LMC LEAGUE of MINNESOTA CITIES

Fiscal Disparities 101

INFORMATION MEMO

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Local government units within the Twin Cities metropolitan area have participated in the Metropolitan Fiscal Disparities tax base sharing program since 1975. The metropolitan area is Anoka, Carver, Dakota, Hennepin, Ramsey, Scott, and Washington counties. A similar program began in 1996 for local government units in the Taconite Area. This area includes portions of St. Louis, Itasca, Crow Wing, and Aitkin counties, and all of Lake and Cook counties.

Under these programs, local government units contribute a portion of the growth in the value of their commercial, industrial, and public utility property to a tax base sharing pool. Each community receives a distribution of property value from the pool based on the market value and population of each city.

Contribution

The contribution to the pool is 40% of the growth in commercial, industrial, and public utility value since the base year (1971 for the Twin Cities; 1995 for the Taconite Area). This measure of growth includes both new construction and inflationary increases in existing property values.

For payable 2021, for example, the total amount of tax capacity contributed to the metropolitan fiscal disparities pool was $499 million. The contribution value is not available for local tax purposes. Therefore, the contribution value must be subtracted from the total tax capacity of each community before the local tax rate is computed.

The Taconite Area program is much smaller. It had roughly $20 million of tax capacity contributed for payable 2021.

Distribution

The tax capacity contributed to the pool is based on a distribution index. This index compares each city's total market value per capita to the average market value per capita for all cities and towns in the seven counties. Cities that have relatively less market value per capita receive a relatively larger distribution from the pool than cities with greater market value wealth per capita.

How are property taxes generated?

The tax capacity contributed to the pool becomes property tax dollars for each local government. These property taxes are called the distribution levy. To determine this levy, the local government multiplies its distribution value by its prior year tax capacity rate. The distribution levy represents the amount of each local government's certified levy raised through the fiscal disparities program. The balance of the certified levy is used to compute the local tax rate.

How are commercial/industrial and utility parcels taxed?

Commercial and industrial properties are not taxed twice. Instead, part of each commercial or industrial property's tax capacity is taxed at the area-wide tax capacity rate and the balance is taxed at the total local tax rate.

For example, in a community that contributes exactly 40% of all commercial, industrial, and utility property to the fiscal disparities pool:

- 40% of each parcel's value is taxed at the area-wide tax rate.
- 60% is taxed at the total local tax rate.

For taxes payable in 2020 (most recent data available) the Twin Cities area-wide tax rate was 142.454% and the Taconite Area-wide tax rate was 166.551%.

Policy issues

The Legislature originally had six objectives for the program:

1. Provide a way for local governments to share resources generated by regional growth.
2. Encourage orderly urban development by reducing competition for commercial and industrial development.
3. Establish incentives for regional cooperation.
4. Make regional resources available through the existing system of local governments.
5. Make resources available to communities at the beginning stages of development or redevelopment.
6. Encourage environmental protection.

Descriptions of the program often highlight two main goals that encapsulate several of the original objectives:

1. Promote orderly urban planning and development.
2. Work toward a more equitable distribution of fiscal resources.

Assessment of the program's success in accomplishing the second goal often points out "winners" (cities that are net recipients) and "losers" (cities that are net contributors).

Proponents of the program focus on:

- The relative uniformity of commercial and industrial property taxation across the metropolitan area.
- The stability the cities that are net contributors provide to the region as a whole.

They argue that greater uniformity and stability give the entire region a competitive edge in national and global marketplaces.

Critics of the system argue that:

- The 40% contribution rate is arbitrary.
- The distribution formula is solely based on the relative property tax base wealth of each city.

- The formula uses non-adjusted assessment levels.
- Cities with high assessment levels contribute more tax base than cities with lower levels, which creates a disincentive to raise the assessment level.

Additional resources

These additional resources can help cities understand more about property taxes and fiscal disparities:

Minnesota House Research write-ups on property tax

Information about tax base sharing in the metro area on The Metropolitan Council's website

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