)} & = & \text{Property Tax} \\ \$860 \times .30 & = & \$258 \end{array}$$

So the property owner pays the city an *effective tax rate* of \$258/\$86,000, or 0.3%.

Next, we will calculate the property tax for the big box retailer:

$$\begin{array}{lcl} \text{Big Box owner Tax Capacity (\$19,250) x Tax Rate (.30)} & = & \text{Property Tax} \\ \$19,250 \times .30 & = & \$5,775 \end{array}$$

The Big Box owner pays the city an effective tax rate of \$5,775/\$1,000,000, or 0.58%.

So the big box owner's tax rate is almost twice the homeowner's rate. The total taxes paid by the big box would be equal to approximately 22 homestead properties worth \$86,000 each.

HOWEVER, what we have calculated is only a portion of the total property tax bill for these two property owners.

Step 4: Overlapping Governments

All levels of local government (i.e., county, school district, mosquito control districts, etc.) also determine their tax levies and tax rates; these amount to additional taxes for each property owner.

So, in our example, if the county has a 25 percent tax rate, the school district 55 percent, and special taxing districts 5 percent, the total property tax rate will be 115 percent. This total tax rate, multiplied by the taxable value, determines the final tax bill. Tax rates as a percentage of tax capacity vary considerably between localities. For taxes payable in 2002 in St. Louis County, the rates ranged from 90% in the City of McKinley to 247% in the City of Kinney. (Rice Lake Township's rate was about 162%).

To complicate the tax calculations, a new state property tax has been added this year for commercial, industrial and seasonal recreational residential classes. This tax revenue will go directly in the general state fund which may or may not be redistributed to local jurisdictions.

To complicate it even further, voter-approved referenda levies are applied to the market value of each parcel, not tax capacity. As a result, each identically-valued parcel, regardless of the property's use, pays the same amount of referenda taxes (with the exception of certain agricultural and seasonal recreational properties, which are exempted from referenda taxes). In 2002, two counties, 32 cities and 272 school districts levied market value-based levies. These communities must have a separate calculation for a market value referenda levy by the total taxable market value of each community.

[parcel market value] * [market value tax rate] = [market value tax bill]

[tax capacity tax bill] + [market value tax bill] = [total tax bill]

Complexities of Local Property Tax Rates and Levels of Services Provided

There are so many variabilities in the system, along with dramatic changes that take effect this year, that making wholesale comparisons between jurisdictions will not likely be meaningful. This section will attempt to discern some very general patterns among local jurisdictions.

It is often assumed that when more services are provided, property taxes will increase. This is not necessarily the case because service providers usually charge user fees which account for a significant portion of the cost of providing the service. For example, the portion of revenue from property taxes for townships in Minnesota is near 60%. For cities, it is only about 20%. This is the case because cities on average provide many more services than townships. About half of cities' revenue comes from user fees from providing services while this source provides only about 20% of township revenue.

A general pattern can be discerned regarding *local* tax rates in Minnesota. It appears that townships in Minnesota with very small populations and very few services provided have the lowest local tax rates. Large cities such as Duluth tend to have somewhat higher local rates. Local property tax rates in townships and cities similar to Rice Lake tend to be higher still. In fact, in 2002 Rice Lake and Hermantown both had higher local rates than Duluth. One reason for this occurrence is the fact that Duluth has a much larger commercial and industrial base and these properties pay a large portion of the tax bill, as shown in the previous example, leaving the residents with a smaller share of taxes to pay. Duluth provides many more services than Rice Lake or Hermantown, but user fees and the commercial and industrial properties more than offset the cost of providing the services.

(For cities within the seven-county Twin Cities metropolitan area and on the Iron Range, tax levies are reduced by an amount of property tax revenue derived from the

metropolitan and range area *fiscal disparities programs*. These programs attempt to decrease the variability of local tax rates by shifting tax revenues from cities with large bases of commercial and industrial property to those with few of these types of properties.)

The changes for 2002 referenced above will lower local tax rates for homes and businesses, but larger businesses will continue to pay higher rates than small businesses. Because the percentage change in the gap of tax rates between large and small businesses will decrease, the impact will differ on communities based on its ratio of small to large businesses in each community; the larger the share of small businesses the lesser the impact will be on local communities.

Changes in Assessed Valuation and Property Tax Intricacies

The technical details of computing property taxes mask many other intricacies of the property tax system. Many communities over the past several years have experienced situations where individual property taxes rise much faster than the increase in the levies that are certified by local units of government.

The most common factor which results in an increase in an individual parcel's tax is the change in the parcel's estimated market value. Without any change in local levies, a property owner can experience a tax increase due almost exclusively to any valuation increase. The Legislature frequently changes the classification system. Changes to the classification system can shift property tax burdens from one type of property to another. Commercial, industrial and apartment properties received significant reductions in their class rates between 1997 and 2002. This shifts tax burden to other classes of property that did not receive class rate reductions. In an effort to minimize the effect of these shifts, the legislature reduced school levies across the state and created the Market Value Homestead Credit. This credit reduces property taxes for homesteads by 0.4 percent of the homestead's market value up to a maximum \$304. The state will reimburse local governments for the amount that this credit reduces their tax receipts.

Economic factors that may affect broad classes of property can also influence the overall tax changes for individual parcels of property. For example, in the early 1990s the Twin Cities metropolitan area experienced major declines in the valuation of commercial and industrial properties. These valuation declines shifted taxes from property classified as commercial and industrial to all other types of property. Valuation declines also may have accentuated the levy changes by local units of government.

A 2002 law change exempted agricultural and cabin property from voter-approved referenda levies. In some jurisdictions where these types of property are a significant part of the tax base, this change shifted taxes onto other classes of property.

SECTION V: OPTIONS AND RECOMMENDATIONS FOR RICE LAKE

In the last 10 years, only two townships in situations similar to Rice Lake have become incorporated cities in Minnesota. These are Oak Grove in 1993 and Grant in 1996. Other incorporations involved different circumstances: The City of Forest Lake and Forest Lake Township merged in 2000; St. Augusta Township incorporated, but only after some of its land was transferred to the City of St. Cloud; and most recently, the Cities of Pleasant Lake and Rockville, along with Rockville Township, merged to form one city.

I talked to representatives of both Grant and Oak Grove that were present at the time of incorporation. Both persons that I spoke with were ambivalent towards their experiences with becoming a city. On one hand, they stated that the city seems to have better secured its borders and neighboring jurisdictions would have a much more difficult task of annexing its land. Also, the city has more control over what happens within their boundaries. On the other hand, they felt that despite incorporation and counter to their expectations, they have no more control over growth issues than they had as a township.

This is a different situation than that which Rice Lake faces. Both of the communities I have used as examples are located on the urban fringe of the Twin Cities metropolitan area, which is experiencing tremendous growth. Rice Lake is growing, but does not have the growth pressure that these two communities face.

Nevertheless, townships like Rice Lake are caught in a catch-22 situation. Their populations are large enough that some services need to be provided, but not large enough to provide the most efficient delivery of services that will spread the cost to enough residents in order to bring down tax rates. Also, the population is not large enough to attract enough businesses to offset a large portion of the tax bill. Of course, many residents moved to Rice Lake because they like the fact that there are fewer people and businesses. The tradeoff appears to be higher local property taxes. Again, this does not necessarily mean that the *overall* property tax rates will be higher because school, county and other taxes must be added to the total.

This issue largely explains why Rice Lake and other communities in similar situations are questioning their township status; they need to add more residents and businesses if they want to provide more services and/or reduce property taxes. But adding more residents and businesses may detract from the rural lifestyle that many in the township value.

Unfortunately, this report is being prepared at a time when the ultimate effects of recent changes remain unknown. As discussed above, the major overhaul of both the municipal boundary process and the property tax system has made the entire situation very unstable. The full effects of the changes will not be known for several years.

Options:

Incorporation of Rice Lake

It appears that the most likely benefits to be received from this action are the achievement of securing the current boundaries of Rice Lake and the restoration of receiving state aid. There are instances in the past where a neighboring city has annexed some land from another. This process is more difficult, however, when both entities are incorporated. Receiving state aid may be attractive to Rice Lake, but the amount can fluctuate year to year and the state legislature frequently changes formulas for all distributions. These benefits would have to be weighed against the costs of incorporation and any animosities generated among neighboring jurisdictions.

The process of incorporation can be time consuming and costly. It would be made more difficult if there is dissent from a neighbor, especially Duluth, because of its size and influence. Also, the local government would have to convert to a municipal government with city council members and a mayor. Those currently on the town board, if interested, would have to run for election in the new style of government. There also would be one time costs of converting to a city government (changing references from “township” to “city” on letterhead, ordinances and other legal documents, buildings, public works equipment, fire trucks, etc.). Just as urban towns have more legislative powers than rural towns, cities have more legislative power than townships. However, the powers as outlined in Minnesota Statutes are complex and not easily determined. If Rice Lake were to become a city, it is very likely that it will feel the need to hire more staff (at the very least, a city administrator) to conduct the day-to-day operations of the City.

Partial Incorporation of Rice Lake

Rice Lake could choose to pursue incorporating just the southern, more developed portion of the township which has a developing commercial and industrial base and where services are most likely to be in demand. This would most likely lower the residential tax rate in this area. This may not be an attractive option, however, because the northern, unincorporated portion of the township would lose this tax base and have to rely almost exclusively on residential properties to handle the tax burden, leaving relations between the two communities strained.

Do Nothing (Remain a Township)

This may be an attractive option. As referenced above, both the state tax structure and process of incorporating are in a state of flux at the moment. It may be prudent to stay current with how these events change in the next several years and revisit this question in the future.

Annexation Agreement with Duluth

The township could enter into an agreement with Duluth where the City would annex portions of the Township as it urbanizes and as sewer, water and other services become available. This would provide for orderly growth in the area, although the township would continue to occupy less and less land as time goes on. This option would only be available, of course, if Duluth is interested.

Annex Entire Township into Duluth

Again, this is only an option if Duluth is interested. This is probably less likely to happen than an annexation agreement because Duluth would have to provide services to a much larger area than it does currently. At this time, Duluth is struggling to provide enough services to its current population that is distributed at a low density and spread out across 68 square miles. Although Duluth has some relatively high density neighborhoods, it also has many large areas of undeveloped land. As of the 2000 census, Duluth has the lowest population density of the 19 largest cities in Minnesota (1,269 persons per square mile).

Merge with Another Township and Incorporate as One City

This option is the least likely to occur. The first step would be to get a neighboring township to agree to this concept. Second, St. Louis County would have to agree to merge the townships into one. Finally, the combined entity could then approach Minnesota Planning regarding incorporation. Probably the biggest benefit of this idea is that the new city, with a population over 5,000, would be eligible for the Municipal State Aid-Street Fund. However, it is extremely unlikely that Minnesota Planning would approve this request when it is obvious that the main purpose of merging and becoming a city is to obtain more funds from the state. The Minnesota Statutes clearly lay out the reasons and justification for becoming a city. Merely obtaining more state funding is not one of them. Several years ago, with its population having dropped below 5,000, the City of Eveleth attempted to annex neighboring Fayal Township to boost its population back above 5,000. After a short hearing, the judge reached a quick decision and did not approve the case because of this situation.

Recommendations:

1. Regardless of the course the Township wants to pursue, the most important thing to do at this point is conduct informal meetings with City staff from Duluth in order to find out what, if any, their intentions are. Members of the ARDC staff could act as facilitators for this process and the meetings could be held at ARDC's office. The first section of this report makes it clear that, at the moment, cities have the upper hand over the interests of townships. Any course that Rice Lake wants to pursue most likely will have to be approved by Duluth. So it is important to engage the City early on and attempt to work out an agreement. As was mentioned earlier, only about 5% of boundary disputes are contested and have to be resolved in St. Paul. In the vast majority of cases, the parties come to an agreement on their own.
2. At this point, it does not appear that Rice Lake has a lot to gain by becoming a city. The legislature created the urban town concept precisely for townships like Rice Lake, that is, growing towns in need of more services. Rice Lake already has many of the legislative powers of cities. Here are just a few examples: zoning power, the ability to define nuisances and provide for their prevention and abatement, regulate by ordinance the protection of trees, regulate by ordinance taxicab drivers, rename or renumber the town streets, etc.

An urban town can also contribute funds to regional or local economic development organizations for promoting, advertising, improving or developing the economic resources of the town and can also join the Minnesota League of Cities and receive the full range of League services. In fact, in the League's *Handbook for Cities*, it is stated that, for the most part, the material in the handbook can also be applied to urban towns.

Among the few powers that urban towns may not exercise are the following: annexing abutting land; owning or operating gas, heat, light or power systems; establishing a municipal liquor store and establishing a civil service system.

Restoring Local Government Aid (LGA) may make this option more attractive. However, as was mentioned earlier, the legislature frequently changes formulas for distribution of revenue. The outlook for next year's state budget does not look good at this point. The Department of Revenue representative stated that he expects that there will probably be more cuts in LGA during the next session. It does not seem beneficial to stake the future of a community on a small, unstable revenue source.

Against this backdrop are the costs of incorporation including: a long, expensive process, the likelihood of an increase in administrative expenses, and the possibility of negative consequences with regard to Rice Lake's relationships with its neighbors.

For these reasons and depending on the results of recommendation number one, it appears that Rice Lake already enjoys most of the advantages of being a city and it may not be worth the costs involved at this point to pursue incorporation.

3. Stay informed on further changes to the boundary adjustment process and property tax system changes. Revisit these issues again when changes are initiated or at least every several years. At some point in the future, depending on changes to these processes and changes to the township itself, it may be prudent to again consider incorporation.
4. If the Township wants to get a complete financial assessment to determine the full impact of incorporation, hire a financial consultant and/or attorney with the expertise to take a detailed look into Rice Lake's finances and to research the intricacies of converting to a City.

Sources of Information

City Limits: A Report to the Minnesota Legislature on Municipal Boundary Adjustments
– Minnesota Planning

Taxes: Where Does the Money Go? – Scott Loveridge, Liz Templin, Carole Yoho and
Nancy Lenhart

Property Taxation 101 – League of Minnesota Cities

Division of Authority in Urban Towns – Troy Gilchrist, Attorney

Chart of Urban and Non-Urban Town Powers – Peter Tiede

Toward Accountability in State and Local Financing – Minnesota Taxpayers Association

Minnesota Highway Financing – Minnesota House of Representatives Research
Department

History of Municipal Boundary Adjustments in Minnesota – Minnesota Planning

St. Louis County Auditor

Minnesota Statutes

Minnesota Department of Revenue

