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Government Finance in Minnesota

Arley D. Waldo and Carole B. Yoho



Since the end of World War II, state and local governments across the nation have been deluged by demands for more and better public services. In Minnesota and elsewhere, these demands have caused sharp increases in government spending. And demands for more public services seem certain to continue.



Higher spending has placed severe pressures on the fiscal capacities of state and local governments. They have had to raise tax rates and broaden tax bases, add new taxes, increase borrowing, and seek additional federal aid.

Governmental units in Minnesota have been deeply affected by the rising demand for public services. The purpose of this article is to provide some basic information on government finance in the state.

GENERAL EXPENDITURE

State and local government spending in Minnesota almost doubled from 1957 to 1966, climbing from \$865 million to \$1,702 million.¹ Local government expenditure has continued to account for about two-thirds of total spending. In 1966, our more than 4,000 local governments spent \$1,158 million. Direct spending by the state government, which excludes state grants to local governments, was \$544 million.

The per capita general expenditure of Minnesota state and local governments was approximately \$476 in 1966.

¹ This estimate includes state expenditures for the fiscal year ending June 30, 1966, and local expenditures for the fiscal years ending between July 1, 1965 and June 30, 1966. (Fiscal years end in different months for some governmental units.) Unless otherwise indicated, all data on expenditure and revenue are from reports of the U.S. Bureau of the Census and exclude the income and outlay of insurance trust funds and publicly operated utilities and liquor stores. Because of differences in classification procedures and, in some instances, sampling variability, census data may not agree exactly with the amounts of revenue and expenditure reported elsewhere by state and local units.

This placed Minnesota 15th among the 50 states and 12.5 percent above the U.S. average of \$423. Per capita state-local spending is higher in Minnesota than in all neighboring states except North Dakota (table 1). However, this does not necessarily mean that Minnesota residents receive more or better state and local public services than the residents of states in which per capita spending is less.

Population growth has been partly responsible for more state-local spending. But per capita spending also has increased sharply. Average annual per capita expenditure jumped by almost 50 percent between 1957-59 and 1964-66 (table 2).

Part of the increase in per capita spending has meant an increase in the

Table 1. Per capita general expenditure of state and local governments, 1966

State	Per capita general expenditure		Rank among 50 states
	Amount	As a percentage of U.S. average	
	dollars	percent	
North Dakota	476.46	112.6	14
Minnesota	476.04	112.5	15
Wisconsin	467.27	110.5	16
South Dakota	440.04	104.0	20
Iowa	433.47	102.5	21
Nebraska	390.80	92.4	30
Illinois	381.53	90.2	32
Missouri	359.02	84.9	38
United States	422.97	100.0	

Source: U.S. Bureau of the Census, *Governmental Finances in 1965-66*, G.F. No. 13 (Washington: U.S. Government Printing Office, 1967).

Table 2. Change in per capita general expenditure of state and local governments, 1957-59 to 1964-66

State	Average annual per capita general expenditure		Percentage increase
	1957-59	1964-66	
	dollars		percent
Wisconsin	253.62	425.47	67.8
Nebraska	220.25	354.92	61.1
South Dakota	262.26	410.96	56.7
Missouri	211.95	330.66	56.0
Iowa	256.06	397.68	55.3
North Dakota	294.74	456.46	54.9
Minnesota	294.78	438.51	48.8
Illinois	253.42	360.32	42.2
United States	257.68	390.63	51.6

Sources: U.S. Bureau of the Census, *Census of Governments: 1962*, Vol. VI, No. 4, *Historical Statistics on Governmental Finance and Employment* (Washington: U.S. Government Printing Office, 1964) and *Governmental Finances* annual reports.

amount and quality of public services provided per person. However, it also reflects higher prices for goods and services purchased by governmental units. Nationally, prices paid by state and local governments rose by about 24 percent between 1957-59 and 1964-66.

State and local government spending per person has increased more slowly in Minnesota than in most neighboring states. Only Illinois experienced a lower percentage increase in average annual per capita expenditure from 1957-59 to 1964-66.

Expenditure by Function

Education, roads, and welfare historically have been major responsibilities of state and local governments. These functions, plus health services and hospitals, account for more than three-fourths of all state-local spending in Minnesota (table 3).

Education is the largest category of government expenditure for Minnesota. Twenty-five years ago, less than 30 percent of all state-local spending was for education. But education accounted for more than two-fifths of all general spending in 1966. The total amount spent for this purpose was \$707 million, with 83 percent going for current operating expenses and 17 percent for capital outlay.

Almost three-fourths of all spending for education has been by school districts for local schools. Public spending in 1966 included \$518.5 million for local schools, \$180.1 million for institutions of higher education, and \$8.6 million for other educational purposes.

Education at all levels has received high priority across the nation. But spending for higher education has risen more rapidly than spending for elementary and secondary schools. In Minnesota, the proportion of educational expenditure going for higher education rose from 18.5 percent in 1942 to 25.5 percent in 1966. Sharply higher spend-

Table 3. General expenditure of Minnesota state and local governments by function, 1966

Function	Amount	Percentage distribution
	million dollars	percent
Education	707.3	41.5
Highways	312.1	18.3
Public welfare	147.5	8.7
Health and hospitals	118.4	7.0
Interest on debt	50.0	2.9
Sewerage	48.8	2.9
Police protection	36.1	2.1
Local parks and recreation ..	29.4	1.7
General control	26.3	1.5
Financial administration	23.6	1.4
Fire protection	17.1	1.0
Sanitation	6.2	0.4
Other	179.7	10.6
Total	1,702.3	100.0

Note: Details may not add to totals because of rounding.
Source: Same as table 1.

ing has been required to meet greatly expanded demands for higher education.

Minnesota ranks 15th in the nation in per capita expenditure for all education. Per capita amounts spent in 1966 for major educational purposes in Minnesota and the United States were:

	Minnesota	U.S.
Local schools	\$144.99	\$128.10
Institutions of higher education	50.37	36.79
Other educational purposes	2.40	5.04
Total for education	\$197.77	\$169.95

Spending for local schools in Minnesota exceeded the U.S. average by 13.2 percent. This placed Minnesota 11th among all states. Minnesota was 36.9 percent above the U.S. average but ranked only 16th in per capita spending for higher education. Iowa, Michigan, North Dakota, and Wisconsin were among the states that spent more per capita for higher education.

Highways, roads, and streets comprise the second largest category of state-local spending in Minnesota. Total expenditure for this function was \$312.1 million in 1966. About two-thirds of this amount was capital outlay for road construction and equipment and one-third was for maintenance.

Per capita spending for highways, roads, and streets was \$87.26. Minnesota ranked 16th nationally.

Public welfare is the third largest expenditure category. Total public welfare expenditure amounted to \$147.5 million in 1966. Federally aided categorical assistance programs such as Old Age Assistance, Aid to Families of Dependent Children, Aid to the Disabled,

and Aid to the Blind make up almost two-thirds of total public welfare expenditure.

In 1966, per capita expenditure for public welfare was \$41.24. This was 19.5 percent above the national average of \$34.50 and placed Minnesota eighth among all states. Although total and per capita expenditures for public welfare have risen, the proportion of total general spending for this function has not changed appreciably.

Health and hospitals ranked fourth among the expenditures of state and local governments. Spending for this function totaled \$118.4 million. This amount included spending for state hospitals, including mental institutions, the University of Minnesota Hospitals, and some support to other public and private hospitals. It also included health research, clinics, and other general public health activities and public welfare services provided through hospital and health agencies.

Per capita expenditure for health and hospital services was \$33.11 in 1966. Minnesota ranked 11th among all states.

Changes in Per Capita Expenditure

There have been sharp differences in the rate of increase in per capita spending for major state-local functions (table 4). Among the four largest expenditure categories, per capita spending for education has increased most rapidly, followed closely by spending for public welfare.

Per capita expenditure for public welfare and for highways has risen faster in Minnesota than in the United States as a whole. The state was below the national average in the rate of increase in per capita spending for education and for health and hospitals.

GENERAL REVENUE

The total general revenue of Minnesota state and local governments in 1966 was \$1,782 million. Of this amount, \$1,495 million was from state and local

Table 4. Change in per capita general expenditure of Minnesota state and local governments, 1957-59 to 1964-66

Function	Average annual per capita general expenditure		Percentage increase
	1957-59	1964-66	
	dollars	dollars	percent
Education	110.59	181.90	64.5
Highways	61.20	81.96	33.9
Public welfare ..	23.87	37.87	58.7
Health and hospitals	25.37	30.99	22.2
All functions	294.78	438.51	48.8

Source: Same as table 2.

Table 5. Per capita tax revenue of state and local governments, 1966

State	Per capita tax revenue		Rank among 50 states
	Amount	As a percentage of U.S. average	
	dollars	percent	
Wisconsin	342.56	118.2	5
Minnesota	331.75	114.5	9
Iowa	316.60	109.3	12
Illinois	296.15	102.2	19
South Dakota	275.62	95.1	28
North Dakota	259.32	89.5	31
Nebraska	247.86	85.6	34
Missouri	245.15	84.6	36
United States	289.70	100.0	

Source: Same as table 1.

sources and \$287 million came from the federal government.

State and local taxes provided two-thirds of total state-local revenue, miscellaneous state-local sources provided 17 percent, and the federal government provided 16 percent. Most federal revenue is earmarked for education, highways, and public welfare.

Federal aid comprises the fastest growing source of state-local revenue. Between 1957-59 and 1964-66, revenue from the federal government jumped by 132.5 percent. During this period, revenue from charges and other miscellaneous sources increased by 87.4 percent and total state-local tax revenue increased by 66.9 percent.

Tax Revenue

Total state and local tax revenue in 1966 amounted to \$1,186 million. Per capita tax revenue was approximately \$332. Minnesota was ninth among all states and, among neighboring states, second to Wisconsin in per capita tax collections (table 5).

Taxes on property, income, and sales and gross receipts accounted for about 90 percent of all tax receipts in Minnesota in 1966.

Property taxes were the largest source of tax revenue. Total property tax receipts were \$591 million in 1966. Property taxes supplied almost half of state-local tax revenue and over one-third of all general revenue. Local units of government, which get virtually all of their tax revenue from property taxes, had property tax receipts of \$559 million. State property tax receipts accounted for only 5 percent of total property tax collections.

Minnesota was among those states that relied heavily upon property taxation in 1966, ranking seventh in per capita property tax collections. The relative importance of the property tax will be altered by the 1967 Tax Reform

and Relief Act. This legislation provided for elimination of the state property tax levy, property tax reductions for homeowners, elimination of taxes on some classes of personal property, and tax relief for senior citizens. These property tax reductions will be financed chiefly by receipts from a 3 percent sales tax. The net effort of these changes will be to reduce the share of general revenue coming from property taxes and to increase the share coming from sales and gross receipts taxes.

Income taxes were the second largest source of tax revenue in 1966. State income tax receipts totaled nearly \$297 million. Individual income taxes supplied about three-fourths of total income tax receipts. The remainder came from the corporation net income tax and the bank excise tax.

Minnesota has relied more heavily upon income taxes than most other states. In 1966, income taxes supplied about 25 percent of total state-local tax revenue in Minnesota, compared with 12.8 percent for all states. Fourteen states did not have an individual income tax and 12 states did not have a corporation income tax at that time. Ten states had neither tax.

Sales and gross receipts taxes of the state government supplied 15 percent of all tax revenue. Minnesota did not have a general sales tax in 1966, but a total of \$181.7 million was raised by taxing selected items such as motor vehicle fuels, alcoholic beverages, and cigarette and tobacco products and through the use of gross receipts taxes. Gross receipts taxes totaled about \$26 million.

Minnesota was one of 10 states without a general sales tax in 1966. In 1967 the Minnesota legislature enacted a 3 percent sales and use tax on the purchase of tangible personal property. Purchases of food for home consumption, clothing, drugs, and certain other items are exempt. The revenue from this new tax, which became effective August 1, 1967, will substantially increase state revenue from sales and gross receipts taxes.

Other taxes provided \$117.1 million in state revenue in 1966. This amount included \$52.7 million from motor vehicle and operator licenses, \$20.6 million from severance taxes, \$14.6 million from death and gift taxes, and \$13.5 million from various state license taxes.

Changes in Per Capita Taxes

Average annual per capita tax collections in Minnesota went from \$193.27 to \$304.28 between 1957-59 and 1964-66. Per capita taxes increased 57.4 percent,

Table 6. Change in per capita tax revenue of state and local governments, 1957-59 to 1964-66

State	Average annual per capita tax revenue		Percentage increase
	1957-59	1964-66	
dollars.....		percent
Wisconsin	190.42	315.76	65.8
Missouri	137.25	225.64	64.4
Minnesota	193.27	304.28	57.4
Iowa	181.99	284.00	56.1
Illinois	178.83	273.02	52.7
Nebraska	149.67	227.34	51.9
South Dakota	175.10	247.63	41.4
North Dakota	177.10	248.32	40.2
United States	176.02	268.52	52.6

Source: Same as table 2.

compared with an increase of 52.6 percent for the United States.

Compared with neighboring states, Minnesota ranked behind Wisconsin and Missouri in percentage increase of per capita tax revenue (table 6).

Nontax Revenue

Revenue from fees, charges, and other miscellaneous state and local sources totaled \$309 million and accounted for about one-fifth of all revenue from state and local sources in 1966.

Nontax revenue includes receipts for the performance of specific services and revenue from the sale of commodities and services other than utility and liquor store sales. Tuition and auxiliary fees charged by institutions of higher education make up the largest component of nontax revenue.

Federal Aid

Minnesota received a total of \$287 million from federal sources in 1966. Of this amount, \$268.5 million represented grants to the state government. The state received \$103.4 million for highways, \$74.6 million for public welfare programs, and \$58.5 million for educational assistance.

In 1966, per capita federal aid to Minnesota state and local governments was \$80.25—slightly more than 16 percent above the U.S. average of \$68.98. The state ranked 22nd in general revenue per capita from the federal government.

REVENUE EFFORT

The revenue effort of state and local governments in providing public serv-

ices can be approximated by comparing general revenue collected from state-local sources with state personal income. Measured in this manner, Minnesota ranked seventh in the nation in revenue effort in 1966.

Among the eight states included in table 7, wide variations in revenue effort are evident. General revenue from state-local sources per thousand dollars of personal income ranged from a high of \$170.68 in North Dakota to a low of \$107.94 in Illinois.

OUTLOOK

Minnesota ranks well above the U.S. average in per capita spending on major state and local public services, per capita tax collections, and state-local revenue efforts. The past decade has witnessed sharp increases in state-local spending, shifts in expenditure allocations, and significant changes in the state-local tax system.

Minnesota citizens will want still more and better public services in the future. Therefore, we can anticipate continued pressures on the fiscal capacity of Minnesota state and local governments. Local governments are likely to press for additional state aid as property taxes again climb. And Minnesota, along with other states, will seek still more financial help from the federal government in the future. ■

Table 7. General revenue of state and local governments from state-local sources per thousand dollars of personal income, 1966

State	General revenue per thousand dollars personal income		Rank among 50 states
	Amount	As a percentage of U.S. average	
	dollars	percent	
North Dakota	170.68	129.9	3
Minnesota	157.49	119.9	7
South Dakota	154.56	117.6	9
Wisconsin	149.62	113.9	16
Iowa	144.24	109.8	20
Nebraska	121.97	92.8	40
Missouri	112.65	85.7	45
Illinois	107.94	82.2	49
United States	131.38	100.0	

Source: Same as table 1.

NEW PUBLICATIONS

An Analysis of Domestic and Foreign Demand for U. S. Soybeans and Soybean Products, J. P. Houck and J. S. Mann. Tech. Bull. 256, Univ. of Minn. Agr. Exp. Sta.

Grain Drying Tables, Ronald E. Kaldenberg. Ext. F. 239, Univ. of Minn. Agr. Ext. Serv. Contains tables developed for operators who are mechanically drying grain, especially field-shelled corn.

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In Perspective

Financing Local Government Services in Rural Minnesota

J. D. Helmberger

Financing adequate local government services in rural communities is becoming an increasingly difficult problem. Basic causes of the problem are:

1. The population of most rural communities is declining.
2. Local governments must bear an unduly large portion of education costs.
3. There are too many governmental units in the state.

During our early history, the population of rural communities grew because net outmigration was smaller than the natural population increase. In recent decades, as a result of the technological revolution in agriculture, net outmigration has exceeded the natural population increase. Since the technological revolution is continuing, rural population will continue to decline in many areas. The farm population is declining rapidly. Population also is declining in many small towns whose reason for being was and is to serve farmers. To make matters worse, improved roads and autos have caused many farmers and small town citizens to shop in larger towns.

Some small towns can survive by luring industry. Some are within commuting distance of a thriving town and might survive as bedroom communities. But many small towns are becoming technologically obsolete.

Between 1950 and 1960, Minnesota's rural-farm population declined by 20 percent. Thirty-seven of the 87 counties lost population. Between 1960 and 1965, farm population declined another 16

percent, and 41 counties had a smaller population in 1965 than they had in 1960. By 1980, 49 counties out of the 87 probably will have smaller populations than they have now.

As the population of small towns declines, the cost of government services falls less than proportionately. If half the population leaves a town, it still needs a whole policeman, a whole fire-truck, a whole snowplow, etc. The town cannot maintain services at half the former cost, and this is the case without any consideration for education costs.

Furthermore, the migrants tend to be the young and middle-aged adults who have higher incomes. The rural community is left with a disproportionate share of old people, giving the town welfare problems. Apart from education costs, rural communities are likely to find it increasingly difficult to finance needed services without aid from the state or federal governments.

The notion that education ought to be locally financed (a notion that was never completely valid) is now clearly obsolete. Expenditures on education are investment expenditures. As long as most people lived out their lives where they were reared, financing education locally was tenable. The taxpayers invested in their children's education, which increased their productivity and taxpaying ability and hence increased the local tax revenue by more than the education cost.

To the extent that the educated children migrated from rural communities to urban areas, the urban governments reaped where the rural governments sowed. As long as the migration was

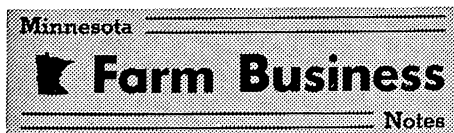
small, the local problem was not serious. But as people began to migrate more, state aid became necessary and the appropriate size of the aid grew both absolutely and relative to the total education cost.

If every state's population were divided about equally between rural and urban, there would be no justification for federal aid except possibly to subsidize the poor states. The past and present methods of financing education have forced agricultural states to subsidize the urban states. In the fifties, 182,000 people migrated from rural Minnesota, taking the local investment in their educations with them. About 102,000 of them moved to the Twin Cities metropolitan area. The metropolitan area reaped the tax collection yield on the investment but shifted a substantial amount of the revenues back to local governments through state aid. But 80,000 left the state entirely. California and other states are reaping tax revenues from Minnesota's education investment. The only way to redress this clear inequity is with federal aid.

In many states, opportunity exists for increasing efficiency through merger of some units of local government and elimination of others. This is particularly true for Minnesota. Only three states had more governmental units than Minnesota in 1962. Efficiency could be increased by eliminating township governments, consolidating small counties, and merging small towns or villages adjacent to larger towns.

To alleviate the difficulty of financing local government, we might:

1. Leave more of the costs of education and perhaps welfare to state and federal governments.
2. Reduce the number of local governments.
3. Adopt tax sharing between state and local governments, utilizing income taxes or sales taxes or both.



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