

Open Government in Minnesota

An Agenda to Support Greater Transparency and Taxpayer Participation in Local Budgeting Processes

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About the Minnesota Taxpayers Association

The Minnesota Taxpayers Association was founded in 1926 for the purpose of disseminating factual information that will educate and inform all Minnesotans about Minnesota tax and spending policies. For eighty-five years, the Association has advocated for the adoption of sound fiscal policies through its research efforts, publications, and meetings.

The Association is a non-profit, non-partisan group supported by membership dues. For information about membership, call (651) 224-7477, or visit our web site at www.mntax.org.

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Introduction

I. Introduction

This is a white paper about government transparency and understanding property taxes. There are many publications and resources designed to educate and inform taxpayers about their property taxes. Non-profit organizations such as the MTA, local and county assessment offices, and other advocacy organizations have published guides and other useful information to help taxpayers navigate and understand what is generally regarded to be the most complex and confusing form of taxation. These resources do a good job of discussing all the interconnected pieces of the property tax system and how they work.

But ultimately local government spending drives property tax levies and, in turn property taxpayers' bills. This is the most influential piece of the property tax system. It is also the most important and – in many ways – the most challenging element for taxpayers to understand.

“The ultimate purpose of this transparency agenda is to open opportunities for citizens to engage officials and become involved in local decision-making processes...”

In this white paper we examine issues affecting the ability of property taxpayers to make informed judgments about local spending and the use of property tax dollars. We identify three requirements for taxpayers to be able to prudently and independently evaluate the efficiency and cost effectiveness of government operations. We discuss issues relevant to these requirements and provide recommendations for improving both the transparency of government operations and taxpayers' understanding of proposed property tax changes.

We call this white paper “open government” because the ultimate purpose of this transparency agenda is to open opportunities for citizens to engage officials and become involved in local decision-making processes. Greater civic understanding of and participation in government is not just the sign of a healthy democracy, it is also a requirement for ensuring confidence and trust in the public sector. Creeping cynicism, suspicion and anger towards government only thrives in a context of ignorance and confusion.

Our analysis and recommendations are based on MTA local government and property tax research and on interviews and information obtained through the NAIOP Nexus taskforce working group.

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Obtaining a Complete and Accurate Understanding of Local Government Cost Structures

II. Requirement #1: Obtaining a Complete and Accurate Understanding of Local Government Cost Structures

Open Government starts with gaining a full understanding of the cost structures and drivers of local government spending.

Government spending can be presented to taxpayers in two ways. The first is by “program area” such as public safety, parks and recreation, etc. This provides information on the amounts local governments spend on various types of public services, and how big a share of the budget each area of government comprises. Trend information is also typically provided to see how program size has changed over time. All local governments typically do a very good and thorough job of providing this information.

Program area reporting can allow citizens to make judgments about how their tax dollars are being allocated to various public services. It gives taxpayers a sense of local government priorities with respect to the use of revenues. But it provides little ability to answer questions about why spending growth is occurring or any perspective on the efficiency or merit of how tax dollars are actually used within these program areas.

The second way to present government spending is by expenditure class or “object code.” Such a presentation provides information on what tax dollars are actually purchasing: such as salaries and benefits, fuel, contracted services, etc. Object code reporting provides critical information on the actual cost structures within government spending and important insights into why budgets and overall spending may be growing.

“Understanding labor cost components and trends are a foundation for understanding property tax drivers.”

This is especially true with respect to labor costs. Government service delivery is a labor intensive enterprise, with labor costs commonly comprising 60%-80% of local operating budgets. Labor cost “object codes” would include salary, health care, retirement, and possibly many other types of fringe benefits. Understanding labor cost components and trends are a foundation for understanding property tax drivers.

Unfortunately, object code information can be challenging to get. The Office of the State Auditor (OSA) provides data that is the gold standard in Minnesota for comparing governments’ budgets and obtaining spending trend information. The OSA facilitates taxpayer reviews by providing a tool that allows for comparisons between multiple years for the same jurisdiction or for comparisons between two different jurisdictions. Spending data is presented by program area, so consumers of the information can easily understand what the costs of doing certain things are, such as providing public safety protection or maintaining and repairing streets and highways; and how those have changed over time. But the OSA does not collect or report spending by object code, and so their information provides no insights as to what those costs reflect or why and how they are changing.

Taxpayers wanting an understanding of cost structures must turn to government budget documents themselves. Many, if not most governments will provide summary object code information. But this information is often of limited use in assembling and assessing the “story” of local government decision-making: Common problems include:

- Combining object code spending items together, effectively hiding important detail. For example, a very large line item “personnel services” will include spending on all salaries, health care, pensions and a variety of other benefits. This is problematic because the growth rates for salaries versus benefits are generally very different.
- A lack of multi-year data – no ability to evaluate trends and growth rates
- A lack of information on employee counts – making it difficult to determine what role changing employee totals may have had in these spending changes

In addition, government budgets typically lack the descriptive detail needed about these object code elements to facilitate taxpayer analysis, benchmarking, and comparisons. For example, spending on government employee health care is a function of both the generosity of the benefit package and the amount of premium cost the government employer is assuming. Similarly, changes in salary spending are often a function of negotiated salary structures and cost of living adjustments. Such important contextual information is seldom found in budget documents but rather must be mined separately from a review of employment contracts – which may or may not be provided elsewhere on government websites.

The challenges of understanding government cost structures are often exacerbated by financial management practices. For example many governments, especially larger ones, utilize “internal service funds” to account for goods or services provided by one department to another on a cost reimbursement basis. This is a well-established budgetary practice. The problem is that dollars moved through internal service funds have been transferred from another government fund. Without careful accounting, those dollars can be counted as revenues and expenditures twice during the same year, even though the government only raises and spends the money once. This practice distorts the true cost of government operations.

Additionally, spending from internal service funds is sometimes labeled as payment for “services” implying the use of outside vendors – even though the services themselves are provided by government employees. This distorts spending by categorizing payment of salaries or payment for supplies as payment for “services” instead.

It is important to note that complex financial management practices and budget reporting practices that omit important information and context should not be interpreted as intentional efforts to confuse taxpayers. Citizens are not the primary audience for government budgets and financial statements. These documents are principally designed to serve the internal needs of public sector managers as well as auditors who ensure accountability in the appropriation and disbursement of funds. Nevertheless, reporting efforts can be enhanced to allow taxpayers greater access to necessary information on the reasons for spending growth.

Recommendations

- 1. Counties and cities with a population of 2,500 or more should be required to report spending to the Office of the State Auditor (OSA) both by functional area and by object code. The OSA should report on both types of spending.**

Obtaining a Complete and Accurate Understanding of Local Government Cost Structures

Although we are wary of imposing another mandate on local governments, we believe that reporting of this data is essential to facilitate greater taxpayer understanding of local budgets and budget trends.

We also believe that as long as the state continues to play an active role in the subsidization of local government service delivery through aids to local governments, it is even more imperative for all state taxpayers to be able to have access to information on the cost structures of local governments around the state.

The OSA already has a recommended set of object codes for local governments to use so no work needs to be done to develop a reporting structure. We encourage an object-based reporting system similar to that developed by the Minnesota Department of Education and employed by Minnesota's school districts.

2. Access and visibility of key features and details of public employee contract provisions must be made readily accessible to facilitate taxpayer review, analysis, and benchmarking among other local units of governments.

We recommend that countries and cities with a population of 2,500 or more must provide information on the following for public review:

- **Employee health plan features, premium costs, and employer cost sharing arrangements**
- **Other fringe benefit plans and features**
- **Wage agreements and their budget implications, including the projected compounding effects of any longevity increases and cost of living adjustments and related benefit costs over the life of the contract**
- **Other key contract features such as workforce rules that may have a substantive and material effect on the cost of local service delivery**

Reporting of this nature on local government internal affairs is not without precedent: for example, the state requires large cities to notify residents of their three highest paid employees.

It is also worth noting that salary and benefits information is currently collected on a survey basis by the League of Minnesota Cities and the Association of Minnesota Counties and is used internally for salary and benefit comparisons across local governments. However, access to this information is limited to their own members and others willing to pay a sizable fee (MTA paid \$1,000 for access in 2009). Our objective in this recommendation is to make this type of reporting comprehensive, uniform, mandatory and readily available to the general population.

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Enabling Taxpayers to Assign Property Tax Responsibility to Appropriate Parties

III. Requirement #2: Enabling Taxpayers to Assign Property Tax Responsibility to Appropriate Parties

Property tax aid and credit reductions have large potential influences on the local property tax levy. Government officials are sure to highlight the impact these changes are having on levy decisions – and justifiably so. But the qualifier “potential” is important because local officials are still in control of most of the spending decisions driving the levy, regardless of what the state may or may not do.

However, there are two primary circumstances where spending destiny lies outside of local government control. The first arises in state mandates, the second in labor arbitration. Open government requires that taxpayers be able to understand these issues and their implications for local spending decisions.

Mandates

Mandates are legal, constitutional, statutory or administrative rules imposed on one level of government by another; as such they restrict local governments’ authority. Mandates take a variety of forms from regulating the activity of government to requiring the provision of certain services. With regard to service delivery, mandates can be categorized into three broad categories:

1. The local government is obligated to provide a particular service using a specific method and/or at a specific level (for example, the election services provided by counties)
2. The local government is obligated to provide a particular service, but has discretion regarding the method used to provide the service and/or the level at which the service is provided (for example, recycling services)
3. The local government is not obligated to provide a particular service, but if it does is obligated to use a specific method and/or at a certain level

Mandates can be conditional in nature – they can require that governments perform certain actions in order to receive aid or funding or to be granted certain authority.

“Mandates are particularly troublesome because they blur the lines of responsibility”

There are various reasonable and rational public policy grounds for imposing mandates on local units of government. However, mandates can add to the cost of operating local governments by introducing complexity and inefficiency to the administration of public services. The cost impacts are intensified when the mandate is “unfunded” – i.e. when a local government is required to provide a certain service but is not given any (or enough) funding to offset the cost. Mandates are particularly troublesome because they blur the lines of responsibility; for example, citizens angry about rising county spending can complain to the county’s board of commissioners. But if the root cause of the spending increase is higher human service costs being passed along by the state, their complaints are being directed to the wrong elected officials.

For county governments alone, officials have suggested that the number of mandates likely number “in the thousands”¹. Many mandates are likely to be process-oriented and highly

¹ “Counties get change to revise unfunded mandate”, Minnesota Public Ratio, January 18, 2010.

procedural in nature and unlikely to trigger major cost burdens that factor into property tax bills. On the other extreme are mandates pertaining to the delivery of significant human service programs and “maintenance of effort” requirements which are major property-tax cost drivers. For example, Ramsey County’s approved 2011 budget includes \$275.9 million – over 47% of the operating budget – for health and human services programs; most if not all of which are federal and state mandates. Human services costs have been a huge property tax cost driver in recent years: in 2004 the county levied \$81.5 million for health and human services programs; in 2011 the county plans to levy \$100.2 million for the same purposes – a nearly 23% increase in the levy over only seven years.

In an ideal world, some comprehensive list of local government mandates and their costs could be readily accessed. Unfortunately, this is far from an ideal world, and a comprehensive list is not available in one place. Minnesota law does provide local governments the opportunity to propose reform of state mandates by written resolution to the State Auditor², who is obligated to list the mandates cited in these resolutions on the OSA website.³ Notably, as of this writing there are over 80 mandate categories that cities alone have identified as needing reform or repeal. Mandates affecting county and school operations simply add to property taxpayer exposure.

Compounding this issue is the fact that many mandates have costs which are difficult to measure. For example, four counties and two cities have filed resolutions with the State Auditor regarding “prevailing wage” provisions which govern compensation for publically-financed construction projects. However, there is no specific line item in a local government budget for “prevailing wage costs”.⁴ This means that measuring the cost of mandates often involves making assumptions and creating hypothetical (“what if?”) scenarios. Such issues make it very difficult to estimate the overall cost of mandates to local government.

Nevertheless, the implications state mandates have on local government spending decisions and cost structures are very real and very significant. At a minimum it is essential to educate taxpayers on their existence and their implications; if for no other reason than the only way reforms can be enacted is if enough critical mass for change is created.

Labor Arbitration

As previously discussed, labor contracts can have profound implications for the cost structures of local government. Minnesota’s Public Employment Labor Relations Act establishes the ground rules for negotiations between representatives of Minnesota’s public employees (unions) and government employers (management).⁵ Public employee unions negotiate contracts with government employers that set the terms of employment; including salary and most fringe benefits.⁶

² Minnesota Statutes § 6.79.

³ And the OSA does so at <http://www.osa.state.mn.us/default.aspx?page=MandateReformProposals>.

⁴ We have discussed the prevailing wage issue at length in *Minnesota Public Sector Compensation: Part 2* available from the Minnesota Chamber of Commerce and NAIOP-Minnesota, and in *Prevailing Wage Rates in Minnesota* available from the Associated Builders and Contractors – Minnesota Chapter.

⁵ Minnesota Statutes, Chapter 179A.

⁶ Minnesota Statutes § 179A.03, Subd. 19 specifically prohibits the negotiation of pension benefits; these are instead set through the legislative process.

Enabling Taxpayers to Assign Property Tax Responsibility to Appropriate Parties

PELRA provides that, in most cases where labor and management cannot agree on a contract, the two negotiating sides may jointly enter into “interest arbitration”. For “essential”⁷ employees, the union can unilaterally initiate interest arbitration so long as the state’s Bureau of Mediation Services⁸ (BMS) rules that good-faith bargaining has occurred and that the sides are at an impasse. Interest arbitration is a specific type of “binding” arbitration, meaning that both sides are required to accept the arbitrator’s ruling. BMS makes arbitrators’ rulings public (see http://www.bms.state.mn.us/arbitration_awards.html).

“Arbitration rulings can result in higher labor costs than locally elected officials would desire to impose on property taxpayers...[and deserve] much greater taxpayer scrutiny...”

Arbitration rulings can result in higher labor costs than locally elected officials would desire to impose on property taxpayers. These rulings are therefore deserving of much greater taxpayer scrutiny than they currently receive. Two particular dimensions of public sector arbitration have the potential to tilt the landscape in favor of decisions resulting in higher labor cost structures – the strike/selection process of choosing an arbitrator and the benchmark comparisons employed.

The strike/selection process is one of several ways an arbitrator may be selected for dispute resolution. In this process, each side involved in the arbitration takes turns eliminating arbitrator candidates from a pre-existing roster until the required number of arbitrator(s) remains. There are no guidelines governing “strikes” by the sides. The strike/selection process is not designed to generate the selection of the best arbitrator (although this may happen anyway); instead, it is designed to select the arbitrator who is least objectionable to the two parties. Since over 900 government entities negotiate with about 20 unions in Minnesota, becoming “objectionable” to one union has the potential to be more detrimental to an arbitrator than becoming “objectionable” to one government – creating at least the perception that the system has a built-in bias in favor of outcomes more friendly to labor.

Of greater concern is the benchmark comparisons employed for resolving contract disputes. The general practice is to compare the salaries, benefits, and other compensation of the employees in the contract dispute with employees in comparable positions with comparable employers. Benchmarking to “comparable employers” generally limits the arbitrator’s focus to the same job titles in the public sector without any reference to non-governmental labor markets from which employers also draw their recruits. Essentially, this practice entails that any increases in pay successfully negotiated by unions in nearby or comparable cities will be the basis for an arbitrator’s decision. Arbitrators in public sector contract dispute generally give little weight to local private-sector labor markets.

Local governments will differ in their negotiating skills, abilities, and stridency in defending of taxpayers’ financial interests. Taxpayers should be able to readily assess how well their financial interests are being represented in these circumstances. In addition, the results of collective bargaining arbitration may trump the efforts of local government officials to control cost structures in a reasonable and prudent manner. It is important to ensure that principles of open government and full transparency also apply to these critical decision-making situations.

⁷ “Essential” employees, broadly speaking, are those public employees engaged in public safety, health care, or supervisory positions. The full definition is at Minnesota Statutes § 179A.03, Subd. 7.

⁸ The Bureau of Mediation Services is the state agency tasked with organizing and overseeing arbitrations, as well as recordkeeping.

Recommendations

1. Local officials should identify, describe, and to the extent possible quantify the cost impacts of state mandates on local government operations and notify residents accordingly either through the local government's primary website and/or as part of the local government's budget documents

Although the OSA's repository of mandate reform proposals provides good information on various concerns of local governments, it is not familiar to taxpayers, nor does it provide relevant cost information. Local governments have a direct interest in providing this information directly to their constituents since necessary reforms will only come once taxpayers mobilize. Of primary concern are those mandates which 1) have a tangible and substantive impact on local government expenditures; 2) are not fully funded by state government; and/or 3) involve cross-subsidization by local property taxes. Such issues include but are not limited to:

- Implicit rate subsidies for early retiree health care
- Mandated increases in employer contributions for underfunded retirement plans
- Maintenance of effort and other cost sharing requirements

2. Results of contract negotiations and binding arbitration decisions should be prominently featured in local government budget documents

3. Reform PELRA to allow offers and counteroffers during union negotiations to be made publically available for review during the negotiation process

4. Labor arbitrators should be required to consider total compensation and prevailing benefit levels and trends offered in the private sector in their arbitration decisions

5. The state should evaluate the public sector arbitration process and biennially assess public sector binding arbitration award trends compared to private sector wage and compensation trends

Gaining Insights on Government Efficiency, Performance, and Cost-Effectiveness

IV. Requirement #3: Gaining Insights on Government Efficiency, Performance, and Cost Effectiveness

“Information about the quality and cost-efficiency of the services local government provide is equally important.”

Traditional financial statements and budget documents do not provide all the information taxpayers require to determine how well local governments are serving their needs. Information about the quality and cost-efficiency of the services local governments provide to taxpayers is equally important.

Over 20 years ago, the Government Accounting Standards Board (GASB)⁹ launched a major investigation into ways to improve governments’ ability to present information that monitors and assesses government operations. The objective was to find ways to provide information not only on how much and on what government spends its resources but also what taxpayers got from the use of public funds and how efficiently and effectively funds were used. In the summer of 2010, this initiative culminated with the release of suggested GASB guidelines for Service Efforts and Accomplishments (SEA) Reporting – a complement to traditional government financial reporting.

According to GASB, reporting of SEA performance information “better meets the needs of users of government financial information by enhancing both accountability and transparency of governments who report this information.”

SEA reporting includes information about the services provided and the degree to which government is achieving its outcomes and performance objectives. Absent SEA-type performance information, it is difficult to know how efficiently government services are being provided and how effective those services are in helping the government to achieve its goals.

The foundation of SEA reporting is connecting government spending with measureable performance benchmarks. Governments develop indicators that relate cost (dollars and/or employee hours) to measures of actual service results, especially indicators that consider the quality and outcome of the service. At its fullest potential, large-scale adoption of SEA reporting would facilitate taxpayer benchmarking of local government operations as well as assist in the identification of best practices in service delivery.

Several local governments in Minnesota have already embarked on ambitious performance measurement and reporting initiatives. Two excellent examples of such work are the City of Minneapolis’ Results Management (<http://www.ci.minneapolis.mn.us/results-oriented-minneapolis/index.asp>) and Woodbury’s Performance Measurement Program (<http://www.ci.woodbury.mn.us/govt/capm.html>). An expansion of such efforts across the state combined with efforts to ensure a level of consistency and comparability – two essential qualitative characteristics for SEA reporting according to GASB – would provide taxpayers with the information they need to judge how closely local governments are operating to their efficiency frontier.

⁹ GASB determines the generally accepted accounting principles (GAAP) used by state and local governments across the United States – essentially setting the accounting rules for governments. Its mission is “to establish and improve standards of state and local governmental accounting and financial reporting that will: result in useful information for users of financial reports; and guide and educate the public, including issuers, auditors, and users of those financial reports”.

Recommendations

- 1. State government should develop and adopt a Service Efforts and Accomplishments reporting infrastructure to supplement traditional state financial reporting**
- 2. State government should also create a supporting infrastructure for SEA reporting among city and county governments. The state can encourage these efforts either through incentives like grants to implement such reporting system – a strategy proposed in the 2010 legislative session. Conversely, the state could withhold a portion of general purpose aids and credits from governments unwilling to embark on these transparency-enhancing reporting efforts.**

Concluding Remarks

V. Concluding Remarks

Budget cuts, increasing demand for services and slower economic growth are converging to produce extraordinary fiscal stress on both citizens and their governments. But this convergence has also stressed the relationship between citizens and their governments.

Restoring confidence and trust in government is inexorably linked to transparency in government. All Minnesotans are capable of developing an understanding of their government and being effective participants in decision-making processes. But it is contingent on providing the necessary information and facts to make informed judgments about where, how, and how well tax dollars are being used.

Pursuing an open government agenda and the recommendations contained in this white paper is a starting point for allowing citizens to reengage in their local governments and participate in the development of policies and practices in support of the common good.

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