HOUSE RESEARCH | Short Subjects

Pat Dalton October 2002

City Local Government Aid Program (LGA)

LGA provides general purpose aid to cities

LGA has two purposes—to provide property tax relief and to ensure that cities can raise sufficient revenues to meet their needs (excluding schools). LGA is the state's largest program of general-purpose aids to local governments. It was created in 1971 as part of a major reform of the state/local finance system. It replaced a variety of categorical aids and "shared tax" programs. Although the original program made payments to all nonschool local governments, it is now paid only to cities.

At $586.8 million in 2003, city LGA is the largest noncategorical state aid program

Distribution of LGA 1975-2003				
	LGA Payments (in millions)			
Calendar Year	**Counties**	**Cities**	**Towns**	**Special Districts**
1975	$31.3	$93.0	$13.9	$0.6
1980	22.0	208.3	15.4	0
1985	14.5	264.9	9.4	0
1990	7.5	337.2	2.2	0
1995	0	336.1	3.2	0
2000	0	394.4	3.6	0
2001	0	411.0	3.8	0
2002	0	565.0	0	0
2003 (certified)	0	586.8	0	0

The city LGA appropriation increased substantially between 2001 and 2002 to partially offset the loss of city homestead and agricultural credit aid (HACA) payments that were eliminated as part of a property tax reform.

The LGA appropriation increases annually for inflation

Unlike many state aid programs, the city LGA appropriation automatically increases every year for inflation, measured by the implicit price deflator (IPD) for state and local government purchases. The annual increase cannot be less than 2.5 percent or greater than 5.0 percent, regardless of the actual change in the IPD. For aids payable in 2003, for example, the IPD was only 0.67 percent but the LGA appropriation increased by 2.5 percent.

The current LGA formula has been in place for eight years

The current method for distributing city LGA was adopted in 1993. The factors and coefficients used in the formula were based on an analysis by the League of Minnesota Cities to identify appropriate measures of city "need."

Earlier formulas had used property tax levies as a proxy for "need." Those formulas also contained a "rolling grandfather" provision. This meant that cities were guaranteed to receive at least as much aid in the current year as they had received in the previous year. This "rolling grandfather" led to some major inequities in payments between cities over time.

LGA consists of two parts—base aid and formula aid

The amount of aid a city receives in any year under the current program consists of two parts: an amount determined by the formula and a "base" amount (also known as "grandfathered" aid). Any increases in the LGA appropriation are usually distributed via the formula; the base aid generally does not increase.

Base aid usually does not grow and is equal to a city's aid in 1993

The base aid is equal to the amount of aid each city received in 1993 in LGA and a couple of other aid programs. Unlike the "rolling grandfather" in previous formulas, the base amount does not increase for any city unless specifically provided for in legislation. Over the years, adjustments have been made to base amounts paid to individual cities to deal with special needs and circumstances that are not accounted for in the formula. Examples include unusually high sewer conversion costs, sudden and dramatic tax base loss, and overburdens in large regional centers that provide services to the surrounding rural population.

When the current LGA formula was first enacted, base aid made up $320 million of the $330 million total LGA appropriation. In 2003, base aid accounts for $360.4 million of the $586.8 million LGA appropriation.

Formula aid is based on city "need" minus "ability to pay"

Each city's formula aid is equal to a percentage of the difference between its "need" and its "ability to pay." This difference is often referred to as "unmet need." A city's "need" is based on four factors:

- population
- population decrease
- percent of its housing built before 1940, and
- percent of its tax base that is classified as commercial or industrial

A city's "ability to pay" is equal to the city's tax capacity multiplied by the average city tax rate.

A city's LGA amount can increase and decrease over time

The amount of aid a city receives under the formula can vary over time depending on changes in its need factors and its tax capacity. Because the appropriation is capped at a specific amount each year, the amount of formula aid a city gets is also dependent on its "unmet need" relative to the "unmet need" in other cities.

A city's LGA payment may not be less than its base aid amount. There are also limits on aid increases in any year. The percent increase in LGA payments to the cities of Minneapolis, St. Paul, and Duluth, may not exceed the percent increase in the total LGA appropriation for that year. The LGA increase for any other city may not exceed 10 percent of the city's property tax levy in the previous year.

For more information: Contact legislative analyst Pat Dalton at 651-296-7434. Also see the House Research publication, *Restructuring of State Aid to Minnesota Cities*, October 1993 with December 1994 addendum.

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