

City of Minneapolis

Minnesota



Cost of Services Analysis and Fee Methodology May 2013

Prepared by: Finance and Property Services Department in cooperation with City staff

Information Compiled By:

Name	Department
Sandy Christensen	Finance and Property Services
Brett Hjelle	Public Works
Maren Anderson	Public Works
Vicki Stone	Public Works
Lee Larson	Regulatory Services
Henry Reimer	CPED
Kristin Guild	CPED
Wes Butler	CPED
Paula Mazzacano	Finance and Property Services
Luke Scardigli	Fire
Robin McPherson	MPD
Daniel Huff	Health Department
Becky McIntosh	Health Department
Joel Fussy	City Attorney
Chris Carlson	Convention Center

Cost of Services Analysis and Fee Study

Contents

Background 1

Cost Analysis – General Methodology 2

Project Process and Methodology 4

Summary of Results 9

Page left blank intentionally.

Background

The City Council of the City of Minneapolis, Minnesota directed City staff to review existing fees throughout the organization for correlation between the amounts charged for various fees and the cost of providing those services. There is both statutory and case law that regulates the issue of allowable licensing and permitting charges. Minnesota Statute 1300.0160, Sub. 2 states that building permit “fees established by the municipality must be by legal means and must be fair, reasonable, and proportionate to the actual cost of the service for which the fee is imposed.”

Relative to charging a fee for the issuance of licenses, Minnesota Stat. 116J.69 states that “it is the policy of the state of Minnesota that to the extent practicable, when required, a business license: Should involve payment of a fee in an amount no greater than specified by statute. If a fee is authorized by statute and set by rule, the fee shall be no greater than necessary to recover the administrative cost issuing or renewing the license or enforcing its terms and conditions.” In some cases, state statute dictates the maximum license fee that a municipality may impose as in the case of MN Stat. 340A.408, Subd. 3 which establishes maximum license fees that cities may impose for off-sale liquor stores; there are similar statutes that impose such restrictions for fireworks permits, vending machine licenses and other types of licenses and permits. MN Stat. 340A.408, Subd. 2(a) specifies that for on-sale liquor licenses, the “license fee is intended to cover the costs of issuing and inspection and other directly related costs of enforcement.”

Case law has arrived at the following conclusions:

- In order to be reasonable, a license fee should be intended to cover the expenses of issuing, the service of officers and other expenses directly or indirectly imposed or incurred and that a court will not declare license fees “unreasonable unless they are palpably so.”
- If the intent of a license fee is to raise revenue rather than cover costs, courts are likely to invalidate the fee.
- License fees may include money to pay for police services that are caused by a particular business, but the fees may not pay for general police service or protection.

Cost Analysis – General Methodology

There are several different methodologies that may be used when considering how to calculate appropriate fee amounts. There is a cost associated with all services provided by the City. It is this total cost that becomes part of the City’s annual budget. The cost of providing various services goes beyond the direct hourly rate of the staff member providing that service. In addition to this direct cost, the cost of employee benefits – including training and paid time off – may be considered part of the inherent cost of having that staff member available to provide the service. In other words, a potentially significant portion of an employee’s wages may be considered an indirect cost. Additionally, the costs of supervision, space, depreciation and other support costs may be considered an indirect, or a fixed cost, that is includable in calculating the cost of providing a service.

According to the League of Minnesota Cities (LMC), “many cities do not adequately calculate overhead charges in arriving at fees. For instance, [cities should include] costs such as insurance, utility the fair value of space, technology, employee benefits, supplies, fuel and other costs adequately captured when deciding how much to charge for city services.” In other cases, “often cities don’t calculate police costs in calculating fees”.¹ The LMC further provides suggestions for cost items to include in the calculation of service provision subject to cost recovery through a fees mechanism that suggest the following²:

Service	Fee Should...
Building Inspections	Cover all overhead costs
Liquor Licenses	Include police oversight
Gambling Licenses	Include costs to process
Zoning Fees	Include city council costs
Business licenses	Include inspection costs

¹ Grundhoefer, T., (2008) League of Minnesota Cities, *Alternative revenues: Beyond bread and butter*.

² Ibid.

The LMC provides further guidance in determining a methodology for establishing defensible fees as:

Step 1

Identify all direct costs associated with the building code administration [or other service provision] activities. These would include:

- Most, if not all, of the salary and benefits associated with staff involved directly in the building code administration [or other service provision] function;
- The annualized cost of supplies, equipment and materials associated with the building code administration [or other service provision] function.

Step 2

Identify the city's general overhead charges such as building costs, insurance, heating, sewer, water, fleet costs, IT costs, administration, finance and city council, and then allocate to the building codes administration [or other service provision] function, a proportionate share of these costs.

Step 3

Interview the other city departments to determine what percentage of those departments' time is reasonable related to supporting building codes administration [or other service provision] activities. Once that "time spent" evaluation is completed, allocate a percentage of the cost of those department budgets to the building codes administration [or other service provision] function. For example, the following departments are likely to devote at least some time to support building codes administration: Planning, zoning and development; engineering and public works; public safety (police and fire); and regulatory services.

Step 4

Arrive at an overall annualized cost to support the building codes administration [or other service provision] activities. This will be the total of the direct cost identified in Step 1, plus the allocation of the general city overhead identified in Step 2, plus the allocation of a percentage of other departments' time identified in Step 3.

Step 5 (Building Permit Fees only)

Since building permit fees must be based on valuation, the city must then make an estimate of potential valuation and set fees accordingly, to generate sufficient revenue to cover all or a portion of the costs calculated in Step 4.³

Project Process and Methodology

The genesis of the cost study and fees review stems from 2013 decision to not generally increase the Regulatory Services License Fee Schedule as part of the 2013 budget process, with the exception of the Pollution Control Annual Billing (PCAB) fees which were increased by 3%. At the time, it was determined that there was a possible disconnect between changes in the total amount of fees income proposed for the budget as compared to the actual receipts and the proposed increase in the individual fee activity as it related to the budget. As a result, the 2013 fee schedule was held flat with staff direction to review the existing fees structure and complete a comprehensive cost analysis to compare to the amount charged. The staff direction adopted as part of the 2013 budget process stated:

- o) Amend the Mayor's 2013 Recommended Budget to include the following staff directions:
 - a) City Departments are directed to work with the Finance Department to review and analyze the City's existing fee structure to determine fiscal relationship between cost of providing activities and ability to recoup costs. The study shall be complete by April 1, 2013, and presented to the Ways & Means/Budget Committee and the Regulatory, Energy & Environment Committee during their regularly scheduled meetings in April 2013.
 - b) City Departments are further directed to work with the Finance Department and City Attorney to incorporate the results of the fees study into the development of a methodology and process to support any proposed ongoing adjustments to existing fees. The proposed methodology and process shall be presented to both the Ways &

³ Merwin, P. (2005), League of Minnesota Cities, *Risk Management Information: Establishing building and development fees*

Means/Budget Committee and Regulatory, Energy & Environment Committee by June 30, 2013.

In response to this directive, Finance and Property Services (FPS) staff initiated a work group by contacting department directors on December 17, 2012 and requesting that a departmental liaison be identified as the point of contact within that department for work associated with the fees study. Once the workgroup was established, a kick-off meeting was held on January 14, 2013 to introduce the general concept of fees as a cost recovery mechanism and craft a work plan.

Staff members were first requested to complete an inventory of existing fees and charges for services performed. In addition to identifying activities that charge a fee, staff were encouraged to list unique services provided for which a fee was not currently charged, with the understanding that the costing of the activity differs from the decision to charge a fee to recover that cost. An interesting outcome of this exercise was the identification of a number of chargeable activities and their associated fees that are documented in ordinance, rather than a resolution-approved fees schedule which renders the fee amounts more cumbersome to change. The group recommended that the City work to remove fees from ordinance where possible and implement an enhanced fee schedule and annual approval process.

Once a universe of general chargeable activities was identified, staff members were asked to estimate the individual tasks required to complete the service activity and the approximate amount of staff time utilized in performing each task, as well as the class/title of position doing the work and the average hourly wage of the position. An average hourly wage for the position was determined most appropriate as in many cases one could not identify specifically which individual was completing the work as well as to account for staffing changes. An outtake of this exercise was the recognition that in many cases, activities for which the City charges require a cross-functional and cross-departmental effort, regardless of the area that was credited with the associated revenue. For example, the acquisition of a business license may require the completion and submission of an application which is received and documented by Community Planning and Economic Development (CPED) staff – this function was formerly in Regulatory Services and for the sake of this study was considered a Regulatory Services function in order to

cost out the service using 2012 actual amounts. The business may require a plan review by Fire Inspection Services to ascertain the occupancy requirements and a physical inspection may be necessary. Additionally, a background check of the owner may be necessary that could be performed by either staff in Business Licensing for drivers' license verifications or the Police Department for more extensive checks. All of these activities were deemed to be a direct function of providing the license, not just consideration of the department that had been associated with the cost-recovery income in the past.

Direct costs associated with performing a single unit of service delivery was determined using the method of time estimation noted above. Following the determination of direct cost, attention was turned to the identification and calculation of indirect costs associated with the support of the direct staff. For this study, indirect costs were deemed to include:

Non-service paid work time	Meetings and training time Paid holidays Paid sick time Paid vacation time
Supervision and Department Administration	Cost of Supervisor in unit (if identifiable) Cost of Support Staff Cost of Department Management Supplies (for example, office supplies) Contractual Service in support of staff (for example, consulting attorney, but not including services that are contracted out for direct service to customers – see pass through costs) Internal Service Charges (General Fund Overhead, BIS, SIF, Property Services)
City Indirect Charges	Internal Service Charges (if not already identified in the departmental budget) Equipment Depreciation

The total cost of each of the indirect costs was then compared to the total amount of employee compensation considered direct service to calculate a ratio of indirect to direct costs. For example, Department A has 24 employees of which 20 are similarly classified direct service staff:

Department A			
Expense Type	Total	Direct	Indirect
Annual Salary (2080 hrs @ \$25 x 20 staff)	\$1,040,000		
Direct Time (1750 hours/yr/staff)		\$875,000	
Meetings/Holidays/Sick/Vacation/staff/year (2080-1750)			\$165,000
Supervisor/Admin Staff/Dept Management	\$300,000		\$300,000
Fringe Benefits (~35% of Wages = .35 x \$1,340,000)	\$469,000		\$469,000
Supplies	\$200,000		\$200,000
Contracts	\$25,000		\$25,000
City Indirect Charges (ISF, Depreciation)	\$800,000		\$800,000
Totals	\$2,834,000	\$875,000	\$1,959,000
Split between direct and indirect		\$875,000	\$1,959,000
Ratio of indirect costs (\$1,959,000/\$875,000)			2.24

In this particular case, for each dollar spent on the direct wage of a staff member performing a service, the cost to the City, and the justifiable amount to charge, is the direct wage amount multiplied by 2.24 as reflected below:

Time to complete one application	30 minutes (or 0.5 hour)
Direct Wage Rate/hour	\$25
Direct Wage Cost attributable (0.5 hour * \$25/hour)	\$12.50
Indirect Ratio	2.24
Allowable charge	\$12.50 * 2.24 = \$28.00

In some cases, staff members were unable to discern the amount of direct time attributable to a specific activity when they were working on a general classification of services, such as general business licenses. This was particularly true with multiple staff working across various classifications of services. In this case, it was more efficient and as reasonably accurate to estimate the percentage of time spent by staff units on types of licensing and activities. For example, using Department A above, the 20 staff members are able to estimate that a certain percentage of their time is spent working on license type 1 and another percentage on license type 2 over the course of a year. The ratio of direct and indirect costs does not change. Rather,

the method to estimate the amount of time utilized to provide a single service is derived by the prorating the direct time based upon the number of service units as shown below:

Department A	
Total Staff Hours (20 staff @ 1750 direct hours ea)	35,000
% of Time Spent on License Classification 1	20%
% of Time Spent on License Classification 2	35%
% of Time Spent on License Classification 1 (35,000 * 20%)	7,000
% of Time Spent on License Classification 2 (35,000 * .35%)	12,250
# of Class 1 Licenses Issued	15,000
# of Class 2 Licenses Issued	18,000
Time per each Class 1 License (7,000/15,000)	.47 hour
Time per each Class 2 License (12,250/18,000)	.68 hour
Cost of Class 1 License Issuance (.47 * \$25/hour * 2.24)	\$26.32
Cost of Class 2 License Issuance (.68 * \$25/hour * 2.24)	\$38.08

The above methodology provides a mechanism to calculate the costs attributable to staff and support of staff providing services. In addition to direct service, the City performs some activities that require the use of outside expertise and services, as well as materials that may be directly linked back to a specific job or activity. In the case of water meter installation, the cost of the physical meter and supplies should be charged in addition to the cost of the staff person providing the service. In general, if the City is required to hire and pay for an outside contractor for the provision of service, these costs should be considered “pass-through costs”, be borne by the customer and invoiced appropriately.

Summary of Results

The study involved reviewing activities of a number of City departments. There are more than 1,000 fee-related and ancillary tasks that were identified as part of the analysis. Departments and activities included in the analysis include (but are not limited to):

Regulatory Services	<ul style="list-style-type: none"> • Animal Care and Control Fees • Traffic Control Fees • Fire Inspections (plan reviews and inspections) • Housing Inspections (VBR, rental licensing)
Community Planning and Economic Development	<ul style="list-style-type: none"> • Construction Code Services Fees (permits and inspections) • Loan Servicing Fees • Business Licensing • Development Services Fees (Zoning, Conditional Uses, Permits)
Health Department	<ul style="list-style-type: none"> • Lead and Healthy Homes-related Fees • Food, Lodging and Pool-related Fees • Environmental Health/PCAB Fees
Public Works	<ul style="list-style-type: none"> • Water Meter and Mains-related Fees • Rainleader Disconnect • Erosion Control, Excavation, Right-of-Way and Construction-related Permits • Event Permits • Plan Reviews • Parking-related Fees
Fire	<ul style="list-style-type: none"> • Plan Reviews • Inspections
Minneapolis Police Department	<ul style="list-style-type: none"> • Patrol costs associated with various establishment licenses • Background Checks

Fees and charges deemed punitive in nature are not included in the scope of this initial analysis. For example, administrative citations and associated fees are governed by separate statutory rules and legal requirements and are not necessarily directly related to the cost of providing a specific service. Additionally, other fees associated with assessments for property abatements and loss-of-use costs are not part of this analysis.