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Budget Manual: An MTAS Guide for Municipal Budget Development and Execution

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for Municipal
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Prepared by
Margaret Norris
Municipal Management Consultant

MTAS
MUNICIPAL TECHNICAL
ADVISORY SERVICE

A statewide agency of
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in cooperation with the
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TABLE OF CONTENTS

INTRODUCTION

Cause it's better to have money and
not need it than to need it and not have it.

- Richard Pryor*, Car Wash*, 1976

We all know what a budget is: a record of the money we expect to receive and how we expect to spend it. It's a pretty simple concept but a little more difficult to put into action, especially when rules and regulations from state and federal agencies are thrown into the mix. This manual will give you a "big picture" look at budgets and tell you what you need to do to stay out of the principal's office (that's the comptroller by the way).

Why You Need a Budget

As stated, the state of Tennessee has a few things to say about the matter of your municipal budget. According to *Tennessee Code Annotated* (*T.C.A.*) 6-56-201 et seq., otherwise known as the Municipal Budget Law of 1982, "The governing body of each municipality shall adopt and operate under an annual budget ordinance. The budget ordinance shall present a financial plan for the ensuing year…" Furthermore, the city's charter may dictate various other regulations, in addition to state, law regarding budget requirements. Refer to your city's charter to ensure proper compliance.

Besides being required by law, having a budget is not a bad idea. Can you imagine what it would be like if your city or town just took whatever money it received and simply paid for everything that the departments spent? It might be fun to buy everything you think you need and want, but how long would it take for your checks to bounce? You need a plan of action with limits and controls.

Types of Budgets

There is more than one way to define a budget. Local governments usually use one of three types of budgets: line item, program, or performance. Which budget you should use will depend on what you plan to measure.

Line Item Budget

The line item budget typically is used when control is the budget's main function. It also is the budget type that most cities and towns use. In a line item budget, expenditures are listed under a large subject area – a fund; then broken down by a function or purpose, such as a department; then by an object, for example, utilities. This can then be further broken down into items such as gas, water, and electricity. Imagine a tree, where you start at the trunk, then split into branches, then spread into leaves. The trunk is the General Fund, the large branches are the departments, and the leaves are all the items that will be purchased within each department.

The more detailed the line items, the more control the governing body or manager has over expenditures. According to *Budgeting: A Guide for Local Governments:*

> *… the line-item budget originated in the late nineteenth century in response to the excesses of the political machines that controlled many state and local governments: this format was ideally suited to shifting power away from political bosses*

and toward legislative bodies, which were more accountable to voters.

The downside to line item budgets is that they provide no information about the activities or functions of a program or department or how efficiently they operate. The focus is strictly on what is purchased.

Performance Budget

A performance budget allocates money to activities or programs, plus it describes the amount of services that will be produced with the money allocated. It allows an adjustment of the level of services provided as to both quality and quantity. It is a very useful budget system, but it is very difficult to prepare because of the amount of information necessary to do so properly.

Program Budget

A program budget focuses on the services to be provided by the city and budgets money according to functions such as public safety, general government, public works, recreation, etc. It shows the purposes for which money will be spent and the importance the city places on these functions. It does not show the level of services provided, and some say that, as a result, its value as a tool for managing the quantity and quality of public service programs is weakened.

Funds

As mentioned earlier, city and state laws dictate a large portion of the budget process. However, there also are other guidelines that cities must follow. The Government Finance Officers Association publishes something familiarly known as the "blue book." Its official title is *Governmental Accounting, Auditing, and Financial Reporting*, often abbreviated as GAAFR, and it outlines standards for governmental agencies to follow, known as "generally accepted accounting principles" (GAAP). Among these principles is the formation of funds. As taken from *Fiscal Administration, Analysis and Applications for the Public Sector* by John L. Mikesell, the definition of "fund" is:

…an accounting device established to control receipt and disbursement of income from sources set aside to support specific activities or attain certain objectives. In the accounts of individual governments, each fund is treated as a distinct fiscal entity.

In simpler terms, a fund is a smaller record of incoming and outgoing money that is divided by type of activity. Using a garden as an example, the budget can be described as the garden, and the different funds would be the vegetables (governmental funds), flowers (proprietary funds), and ornamental plants (fiduciary funds).

Governmental Funds

Again, referring to GAAFR for a definition, governmental funds are "funds generally used to account for tax-supported activities." That's pretty straightforward. However, as with most everything else to this point, it can be broken down further. There are five types of governmental funds: General Fund, special revenue funds, debt service funds, capital project funds, and special assessment funds. So, within the vegetable patch, you may have peas, beans, green peppers, squash, and tomatoes.

While there is only one General Fund, which is the primary operating fund, there can be several "varieties" of the other governmental funds – just like there are Roma tomatoes, cherry tomatoes, grape tomatoes, beefsteak tomatoes, etc. For example, you may have multiple special revenue funds for projects that are restricted for specific purposes: CDBG Grant Fund, State Street Aid Fund, Drug Fund, etc. (See the appendix for information regarding special restrictions on Drug Funds.) You also may have multiple debt service funds, such as those that account for long-term debt: General Obligation Bond Fund, General Debt Service Fund, etc.

Likewise, the city may have multiple capital project funds that are set aside for acquisition and/or construction of major capital facilities: City Hall Fund, Fire Truck Capital Reserve Fund, Ballpark Improvement Fund, etc. Finally, there can be multiple special assessment funds: Curb and Gutter Fund, Solid Waste Fund, and Special School District Fund, for example.

Proprietary Funds

Proprietary funds are those that are most like funds in the private sector. Again, according to GAAFR, proprietary funds are "funds that focus on the determination of operating income, changes in net assets (or cost recovery), financial position, and cash flows." There are two types of proprietary funds: enterprise funds and internal service funds. Going back to the garden, it's similar to the flower bed in which you have annuals and perennials.

As defined by GAAFR, enterprise funds are used to "report activities for which a fee is charged to external users for goods and services." Examples include Water Fund, Sewer Fund, Natural Gas Fund, Cemetery Perpetual Care Fund, Airport Fund, and possibly the Solid Waste Fund.

Internal service funds are used to track the activity provided by one department for another department. A common example is the city garage charging various city departments for its services. The benefit to tracking the expenditures this way is to encourage efficiency. If a department is being charged for an otherwise "free" activity, the department using the service will be less likely to abuse it.

Fiduciary Funds

Once again, we go to GAAFR for a definition. Fiduciary funds are "funds used to report assets held in a trustee or agency capacity for others and which therefore cannot be used to support the government's own programs. The fiduciary fund category includes pension (and other employee benefit) trust funds, investment trust funds, private-purpose trust funds and agency trust funds." Examples of fiduciary funds a city may have include a law enforcement trust fund and firemen's pension fund.

There is, in effect, no limit on the number of funds that a city can establish. However, since each new fund adds to the complexity of the city's financial operation and takes away flexibility, it is advisable to keep the number of funds as low as possible within legal and financial requirements. In general, the budget process is the same for each fund. The most difficult part of the budget process is making projections of revenues and expenditures for the next fiscal year.

THE BUDGET PROCESS/CYCLE

Evolution is not a force but a process; not a cause but a law.

John Viscount Morley (1838–1923*),*
On Compromise

Overview

The budget process actually begins with the preceding year's audit. Municipalities have their fiscal affairs audited every year, another legal requirement found in *T.C.A.* 6-56-105. The audit helps provide a "picture" of how well the city is doing financially. Information found in the audit can be used to help determine where new revenues are needed and what to set aside for bonded indebtedness, etc. The portion of the audit dealing with revenues and expenditures should be based on the prior fiscal year's budget so that a municipal official can readily compare actual figures with budget estimates. This information, when considered with the staff's day-to-day knowledge, provides a basis for developing a budget, as well as determining needs for improving the city's fiscal picture. The auditor's recommendations for changes in bookkeeping, accounting, etc. complete the review and allow deficiencies to be rectified. Once a review of the financial affairs is completed, this knowledge can be used to plan for the coming year.

Most cities are required to follow guidelines set forth in the Municipal Budget Law of 1982 (*T.C.A.* 6-56-201 et seq.). However, there are exceptions. If your charter requires estimates of proposed expenditures for each department, board, office, or other agency of the city; and if your charter requires estimates of anticipated revenues from all sources, including current and delinquent taxes, non-tax revenues, and proceeds from selling bonds or long-term notes, then it is sufficient to follow your city's charter and not the Municipal Budget Law. Mayor-aldermanic (general law) charters require following the budget law; however, modified-city manager-council (general law) charters already require sufficient detail and are not required to follow the budget law. Private act charter cities will have to examine their budgeting provisions to determine if the charter provides enough specificity. Finally, city-manager-commission (general law) charters seem to meet the detailed requirements; however, it is recommended that you contact your auditor for a conclusive determination.

With that being said, according to the Municipal Budget Law of 1982 (*T.C.A.* 6-56-203), all budget ordinances require the following six elements:

1. Estimates of proposed expenditures for each department, board, office or other agency of the municipality, showing, in addition, expenditures for corresponding items for the last preceding fiscal year, projected expenditures for the current fiscal year and reasons for recommended departures from the current appropriation pattern in such detail as may be prescribed by the governing body. It is the intent of this subdivision that, except for monies expended pursuant to a project ordinance or accounted for in a proprietary type fund or a fiduciary type fund, which are excluded from the budget ordinance, all monies received and expended by a municipality shall be included in a budget ordinance. Therefore, notwithstanding any other provision of law, no municipality may expend any monies regardless of their source (including

monies derived from bond and long-term note proceeds, federal, state or private grants or loans, or special assessments), except in accordance with a budget ordinance adopted under this section or through a proprietary type fund or a fiduciary type fund properly excluded from the budget ordinance;

2. Statements of bonded and other indebtedness of the municipality, including debt redemption and interest requirements, debt authorized and unissued, and the condition of the sinking fund;
3. Estimates of anticipated revenues of the municipality from all sources, including current and delinquent taxes, nontax revenue, and proceeds from the sale of any bonds on long-term notes with a comparative statement of the amounts received by the municipality from each of such sources for the last preceding fiscal year, the current fiscal year, and the coming fiscal year in such detail as may be prescribed by the governing body;
4. A statement of the estimated balance or deficit as of the end of the current fiscal year;
5. A statement of pending capital projects and proposed new capital projects relating to respective amounts proposed to be raised therefore by appropriations in the budget and the respective amounts, if any, proposed to be raised therefore by the issuance of bonds during the fiscal year; and
6. Such other supporting schedules as the governing body deems necessary or are otherwise required by law.

Budget Calendar

The budget cycle consists of four main steps or phases: preparation, approval, execution and audit. The audit, previously mentioned, is typically considered the last phase of the budget cycle; however, it is an integral tool in budget preparation. The following chapters describe in detail how to perform and prepare budget estimates.

The budget calendar is centered around budget adoption. Refer to the appendices for samples of required budget documents, including the public notice, the budget ordinance, and a few sample pages from a General Fund budget narrative (line item descriptions of the individual departments). Keep in mind that charters may vary as to publication and public hearing requirements so be sure to double check your charter before setting your budget calendar.

On the following page is a sample budget calendar for small- to medium-sized cities. The size, complexity, and any additional charter requirements of your municipality may change the preparation dates; however, the end of the fiscal year for Tennessee municipalities is June 30, and audits always follow closely thereafter.

BUDGET CALENDAR		
DATE	**PHASE**	**EVENT**
On or before March 15	Preparation	Finance officer prepares previous and current year financial data on estimate forms.
March 15	Preparation	Estimate forms are forwarded to mayor, finance committee, or chief administrative officer and to department heads with instructions.
By April 15	Preparation	Finance officer prepares revenue estimates.
By May 1	Preparation	Department heads prepare estimates and forward to mayor, finance committee or chief administrative officer.
By May 15	Preparation	Mayor, finance committee or chief administrative officer reviews estimates and develops recommendations for legislative body.
By May 15	Preparation	Submit proposed budget or budget requests to legislative body.
By June 30	Approval	Legislative body finalizes budget, holds necessary public hearings, and adopts the budget. State law requires a notice of the budget ordinance to be published "in a newspaper of general circulation … not less than ten days prior to the meeting where the governing body will consider final passage of the budget."
July 1 to June 30	Execution	Close monitoring of revenues and expenditures. Budget amendments, as permitted by state law and local charters, should be prepared as necessary.
"As soon as practicable after the end of the fiscal year."	Audit	Audit firm comes to city hall to conduct fieldwork. This usually is done any time between July and October.
By end of calendar year	Audit	Audit firm should make a presentation to the governing body, which should then accept the report. Per *T.C.A.* 6-56-1204(b), "A summary of the audit, prepared by the auditor, shall be published in at least one issue of a newspaper of general circulation in the corporation, if there is one."
By end of calendar year	Audit	Send one copy of the audit to "the mayor, chief executive officer, each member of the governing body, and the comptroller of the treasury. Copies of each audit shall also be made available to the press."

Emergencies

What do you do when a tornado rips through the middle of downtown or a blizzard dumps inches upon inches of snow on the ground and paralyzes the town for days? Of course you don't intend for these events to happen when you prepare the budget, but you have to anticipate the realities of an emergency – and sooner rather than later.

According to state law (*T.C.A.* 6-56-205), the governing body may spend more than the estimated available funds, but only when there is "an actual emergency threatening the health, property or lives of the inhabitants of the municipality and declared by a two-thirds (2/3) vote of all members of the governing body present, when there is a quorum."

In such a case, *T.C.A.* 6-56-304 (3) requires the following recordkeeping:

> *A record of any such emergency purchase shall be made by the person or body authorizing such emergency purchases, and shall specify the amount paid, the items purchased, from whom the purchase was made and the nature of the emergency. A report of any emergency purchase shall be made as soon as possible to the municipal governing body and the chief executive officer of the municipality, and shall include all items of information as required in the record.*

From a financial perspective, this is why you have an undesignated fund balance, retained earnings and, possibly, contingency funds. Disaster assistance may be available in some situations; however, cities and towns should be prepared to handle the immediate circumstances. A good rule of thumb is to have the equivalent of at least two months' operating expenses available as an undesignated fund balance.

Deadline

In the event the governing body does not pass the budget by June 30, *T.C.A.* 6-56-210 takes effect. It states:

> *If for any reason a budget ordinance is not adopted prior to the beginning of the next fiscal year, the appropriations for the last fiscal year shall become the appropriations for the next fiscal year, until the adoption of the new budget ordinance.*

While this provision exists, municipalities are strongly urged to meet the June 30 deadline.

REVENUE ESTIMATES

What we have here is a failure to accumulate.

Jim Varney, *Ernest Saves Christmas,* 1988

Revenue Estimation

Estimating revenue may seem like a daunting task, but it's really not. It doesn't require a degree in rocket science to be able to arrive at sound, logical figures. It's really just using averages and common sense.

In the appendix, there is a list of all revenues that Tennessee municipalities can expect to receive in their governmental funds. The list includes the revenue class (local taxes, licenses and permits, intergovernmental, etc.), the fund (general, state street aid, etc.), account number (state chart of accounts), a description, any related authorizing state statutes, restrictions, the current rate if it applies, the timing of the payment, if late fees can be assessed, where the money comes from (taxpayers, businesses, water users, etc.), how the money is collected, and any use restrictions. This list is a great tool to help you learn the "who, what, when, where, and how" of each revenue source.

Assuming that you now know all the revenues you need to estimate, where do you begin? Let's start in the governmental funds with the local tax class. This typically is the largest of the revenue classes, and it includes real property taxes, personal property taxes, public utility property taxes, property taxes from prior years, property tax penalties and interest, payments in-lieu-of taxes from electric utilities and industry, local option sales taxes from the city and county, wholesale beer taxes, wholesale liquor taxes, mixed drink taxes, minimum business taxes, natural gas franchise taxes, special assessments, room occupancy (hotel/motel) taxes, and cable TV franchise taxes.

Real Property Tax, Personal Property Tax (levied on businesses), and Public Utility Property Tax

When property taxes are levied, they represent a substantial percentage of the municipality's overall revenue. It is true that most Tennessee cities are not able to control the appraisal of property within their corporate limits, but they are able to control their tax rate, which is unlimited (unless reimposed by a charter provision subsequent to a 1973 act by the legislature that removed all maximum limits). It is useful to calculate the value of one cent in the tax rate based on the latest assessment figures, so that the governing body can calculate the tax rate necessary to balance the budget.

How to Project Property Taxes: In projecting property tax receipts, a city should project only the amount of current property taxes it anticipates collecting during the fiscal year. This invariably will be less than the total amount of taxes due. This projection should use a percentage factor based upon the actual collection experience of the past two or three years. Such information is available in each city's audit report for every previous year.

For example, if an average of only ninety percent of total taxes due has been collected, then the maximum revenue entry for current property tax would be ninety percent of the current taxes due. However, unless absolutely necessary, we do not recommend that the maximum amount projected be budgeted for any revenue. It is always better to underestimate a revenue projection than to overestimate one. An exception to this would be a fixed item, such as an agreed upon in-lieu-of-tax payment from a municipally owned electric utility. Reasons for budgeting less than the maximum amount anticipated vary for each revenue source. In the case of property tax, a city must allow for economic downturns, or more specifically, in the case of public utility property, assessment action by the Office of State Assessed Property that may reduce the maximum taxes anticipated. Some Tennessee cities have experienced this difficulty in the past when public utility property was a substantial factor in their tax base.

Property Taxes from Prior Years

As the name implies, these are delinquent property taxes. Projection of delinquent property tax receipts depends primarily on two factors: the extent of delinquent taxes outstanding and the level of effort to be exerted in collecting those delinquencies.

Delinquent taxes can be collected under a general law procedure (*T.C.A.* 6-55-201 et seq.) or as provided in a city's charter. Many cities enter into a joint effort with their county government as a practical solution to the problem. But whether working with the county or not, city staff need to remember that by current state law a time limit of six years from January 1 of the year in which the delinquent tax accrued is in effect for filing suit.

How to Project Property Taxes from Prior Years: The projection of this revenue item should be based on collections for the past two or three years. However, be sure to pay attention to the city's collection effort over the last few years. If the efforts produced a relatively constant collection rate, and the same efforts are expected for the upcoming year, then the previous years would be good indicators. A greater collection effort can increase substantially the amount collected. When budgets become tighter, it appears that efforts intensify for the collection of delinquent property taxes.

Property Tax Penalties and Interest

Penalties and interest are collected at the same time as delinquent property taxes. The penalty for late payment is one-half percent, and the interest is one percent, imposed on March 1 and on the first day of each subsequent month, unless the municipality stipulates otherwise through its charter or an ordinance.

How to Project Property Tax Penalties and Interest: See Appendix D for a table of interest rates by month delinquent. If you have only 10 delinquent taxpayers, it would be easy to calculate this systematically by using the table. However, most cities have many more delinquencies than this. The rule of thumb here is the same as with prior year estimates: base it on collections for the past two or three years.

Payments in Lieu of Taxes from Electric Utilities and Industry

As with most things in government, there is a handy acronym for this: PILOT. Payments are based on the plant value of the electric (or gas) system and represent the utility's fair share of the cost of local government. This applies only to cities that own electrical distribution and gas systems. Industrial firms that are eligible for PILOT are those that are declared to be "performing a function in behalf of the municipality …" (*T.C.A.* 7-53-305(a)). The principal payers are lessees of projects financed by an Industrial Development Corporation.

How to Project Payments in Lieu of Taxes: There are complex formulas that can be found in *T.C.A.* 7-39-404 for gas systems, *T.C.A.* 7-52-304 for electrical systems, and *T.C.A.* 7-53-305 for industrial firms. However, the easiest way to calculate this revenue estimate is to, again, base it on the last two or three years' experience.

Local Option Sales Taxes

These taxes are based on sales receipts within the county and municipality. The principal payers are the shoppers. This makes projections a little more difficult due to economic fluctuations. When times are tough, the money may only trickle in, but when the economy is booming, shoppers will more easily part with their discretionary money.

The maximum amount allowed by *T.C.A.* 67-6-701 et seq. is two and three-quarters percent. If your city is not charging the maximum amount and would like to increase its rate, a referendum of the voters is required pursuant to *T.C.A.* 67-6-705 – 706.

It is important to make sure that you are getting all the money that's coming to you from the businesses in your town. Periodically (once a year) obtain a *situs* report by contacting:

Karen Blackburn, Manager of Financial Control
Department of Revenue, Division of Fiscal Svcs.
1220 Andrew Jackson State Office Building
500 Deadrick Street
Nashville, TN 37247
Phone: (615) 741-1028
Fax: (615) 532-8971

The department will accept faxed requests if they are on municipal letterhead. The report lists all the retailers that the state has listed in your town and their sales tax numbers (highly confidential). Pay close attention to the businesses at the edges of town. The county may be getting your money from the Walgreens at the city limit. For more information on *situs* reports, refer to the MTAS Technical Bulletin entitled *Get Your Share of the Local Option Sales Tax and Hall Income Tax: Request a* Situs *Report* reprinted in Appendix E.

How to Project Local Option Sales Taxes: We recommend that you base local sales tax projections on at least three years of data. The first two years should be year-end actual figures obtained from past audit reports.

The third year of data is the current year and is obtained by using actual year-to-date collections extended to arrive at a total for the current year. It is recommended a city use all possible approaches to estimate current year collections. Each approach requires year-to-date totals through the most recent month. If the budget is prepared in April, revenues should be totaled through March.

Once these data are available, the first approach involves dividing the total by nine (number of months) to obtain a monthly average for the nine-month period. Then multiply by 12 for a yearly projection as follows:

Year-to-Date Projection		Months		Monthly Average		Months		Year
$900	÷	9	=	$100	X	12	=	$1,200

The second approach involves multiplying March figures by three and adding the result for your nine month year-to-date to arrive at a yearly total.

March Projection		Current Year Remaining Months		Quarterly Projection		Year-to-Date		
$175	X	3	=	$525	+	$900	=	$1,425

The third approach involves adding the current year-to-date total to the actual amount of the last quarter of the previous fiscal year.

Year-to-Date		Actual Last Year Quarter		Current Year Projection
$900	+	$400	=	$1,300

All three approaches result in relatively similar results. However, when multiplied to reflect many cities' actual sales tax revenue, the differences could amount to several thousand dollars. It is recommended that a figure be used that is half way between the high and low figures.

Once three years of data are in place, it is time to make projections for the coming fiscal year. If current year collections are less than in previous years, you should make an effort to determine why. When the factors are identified, determine whether they are temporary or long term.

If current year projections are substantially higher than previous year collections, you must determine the cause. However, unless unusual commercial growth is taking place, *i.e.*, more businesses opening and/or attracting more shoppers, the safe approach is to budget the coming year at the current year level with a maximum increase of five percent.

It has been stressed previously, but it is important not to overproject revenues.

Wholesale Beer Tax

For cities with beer retail outlets within the corporate limits, the local wholesale beer tax is a 17 percent tax levied on the wholesale price of beer. State law requires the wholesaler to pay this tax directly to the city and to file monthly reports with the city and the state Department of Revenue. It is easy to understand that volume of sales determines the amount of this revenue since the rate is fixed at 17 percent. However, it is important that each city monitor monthly receipts for any exceptional fluctuations and check occasionally to be sure that payments are being received from all beer wholesalers serving the area. Inadvertent errors may result in lost revenue.

How to Project Wholesale Beer Tax: The minimum two- or three-year history referenced earlier should be used to project wholesale beer tax collections. If the history shows a steady growth in revenues year after year, the average percentage growth can be projected for the coming year. However, if current year projections are indicating a downturn, the cautious approach would be to budget no more than the current year's receipts. The addition of retail beer outlets within the city will not necessarily result in increased revenues if there are several other outlets already located within the corporate limits. However, annexation of existing beer outlets usually will increase revenues. The approximate extent of such increase usually can be determined if the wholesaler or retailer cooperates by supplying the volume of wholesale sales or purchases for the business in the annexed area.

Wholesale Liquor Taxes

Cities with package liquor stores are authorized to collect a municipal inspection fee from licensed liquor retailers. The fee cannot exceed eight percent of the wholesale price of alcoholic beverages supplied by a wholesaler for cities located in counties with populations of fewer than 60,000. Cities in counties with a population of greater than 60,000 can assess a fee of no more than five percent. The fee is collected by the wholesaler, who then makes a monthly payment to the municipality. The wholesaler is allowed five percent of the revenue for performing collection and remittance; therefore, cities receive 95 percent of the total fee. The reimbursement deduction should be reflected on the wholesalers' monthly reports.

How to Project Wholesale Liquor Taxes: The same "rules" apply here as for the wholesale beer tax. Make adjustments up or down as appropriate if any package stores have opened or closed during the previous year.

Mixed Drink Taxes

This revenue source is available only to cities that have approved liquor-by-the-drink. The tax is based on the sale of alcoholic beverages for consumption on premises. The rate is 15 percent of the gross sales of all alcoholic beverages sold for consumption on the premises. Cities receive 25 percent of the 15 percent tax that is collected. The city will receive a monthly check from the Commissioner of Revenue.

How to Project Mixed Drink Taxes: Just as with the wholesale beer and liquor taxes, look at the last two or three years to spot trends. As always, it is better to estimate low than too high.

Minimum Business Tax

State law establishes business taxes and their maximum rate limits. However, the decision to impose a business tax and set the rates up to the maximum is left to the local governing body. An important source of information when looking for new revenues is to know whether your city imposes a business tax and whether it is levied at the maximum limit.

Collecting current and delinquent business taxes is a local responsibility, and an appropriate amount of effort should be devoted to it. After the tax is six months delinquent, it becomes the duty of the state to collect the tax, penalty and interest. All amounts collected by the state from the delinquent taxpayer will be retained by the state. Therefore, if a city imposes a business tax, the city should collect it in order to receive the revenue.

How to Project Business Taxes: Projections of business tax revenues rely on a minimum two- or three-year performance history. The impact of additional commercial area (through annexation and/or new construction) should be considered. Additional city collection efforts also should be taken into account.

In most cases, significant fluctuations in business taxes will not occur, and current year receipts are a good basis for safely projecting the coming year.

Natural Gas Franchise

This differs from the PILOT listed earlier in that the city is imposing a fee upon the operation of a gas company within the corporate limits. The franchise agreement is passed and implemented by municipal ordinance.

How to Project Natural Gas Franchise Fees: This amount is based upon the agreement and won't vary from year to year unless the agreement is amended.

Special Assessments

Municipalities have the power to design and execute construction and improvement or reconstruction of any street, avenue, alley, highway or public place. The municipality "may prescribe, and to cause not less than two-thirds of the cost or expense of the aforementioned work and improvements to be assessed against the property abutting or adjacent to the street, avenue, alley, or any other public place so improved" (*T.C.A.* 7-32-101). The municipality must hold a public hearing and adopt an ordinance prior to making the improvements; the ordinance must describe the nature of the intended work.

How to Project Special Assessments: Base this revenue estimate on cost projections, including items such items as materials, labor, engineering fees, etc.

Room Occupancy Tax

This applies to about 30 Tennessee cities that have statutory authority to pass a hotel/motel tax. If the county in which your city is located is already levying this tax, the city cannot levy it. Cities with home rule charters can levy the tax by ordinance; however, all other charters must adopt the tax by a private act of the state legislature. "If your city is eligible to adopt a hotel/motel occupancy tax, try to estimate the expected annual revenues to see if the results are worth the effort. The expected revenues depend largely upon tourist or transient flow." (MTAS Technical Bulletin *Hotel/Motel Tax in Tennessee Municipalities*).

How to Project Room Occupancy Tax: "While [projecting] an exact revenue figure may not be possible beforehand, one of the following methods may be helpful to estimate annual revenues.

1. "Examine the gross receipts reported by each hotel and motel on its municipal business tax return and contained in confidential state sales tax reports. This information gives you a rough idea of each establishment's annual volume of business. Unfortunately, these returns usually combine room receipts with receipts from the restaurants, bars, and gift shops.
2. "Determine the total number of hotel/motel rooms subject to the tax along with an average room rate per night, then estimate the overall percentage rate of occupancy, and use the following formula to arrive at an estimated annual tax yield:

   # of rooms x average room rate per night x tax rate x 365 days x percent of occupancy = annual revenue from hotel/motel tax.

   This formula might have to be applied to individual establishments, or to groups of similar establishments, rather than entire cities. It is difficult to calculate accurate citywide averages." (MTAS Technical Bulletin *Hotel/Motel Tax in Tennessee Municipalities*.)

Cable TV Franchise

This is a relatively straightforward revenue source. As the name implies, municipalities are authorized under *T.C.A.* 7-59-101 et seq. to regulate, by way of franchise licenses, any cable television company that operates within city limits. The agreement has a timeframe, and the expiration date should be noted, as should any provisions on renewal or extension.

How to Project Cable TV Franchise Receipts: Refer to the agreement. Many municipalities base the franchise license on a percentage of sales receipts, either gross or net. Be sure to double check that the amount the cable company is sending you concurs with the agreement and is accurate. One thing to keep in mind when estimating the company's profit is the influx of satellite service and the impact it may have on the local cable company.

Licenses and Permits

Licenses and permits generally account for about three to four percent of a municipality's General Fund revenue budget. Normally, the two most significant licenses and permits are automobile registration (city sticker) and building code permits. There are other types of permits (taxicab licenses, beer licenses and liquor licenses), but these usually do not generate a significant amount of revenue.

If the municipality levies or enacts a city sticker program, collection can be handled for a fee through a contract with the county clerk. The benefit of this arrangement is that clerks collect almost 100 percent of the charge since it is tied to annual license plate renewals.

Consideration should be given to the following three factors when reviewing license and permit collections. Changes in these factors can make the two-year history almost meaningless.

1. Anticipated volume of business. This should not affect auto registration or annual renewals on licenses, but during periods of slowdown in the building industry, the number of building-related permits will be a fraction of those in earlier years.
2. License or permit fee. If fees are significantly lowered or raised, it will directly affect the amount of revenue received.
3. Collection effort. If a strong effort is not made to ensure that all contractors acquire a permit for new construction, receipts will be reduced. This also is true for auto registration where a slowdown on the part of the enforcement agency can result in a significant reduction in receipts.

Each city should closely review the amount of construction taking place and, by talking to local contractors and developers, try to determine the approximate amount of planned activity for the coming year. Fees for each type of permit connected with building should then be applied to the anticipated volume of business to determine the projection for the coming year.

Intergovernmental Revenue

Again, here's a case of appropriate naming: intergovernmental revenues are those that municipalities receive from other governments, both state and federal. Intergovernmental revenues can be in the form of state and federal grants, an in-lieu-of-tax payment from the local housing authority and, most significantly, state shared taxes.

State and Federal Grants

State and federal grants are obtained by an application, which states the amount requested. Budgeting these grants, even though the grant may not be secured, should not affect other parts of the budget since these grant revenues are tied directly to specific expenditure line items. A city should avoid expending money for a grant program until the grant is finally approved. In many cases, federal regulations state that money spent before a grant is approved cannot be charged against the grant. Examples of such grants include Community Development Block Grants (CDBG), the Local Parks and Recreation Fund (LPRF), the Land and Water Conservation Fund (LWCF), and the Heritage and Community Tourism Development Division assistance program.

Housing Authority in-Lieu-of-Tax Payment

The in-lieu-of-tax payment from a housing authority should remain constant from year to year unless expansion occurs within the system. Discussion between the housing authority director and the preparer of the budget should provide a reasonably accurate projection for this revenue.

State Shared Taxes

Just like the garden mentioned in the fund descriptions, state shared taxes comprise several sections. One row in the garden of state shared taxes is sales tax, another is the Hall Income Tax, then come the beer tax, gasoline and motor fuel tax, streets and transportation, gross receipts from TVA, and finally the corporate excise tax.

Projections of state shared taxes are based primarily on per capita amounts calculated from total state appropriations, which are based on the results of each annual session of the state legislature. Any changes that remove, add or adjust the regulations on use of state shared taxes are a result of legislative action. Specific exceptions are state shared income tax and the state shared corporate excise tax.

Two factors are most important in projecting state shared revenues. First is each city's certified population count. This count should be the same as the previous year unless a city has annexed additional population, conducted a special census (two special censuses per decade are allowed for each city) or resolved a challenge to the Bureau of the Census during the current fiscal year. If none of these events has occurred, and your city is still in question about the previous year's certified count, refer to the current MTAS *Directory of Tennessee Municipal Officials*, which contains the latest certified population figure for each listing. If any of the three events did occur, or if there is a question about the certified population count, the regional office of the Local Planning Office should be contacted.

If a city anticipates a special census or annexation, it should plan on having the process completed and the new census result to its Local Planning Office for certification no later than May 15 of the current fiscal year.

Once the population is certified, the second factor is to determine per capita amounts. Adoption of the state budget usually occurs toward the end of the legislative session. The result has been the late issue of per capita amounts, sometimes as late as June. Waiting for this data can make a city very late in preparing its budget. It is recommended that cities use the current year per capita amounts to establish a tentative revenue projection for state shared taxes. Once data for the coming year are available, the projections can be adjusted.

In reviewing its past history, each city should compare the revenues that it actually received for each of these items against the amount that it was supposed to receive based on the appropriate per capita amount. The reason is that many of the per capita amounts are based on projected sales volumes. This is especially true for state sales tax and state street aid. If the review indicates a significant difference between projected and actual receipts, a cautious approach might require an adjustment of the projections for these items to reflect past history.

On the two exceptions noted previously, the Hall Income Tax and the excise tax, a city will have to refer to its past history to make projections. However, a city should be careful not to project the coming year at a higher rate of increase than the increase shown between the two actual previous years and the current year estimate.

Three-eighths of the Hall Income Tax is returned to the location where it is collected. This is done by means of a code placed on the tax return by the preparer. Therefore, it is very important that each person in your community place the correct code number on his or her return so that the city will receive credit. For more information on maximizing your share of the local option sales tax and income tax, please refer to Appendix E for a technical bulletin on the subject.

The table on the next page shows a breakdown of the estimated state-shared revenue amounts for fiscal year 2001-2002. Each year MTAS publishes a *Hot Topic* outlining this data, so look for it when you are preparing your state-shared revenue estimates. Also, there are:

- The Hall Income Tax. The statewide projected increase is three percent, but individual city amounts will fluctuate. This revenue is distributed once a year;
- The Corporate Excise Tax. Statewide revenues are projected to decrease four percent from FY 2001. This revenue comes annually in the third quarter;
- The State Mixed Drink Tax. The statewide projected increase is 4.8 percent. This revenue is distributed monthly;
- Public safety salary supplements are projected to remain the same as in FY 2001. The state will provide salary supplements not to exceed $600 for police officers and $450 for fire personnel.

These supplements are not automatic; public safety personnel must meet certain requirements to qualify for these payments that are made once a year.

Estimated State Shared Revenue for Fiscal Year 2001-2002

General Fund	**Distribution Frequency**	**Amount per Capita**
State Sales Tax	Monthly	$66.87
State Beer Tax	Semi-annually	$ 0.42
Special Petroleum Products Tax (gasoline inspection fee)	Monthly	$ 2.31
Gross Receipts (TVA in lieu of taxes)	Quarterly	$ 6.58
Total General Revenue Per Capita		$76.18
State Street Aid Funds Gasoline and Motor Fuel Taxes	Monthly	$23.28
Total per Capita (General and State Street Aid funds)		**$99.46**

EXPENDITURE ESTIMATES

I have but one lamp by which my feet are guided, and that is the lamp of experience. I know no way of judging of the future but by the past.

Patrick Henry (1736–1799)
Speech in the Virginia Convention, March 1775

Now that you know the basics of estimating revenue, you should have no trouble estimating expenditures. Often, the same method is applicable here: past history is a good indication of future performance. If, for the last two years, you haven't spent as much on office supplies as budgeted, chances are you won't spend as much in the upcoming year. However, there are always unusual circumstances that must be addressed, but overall, this is a useful method for estimating expenses.

Chart of Accounts

The following comments apply to revenues, as well as to expenditures, but we have chosen to use expenditures to stress the benefits of a chart of accounts. Expenditure accounts are far more numerous than revenues in the typical city budget. Each city must determine the optimum number of line items required for financial management. Too few or too many accounts will decrease the ability of financial managers to properly analyze cost centers. For example, it is difficult to hold down electric costs if they are included in a single line item with other types of utility expenses.

The chart of accounts found in the comptroller's *Uniform Accounting Manual* should be used in the city's budget, accounting records, and annual audit. This applies to any other finance-related activity. The benefits are uniformity in the city's total financial picture, reduced audit costs, and simplicity if a city has or is going to have an automated accounting system. Furthermore, it is important that the same level of detail is used throughout finance documents. If utilities are listed separately in the budget and accounting records, but the auditor groups all utilities together, then obtaining the specific data you need to begin your budget next year is very difficult.

Projections

For accounting purposes all expenses are classified first by fund, second by function (general government, public safety, public works, etc.) and, finally, by object. The state comptroller's *Uniform Accounting Manual* places all expenses in one of eight major object classifications.

For the purpose of making projections, all expenses can be placed in one of five categories:

1. Personnel services;
2. Contractual services, supplies and materials;
3. Fixed charges;
4. Debt service;
5. Capital outlay.

Personnel Services

Personnel and associated expenses are among the largest expenditure items of any municipal operation. Salary expense projections for the current year can be obtained by multiplying current salaries by the number of pay periods left in the year, adjusting for any changes that will occur before the end of the year and adding to this the actual year-to-date totals. A similar system can be used to make current year projections of fringe benefit costs.

When making projections for the next fiscal year it is important that those preparing the budget use a format that clearly identifies current personnel costs and the impact of any proposed increases. Such analysis should be prepared on a departmental basis so that current costs and increases can be related directly to municipal services. This analysis should be prepared using a format similar to the one shown below. It provides a salary breakdown for each authorized position and for each employee within a department. After salaries are computed and a departmental total is reached, annual costs should be computed for fringe benefits using present rates or percentages.

The sixth column of the personnel cost worksheet is used to list projected salaries without any increases except those provided by guaranteed steps within an existing pay plan. It also is used to show increased fringe benefits based upon the percentage or fixed costs estimated for the coming year. Each city should attempt to obtain percentages for Social Security, retirement and unemployment compensation for the coming fiscal year from the respective offices that manage each item. Contact your hospitalization insurance agent about projected increases if the city pays any portion of such premiums. The total of the sixth column shows the governing body what personnel costs will be for the coming year if no across-the-board salary increases are granted.

The seventh through ninth columns are used to project across-the-board percentage increases

Personnel Cost Worksheet

Fund: ____________________

Department: ____________________

	Current				Without Increase	With ___% Increase		
Position	**Employee**	**Hourly**	**Monthly**	**Annually**	**Annually**	**Hourly**	**Monthly**	**Annually**
Police Chief	John Doe	—	$2,196	$26,350	$26,350			
Sergeant	Vacant	—	$1,946	$23,350	$23,350			
Patrolman	John Smith	$9.13	$1,583	$19,000	$19,000			
Total Salaries		**$9.13**	**$5,725**	**$68,700**	**$68,700**			
		Hourly	**Monthly**	**Annually**	**Annually**	**Hourly**	**Monthly**	**Annually**
Total Costs	Salaries	$9.13	$5,725	$68,700	$68,700			
	OASI							
	Retirement							
	Health Ins.							
	Unemploy.							
TOTAL								

and to adjust all associated costs. Before making a projection, you should make comparisons with previous years' efforts and with what neighboring cities are doing (you can use the MTAS *Salary Survey*), and you should discuss it in advance with the governing body.

Contractual Services, Supplies and Materials

The calculation process discussed in the section on revenues is applicable here and is important to these expenditures. A city should use two years of actual data taken from the immediate previous fiscal years' audits. The city also should calculate expenses for the entire current year period. The method for making calculations was discussed in the revenue section. However, for expenditures, a city should not forget any extraordinary disbursements for the current year that may not develop until April, May or June. When projecting expenditures, it is better to over-project than under-project. Expenses, especially utility costs, are determined largely by unit costs and usage. It is difficult for cities to affect unit costs except through purchasing methods that seek the lowest price and take advantage of bulk consumption. However, such efforts may not be successful, especially when dealing with a limited number of suppliers. The only other recourse is to reduce consumption, which has proven successful in utility costs. The city should contact each utility to obtain a projection of increases expected in the coming year. Once that percentage is obtained, it should be multiplied by estimated current year costs to reach next year's projection. If information is not available, use past history to determine the trend in annual increases, and apply this to the estimated current year costs.

Applying an estimated percentage of increase is about the only way to project other expenses in this category, such as repair and maintenance. One should note proposed changes in present or future operations that might affect such projections. For example, adding police cars can increase repair and maintenance expenses; however, replacing high maintenance cars with new ones could reduce those costs.

Fixed Charges

Fixed charges include items such as insurance, bonds, rents, data processing services, etc. These are among the easiest expenses to project since they are based on fixed costs that can be obtained from the appropriate supplier.

Debt Service

Each city with outstanding debt obligations should develop and maintain a payment schedule for each debt. The city's auditor can help prepare the schedule and update it to reflect principal and interest due during the coming fiscal year. The schedule should provide the necessary information on a monthly basis.

Once the schedule is prepared, a cash flow plan should be developed so that each fund is paying an appropriate share on a monthly basis. Monthly set asides will prevent bonds or interest coming due without sufficient money on hand to meet the obligation. This information can be used to project debt service expenses for the next fiscal year.

Capital Outlay

This category includes the purchase of land, buildings, equipment and improvements. Projections of these expenses should be based on contracts, if available; otherwise estimates obtained from suppliers or consulting engineers should be used. Use the largest estimate or an average of several estimates to budget for equipment purchases.

State Street Aid

MTAS periodically publishes articles and reports with information for local governments. One of these reports is on the proper and improper uses of State Street Aid entitled *State Street Aid Fund Expenditures, On the Road to Understanding*. State Street Aid is a restricted fund and cannot be combined with any other fund. If you have specific questions, please refer to this publication.

Enterprise Funds

Budgeting expenditures for Enterprise Funds, such as water or sewer, does not differ from what has been discussed for other funds except for two important points. Fund balances that are referred to in Enterprise Funds as retained earnings are not supposed to be used to fund coming year operational expenditures except to assist in cash flow shortages during the year or for plant additions. Also, an item called depreciation that does not normally appear in other funds is a required item in an Enterprise Fund based upon the amount of undepreciated plant value. Depreciation is not an actual cash payment item but should be budgeted after consultation with the auditor on the proper amount of undepreciated plant value to schedule for the coming year. The auditor will then charge out such depreciation at the end of the fiscal year. The reason for budgeting depreciation is to assure that money is set aside for the replacement of a plant when it wears out and to end the year with positive retained earnings.

Fund Balances

Once the current year estimates for all expenditures have been completed and balanced against estimated revenues, the resulting fund balance can be used to meet projected operational needs for the coming year in all funds except Enterprise Funds.

CAPITAL BUDGETS AND MULTI-YEAR BUDGETS

We estimate the wisdom of nations by seeing what they did with their surplus capital.

Ralph Waldo Emerson,
"Wealth," *English Traits* (1856)

Overview

The International City/County Management Association publication *Budgeting: A Guide for Local Governments* defines a capital budget as "a spending plan for improvements to or acquisition of land, facilities, and infrastructure." The definition continues by describing its elements: "The capital budget (1) balances revenues and expenditures, (2) specifies the sources of revenues, (3) lists each project or acquisition, and (4) must ordinarily be approved by the legislative body."

Capital Budget vs. Operating Budget

How is a capital budget different from the adopted operating budget? The capital budget is a subset of the adopted budget. A municipality can have a regular budget without a capital budget, but it can't have a capital budget without a regular budget. Furthermore, state laws do not require capital budgets.

Capital budgets typically operate on a project length schedule rather than a fiscal year schedule. Capital budgets also mark the first year of a Capital Improvement Program (CIP) or multi-year budget, which typically spans five years. The CIP should be updated every year to review expected revenues, inflation, project length, project necessity, and prioritization.

So why go to the trouble? For large projects that will take more than one year to complete or finance and for projects that are not financed by proprietary or trust funds, having a separate place to track the project and its expenses is much easier. In addition, these are very expensive (typically over $25,000) undertakings and deserve closer attention and scrutiny. Furthermore, this type of long-term planning helps set priorities, forces consideration of life expectancies of facilities and equipment, allows multi-year financing for projects that could otherwise not be attempted without debt issuance, improves cash management by simplifying debt retirement, and rating agencies look favorably upon cities with CIPs.

Developing a Capital Budget

The first step in developing a capital budget is to plan. This includes setting a calendar (much like the one for the annual budget); creating an inventory of equipment, buildings, and facilities; assessing the status of current large projects, including funding and targeted completion dates; identifying future needs; and finally prioritizing the items. All departments need to be involved in this process.

The next step is to look at finances. Assess and establish your financing options (Can we pay for this in cash if we set aside $10,000 each year for five years? Is lease/purchase a better option? What about issuing a bond for the new public works garage?); determine financial limits (How much will we have to work with in two years?); and determine your current debt obligations (We owe $2,000 on this loan and will have it paid off in the middle of next year).

The last stage of the capital budgeting process is implementation. The CIP normally is approved by resolution, with the first year of the program (the capital budget) adopted as a separate section in the annual budget. As mentioned earlier, once the program has been adopted and firms are hired, land is purchased, and construction begins, close scrutiny of these large and expensive projects will save you a lot of headaches and, potentially, bad publicity in the future.

BUDGET EXECUTION

The honor of my country shall never be stained by an apology from me for the statement of truth and the performance of duty; nor can I give any explanation of my official acts except such as is due to integrity and justice and consistent with the principles on which our institutions have been framed.

Andrew Jackson (1767–1845), U.S. President. Seventh annual message to Congress, December 7, 1835. *Compilation of the Messages and Papers of the Presidents*, Vol. II, Ed. J.D. Richardson, Washington (1908)

Overview

Okay, you've learned about the different funds, you set your calendar, you researched your revenues and expenditures, you compiled them into a meaningful document, you met your deadlines, and the governing body adopted the budget. Whew! Now you can sit back and relax until next spring, right? Sorry, try again. The last phase of budgeting is execution. Although you might like to try out a guillotine on someone, we're talking about putting the plan into action.

Budget execution requires overseeing revenue collections, purchases, cash management, and proper accounting and auditing. What are some of the rules you need to follow here? Again we look to the *Tennessee Code Annotated* for guidance. Chapter 56 of Title 6 offers us the most guidance. There we find the Municipal Budget Law of 1982 and the Municipal Purchasing Law of 1983.

The general provisions of this chapter include items such as the requirement of audits, where the municipality can legally invest idle money (bonds, notes, and treasury bills; nonconvertible debt securities; U.S. guaranteed obligations; certificates of deposit; money market funds; and the local government investment pool to name a few); how soon you must deposit the money you've collected (within three working days); and the short and sweet statement that "All expenditures of money made by a municipality must be made for a lawful municipal purpose" (*T.C.A.* 6-56-112).

The Municipal Budget Law of 1982

Some items in the Municipal Budget Law of 1982 that we haven't covered include the fact that municipalities can't plan to spend more money than they expect to receive (*T.C.A.* 6-56-205); municipalities can't levy property taxes until a budget ordinance has been adopted (*T.C.A.* 6-56-207); the budget officer has the right to transfer money from one appropriation to another within the same fund and must report the transfer to the governing body and have the transfer recorded in the minutes (*T.C.A.* 6-56-209); and any money left over at the end of the fiscal year is credited to its appropriate fund for further appropriation (*T.C.A.* 6-56-211).

The Municipal Purchasing Law of 1983

The Municipal Purchasing Law of 1983 is where you'll find the statement "All purchases made from funds subject to the authority of this part shall be made within the limits of the approved budget, when required, and the appropriations, when required, for the department, office or agency for which the purchase is made" (*T.C.A.* 6-56-303). As if you didn't already know, you can't spend it if it wasn't approved.

This law also covers advertising and bidding requirements, the exceptions to those requirements, and the authority of municipalities to increase and/or lower advertisement and bidding amounts. One of the exceptions to the advertising and bidding requirements is emergencies.

T.C.A. 6-56-304(3) states:

> *A record of any such emergency purchase shall be made by the person or body authorizing such emergency purchases, and shall specify the amount paid, the items purchased, from whom the purchase was made and the nature of the emergency. A report of any emergency purchase shall be made as soon as possible to the municipal governing body and the chief executive officer of the municipality, and shall include all items of information as required in the record.*

The purchasing law also refers to Part 10 of the Public Purchases Chapter of *T.C.A.* Title 12 regarding purchases for local governments: public auctions, buying from other local governments, competitive bidding, and cooperative purchasing agreements. These subjects are covered extensively in other MTAS publications and technical bulletins so they won't get much coverage here, except to note that compliance with these regulations is very much a part of budget management and control.

Monitoring

The most important step of the budget process follows adoption: monitoring revenues and expenditures for the budget year. A few basic practices will help you adequately monitor the income and expenditures of your city.

First, devise a monthly report in order to give officers and department heads a current picture of the city's finances.

Second, during the course of the fiscal year, prepare a quarterly or mid-year budget review. This will help with the third most important aspect of the monitoring process: budget amendments. Even the best budget will miss a line item or several line items. The law allows for amendments to the budget in order to bring actual expenditures in line with the budget.

It is impossible to overemphasize the need for budget monitoring. Without it, the budget process is incomplete and may place the city in a tenuous financial position. Audit reports should be used to streamline accounting operations.

Charitable Contributions

One budget management issue that comes up frequently is the subject of charitable contributions. How many times have you been asked to contribute to the high school marching band, the Dixie Youth League, the Boy Scouts, the Girl Scouts, or a family who lost everything in a house fire? While your heart may go out to each one of those groups, oftentimes city money can't. The attorney general has issued several opinions on the subject, and you can refer to Appendix F for a few examples of them. Before the governing body agrees to donate money, be very sure that the charity meets all legal requirements (*T.C.A.* 6-54-111):

> *For the purposes of this section, [a] "nonprofit charitable organization" is one in which no part of the net earning inures or may lawfully inure to the benefit of any*

private shareholder or individual and which provides year-round services benefiting the general welfare of the residents of the municipalities.

For the purposes of this section, nonprofit civic organization means a civic organization exempt from taxation pursuant to 501(c)(4) or (c)(6) of the Internal Revenue Code of 1954, as amended, which operates primarily for the purpose of bringing about civic betterments and social improvements through efforts to maintain and increase employment opportunities in the municipality by promoting industry, trade, commerce, tourism and recreation by inducing manufacturing, industrial, governmental, educational, financial, service, commercial, recreational, and agricultural enterprises to locate in or remain in the municipality.

In addition to meeting these strict requirements, any nonprofit organization that seeks a contribution from your municipality must give the city clerk a copy of its annual report, including its audit, its program that serves the residents of the community and the proposed use of the municipal funds.

There is one loophole in this legislation. Municipalities may make appropriations to nonprofit organizations other than charitable organizations, but only after publishing in a newspaper the municipality's intent to make the contribution and specifying the intended amount and the purpose for which the money will be spent.

In addition to *T.C.A.* requirements, the comptroller's office has prepared guidelines for making donations. One of the requirements is that "The governing body of each municipality shall adopt a special resolution, stating the purpose for which funds are being appropriated for each nonprofit charitable organization or nonprofit civic organization that is to receive municipal funds."

Furthermore, payments made to these organizations "… shall be limited to the amounts appropriated for such purposes and in keeping with the municipality's guidelines for how the appropriated funds may be spent." See Appendix G for a sample resolution that complies with the comptroller's requirement.

Finally, there is a slight discrepancy between state statute and the comptroller's guidelines as to which nonprofit charitable and nonprofit civic organizations are eligible to receive municipal money. As previously mentioned, state statute allows contributions to groups classified as 501(c)(4) and (c)(6); however, in the comptroller's compliance manual, 501(c)(3) organizations also are listed as permissible. 501(c)(3) groups consist of charities and religious, educational, scientific, and literary groups, as well as those that test for public safety, foster national or international amateur sports competition, and aim to prevent cruelty to children or animals. 501(c)(4) groups on the other hand include civic leagues, community organizations, and other social welfare organizations, while 501(c)(6) organizations are trade associations, chambers of commerce, real estate boards, and other business leagues.

AUDIT

The first thing to be done by a biographer in estimating character is to examine the stubs of his victim's cheque-books.

Silas Weir Mitchell (1829–1914), U.S. physician, author.
Quoted in Harvey Cushing, *Life of Sir William Osler*, Vol. 1, Ch. 21 (1925)

The audit is the last phase of the budget cycle. As mentioned earlier, the audit is prepared after the fiscal year ends but usually before the end of the calendar year. Steps involved in acquiring an audit include creating a request for proposal, accepting proposals, selecting a firm or accountant to conduct the audit, agreeing to a contract, having the contract approved by the state, doing audit preparation work for the auditor, hosting the auditor at city hall during the field visit, responding to any findings, and having the governing body receive and accept the audit report.

If you have done an adequate job of budget execution, the audit should go very smoothly with few or no findings. Referring to GAAFR for one last definition, a finding is a "published communication of an internal control weakness or instance of noncompliance…" This is where your auditor tells you that you have room for improvement.

The basic components of an audit are the introductory, financial and statistical sections. The introductory section usually consists of a report cover, title page, table of contents, list of principal officials, an organizational chart, and a letter of transmittal. The financial section includes the independent auditor's report, management's discussion and analysis (MD&A), basic financial statements, required supplementary information (RSI) and combining and individual fund presentations and supplementary information. Finally, the statistical section comprises trend data (over the previous 10 years) and other non-financial information that is useful in determining a city's credit worthiness.

Most city officials and employees will refer to the audit only when they are preparing the next year's budget. However, the audit also may be pulled off the shelf when a credit ranking agency calls, when the city is interested in issuing debt, when fund balance is discussed as a funding source for an unexpected expense, and when you need to know about transfers between funds.

SUMMARY

Vision without action is a daydream. Action without vision is a nightmare.

Japanese proverb

This manual is designed to give Tennessee city employees and elected officials a broad overview of the budgeting process with general instructions on how to complete and compile a budget that complies with state and federal laws and guidelines. It is hoped that you now know the difference between governmental, proprietary, and fiduciary funds; how to budget estimated revenues and expenditures; and how to properly execute your budget. In addition, you should know how a capital budget differs from the annual operating budget and multi-year budgets. Armed with this knowledge, you should be able to breeze through all phases of the budget cycle: preparation, approval, execution and audit, all in time to turn around and do it again next year.

Appendix A: DRUG FUND GUIDELINES

DRUG FUND "CHEAT SHEET"

by Rex Barton, Police Management Consultant

[The Drug Fund is a] special revenue account authorized by *T.C.A.* 39-17-420: "All fines and forfeitures of appearance bonds … and the proceeds of goods seized and forfeited … and disposed of according to law, shall be accounted for in a special revenue fund of the jurisdiction that initiated the arrest. All financial activities related to funds received under this part shall be accounted for in this fund." Listed below are some guidelines that cities should use (and are required to by law) in accounting for these funds.

The account is under the control of the city recorder. The police chief and the mayor or chief executive officer will recommend a budget for the special revenue fund to be approved by the governing body. It is best to budget for all the money in the account. You do not have to spend the money, but you cannot spend money that has not been appropriated. Any money left over at the end of the year will carry over to the next year's fund balance. You need to ensure that you keep an amount in the account equal to at least 20 percent of the revenues coming in. You can spend only as much money as you have budgeted, and you can spend only as much money as is in the account. In other words, you can't spend money that you anticipate receiving until you have actually received it.

REVENUES – Allowable deposits of funds into the Drug Fund Account.

A. **Fines for drug offenses.** The Sessions or Criminal Court returns fines for all drug offenses to the city. The city deposits 50 percent of fine revenue into the drug fund and 50 percent into the city's general fund. Note: the 50/50 split applies ONLY to drug offense fine revenue. *T.C.A.* 39-17-428 specifies certain minimum fines for different classifications of most drug charges.

B. **Forfeited cash.** Any cash seized pursuant to the drug control laws that is ultimately awarded to the city goes into the drug fund pursuant to *T.C.A.* 53-11-451.

C. **Proceeds from the sale of items seized pursuant to the drug laws that are ultimately forfeited to the city.** All proceeds from the sale of these items go into the drug fund pursuant to *T.C.A.* 53-11-451. The items themselves, usually vehicles, may be used for drug enforcement activities. They cannot be used for other city activities, such as using a forfeited pick-up truck at the wastewater treatment plant.

D. **Proceeds from the sale of vehicles seized and forfeited for DUI offense.** Vehicles may be seized when a driver is arrested for a second or subsequent DUI. Proceeds from the sale must be used for "law enforcement or drug education."

E. **Contributions.** As part of a plea bargain, there may be some amount of money contributed to the city's drug fund. Civic organizations also may contribute funds.

F. **Budget allocations.** The governing body may allocate general fund money to the drug fund.

EXPENDITURES – Allowable uses for funds in the Drug Fund Account.

A. **Local drug treatment programs.** Drug fund money can be used to fund local drug treatment programs. Expenditures must be made in accordance with local purchasing guidelines.

B. **Drug education.** The drug fund can be used to fund drug education programs. Typical examples are the D.A.R.E. program, anti-drug magazines or literature, and anti-drug billboards.

C. **Drug enforcement.** The drug fund can be used for any legitimate drug enforcement activity, operational or capital. Although we strongly recommend against it, drug enforcement salaries may be paid from the drug fund.

There are two types of drug enforcement expenditures: regular and confidential. Regular drug enforcement expenditures include the purchase of surveillance equipment and drug identification kits, maintenance on a narcotics officer's vehicle, and drug enforcement officers' monthly cell phone bills, etc. Confidential expenditures include money paid to informants; gasoline for informants' vehicles; and money spent purchasing drugs, etc.

D. **Non-recurring *general* law enforcement expenditures.** Generally, but not always, these are capital purchases. These expenditures do not have to be related to drug enforcement, but they cannot be operational expenditures. Legitimate examples include vehicles, standard equipment for the vehicles, body armor, weapons, and computers.

Examples of items that cannot be purchased as non-recurring general law enforcement purposes are uniforms, ammunition, general law enforcement officer's cell phone bill or salary, and jackets for the police department.

ACCOUNTING FOR DRUG FUND MONEY – Required accounting practices for the Drug Fund Account

A. **Special Revenue Account**

ALL revenues destined for the drug fund MUST go into a special revenue account under the control of the city recorder.

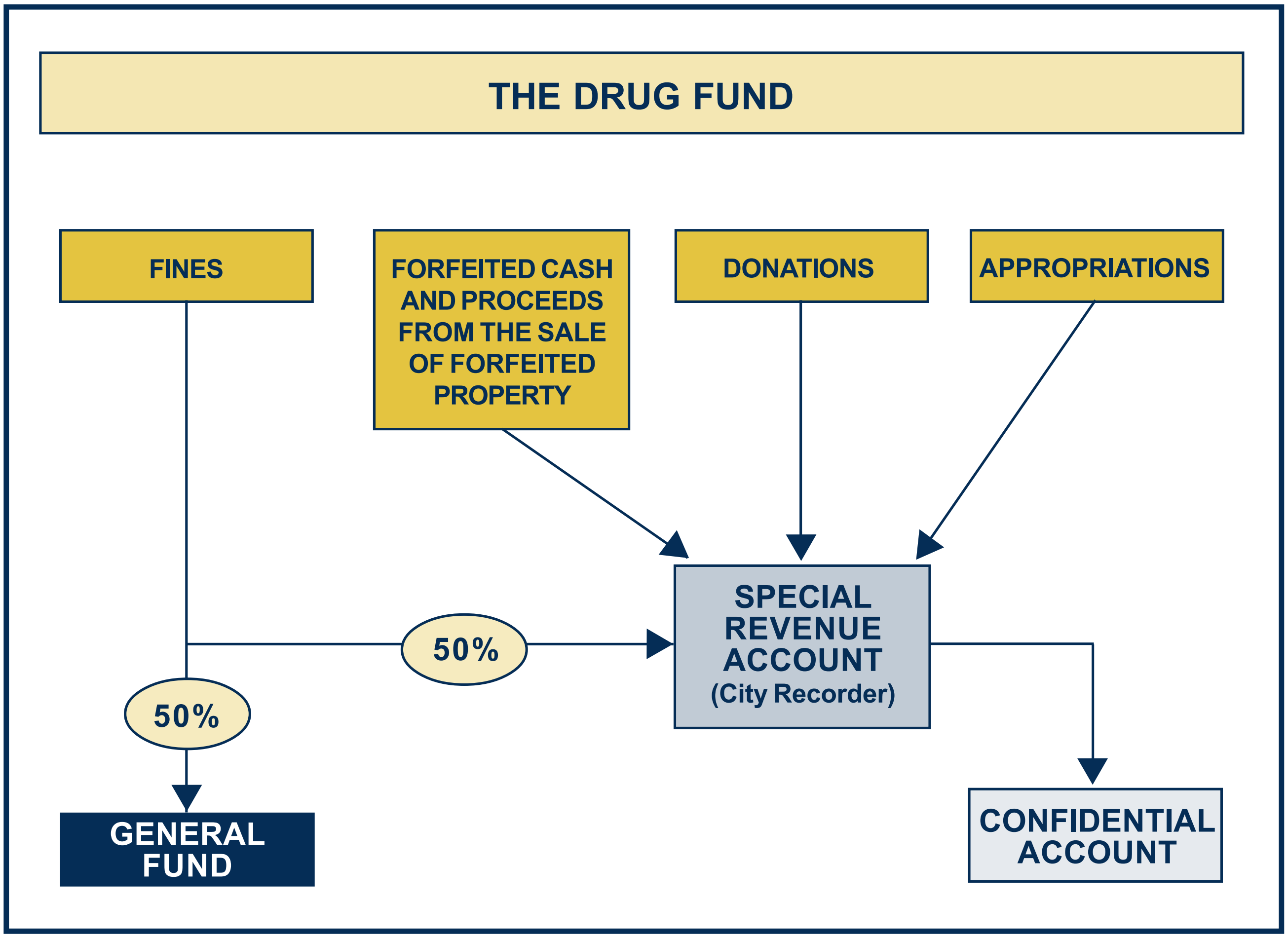
The special revenue account should be handled in the same way as other special revenue accounts such as those for street aid or solid waste.

With the exception of confidential expenditures, all expenditures MUST follow the city's purchasing guidelines.

B. **Confidential expenditures**

Confidential money must be accounted for according to *Procedures for Handling Cash Transactions Related to Undercover Investigative Operation of County and Municipal Drug Enforcement Programs* prepared by the comptroller's office.

Generally, for confidential expenditures the police chief requests that the city recorder write him/her a check from the Drug Fund Account. The chief then deposits the check into a separate bank account over which the chief has control. Next, the chief writes a check to an undercover agent/officer who cashes the check. Unused funds should be returned to the recorder. The police department will generally keep SOME funds in the account or may keep cash for immediate needs.


THE DRUG FUND
FINES
FORFEITED CASH AND PROCEEDS FROM THE SALE OF FORFEITED PROPERTY
DONATIONS
APPROPRIATIONS
SPECIAL REVENUE ACCOUNT (City Recorder)
50%
50%
GENERAL FUND
CONFIDENTIAL ACCOUNT

Appendix B: BUDGET DOCUMENTS

SAMPLE PUBLIC NOTICE

The City of Everywhere, Tennesseee, hereby provides certain financial information for the 2003-2004 fiscal year budget in accordance with provisions of Chapter 484, Public Acts of 1991, as amended. There will be a public hearing concerning the budget at City Hall on June 17, 2003, at 7:00 p.m. All citizens are welcomed to attend and to participate.

	ACTUAL 2001-2002	ESTIMATED 2002-2003	PROPOSED 2003-2004
GENERAL FUND			
Estimated Revenue			
Local Taxes	$4,260,000	$4,214,500	$4,260,000
State of Tennessee	550,000	534,500	550,000
Federal Government	50,000	50,000	50,000
Other Sources	330,000	338,000	320,300
Total	**$5,190,000**	**$5,137,000**	**$5,180,300**
Estimated Expenditures			
Salaries	$2,400,000	$2,420,000	$2,496,000
Other Costs	2,513,175	2,466,130	2,616,800
Total	**$4,913,175**	**$4,886,130**	**$5,112,800**
Estimated Fund Balance			
Beginning	$1,500,000	$1,776,825	$2,027,695
Ending	$1,776,825	$2,027,695	$2,095,195
Employee Positions	85	87	88
STATE STREET AID FUND			
Estimated Revenue			
State of Tennessee	$57,000	$56,000	$57,000
Other Sources	2,800	2,300	3,000
Total	**$59,800**	**$58,300**	**$60,000**
Estimated Expenditures			
Salaries	$15,000	$16,000	$15,000
Other Costs	64,200	33,400	40,200
Total	**$79,200**	**$49,400**	**$55,200**
Estimated Fund Balance			
Beginning	$20,000	$600	$9,500
Ending	$600	$9,500	$14,300
Employee Positions	0	0	0

SAMPLE BUDGET ORDINANCE

ORDINANCE NO. 03-12

AN ORDINANCE OF THE CITY OF EVERYWHERE, TENNESSEE, ADOPTING A BUDGET FOR THE FISCAL YEAR JULY 1, 2003, THROUGH JUNE 30, 2004.

BE ORDAINED BY THE CITY OF EVERYWHERE, TENNESSEE, AS FOLLOWS:

SECTION 1. A budget consisting of the Available Funds and Appropriations listed in SECTION 2 and SECTION 3 below be adopted for the Fiscal Year July 1, 2003, through June 30, 2004.

SECTION 2. Available Funds for said budget are as follows:

GENERAL FUND

Local Taxes	$4,260,000	
Intergovernmental Revenue	600,000	
Fines and Forfeitures	113,300	
Miscellaneous Revenues	207,000	
Fund Balance	2,027,695	
Total Available Funds - General Fund		$7,207,995

STATE STREET AID

Intergovernmental Revenues	$57,000	
Miscellaneous Revenues	3,000	
Fund Balance	9,500	
Total Available Funds - State Street Aid Fund		$69,500

DRUG FUND

Court Fines and Costs	$4,000	
Fund Balance	3,500	
Total Available Funds - Drug Fund		$7,500

WATER AND SEWER FUND

Revenues	$2,542,000	
Estimated Available Cash	$808,000	
Total Available Funds - Water and Sewer Fund		$3,350,000

NATURAL GAS FUND

Gas Revenues	$4,745,000	
Estimated Available Cash	$435,000	
Total Available Funds - Natural Gas Fund		$5,180,000

Total All Funds $15,814,995

SECTION 3. Appropriations for said budget are as follows:

GENERAL FUND

General Government	$2,073,200	
Police	880,500	
Fire	826,000	
Streets	672,000	
Parks and Recreation	661,100	
Total General Fund		$5,112,800

STATE STREET AID

Streets	$55,200	
Total State Street Aid Fund		$55,200

DRUG FUND

Police	$5,000	
Total Drug Fund		$5,000

WATER AND SEWER FUND

Expenses	$2,385,900	
Total Water and Sewer Fund		$2,385,900

NATURAL GAS FUND

Expenses	$4,466,000	
Total Natural Gas Fund		$4,466,000

Total All Funds $12,024,900

SECTION 4. No appropriation listed above may be exceeded without appropriate ordinance action to amend budget.

SECTION 5. A detailed line-item financial plan shall be prepared in support of the budget.

SECTION 6. All unencumbered balances of appropriations remaining at the end of the fiscal year shall lapse and revert to the respective fund balance.

SECTION 7. The appropriations of this budget shall become the appropriations for the next fiscal year until the budget for the next year has been adopted.

SECTION 8. There is hereby levied a property tax of $1.00 per $100 of assessed valuation for the purpose of funding General Fund services.

SECTION 9. This ordinance shall take effect July 1, 2003, the public welfare requiring it.

SAMPLE BUDGET NARRATIVE

CITY OF EVERYWHERE, TENNESSEE
2003-2004 FISCAL YEAR BUDGET
FUND 110 - GENERAL FUND

110 GENERAL FUND REVENUES	2001-2002 Actual	2002-2003 Year End Est.	2003-2004 Proposed
LOCAL TAXES			
31100 Property taxes	$2,000,000	$1,986,000	$2,000,000
31120 Public utilities tax	50,000	50,000	50,000
31200 Prior year taxes	30,000	28,000	30,000
31300 Penalty and interest	10,000	9,500	10,000
31500 In lieu of taxes	40,000	40,000	40,000
31600 Local sales tax	1,500,000	1,480,000	1,500,000
31710 Wholesale beer tax	350,000	345,000	350,000
31800 Business taxes	250,000	246,000	250,000
31912 Cable TV tax	30,000	30,000	30,000
Total Taxes	**$4,260,000**	**$4,214,500**	**$4,260,000**
LICENSES AND PERMITS			
32610 Building licenses	$40,000	$42,000	$42,000
Total Licenses and Permits	**$40,000**	**$42,000**	**$42,000**
INTERGOVERNMENTAL			
33100 Federal grant (cops)	$50,000	$50,000	$50,000
33510 State sales tax	370,000	360,000	370,000
33520 State income tax	60,000	55,000	60,000
33530 State beer tax	10,000	9,500	10,000
33553 State streets and transportation	20,000	21,000	20,000
33591 State TVA gross receipts	60,000	58,000	60,000
33593 Excise tax	30,000	31,000	30,000
Total Intergovernmental	**$600,000**	**$584,500**	**$600,000**
FINES AND FEES			
35100 Court fines and fees	$110,000	$115,000	$113,300
Total Fines	**$110,000**	**$115,000**	**$113,300**
MISCELLANEOUS			
36100 Interest earned	$130,000	$125,000	$130,000
36300 Sale of fixed assets	30,000	50,000	15,000
36930 Note proceeds (TML bond fund)	0	0	0
36990 Miscellaneous	20,000	6,000	20,000
Total Miscellaneous	**$180,000**	**$181,000**	**$165,000**
TOTAL GENERAL FUND REVENUE	**$5,190,000**	**$5,137,000**	**$5,180,300**
BEGINNING FUND BALANCE	**$1,500,000**	**$1,776,825**	**$2,027,695**
TOTAL AVAILABLE FUNDS	**$6,690,000**	**$6,913,825**	**$7,027,995**

Sample Budget Narrative continued

CITY OF EVERYWHERE, TENNESSEE
2003-2004 FISCAL YEAR BUDGET
FUND 110 - GENERAL FUND

110 GENERAL FUND EXPENDITURES		2001-2002 Actual	2002-2003 Year End Est.	2003-2004 Proposed
41000	**GENERAL GOVERNMENT**			
111	Salaries	$400,000	$400,000	$416,000
141	FICA	30,600	30,600	32,000
142	Hospital and health insurance	750,000	750,000	780,000
146	Workers' compensation	90,000	90,000	93,000
148	Employee education & training	15,000	10,000	15,000
211	Postage	20,000	20,500	21,000
235	Memberships, registration fees	12,000	11,500	12,000
240	Utilities	65,000	68,000	72,000
245	Telephone	15,000	14,000	15,000
252	Legal services	13,000	11,000	13,000
255	Data processing support service	15,000	15,000	15,600
311	Office supplies	15,000	12,500	15,600
510	Liability insurance	35,000	37,000	38,000
610	Bond principal	230,000	235,000	245,000
630	Bond interest	300,000	300,000	285,000
790	Miscellaneous	5,000	4,500	5,000
	Subtotal	**$2,010,600**	**$2,009,600**	**$2,073,200**
900	Capital outlay	10,000	10,000	0
	Total General Government	**$2,020,600**	**$2,019,600**	**$2,073,200**
42100	**POLICE DEPARTMENT**			
111	Salaries	$600,000	$610,000	$624,000
141	FICA	45,900	46,665	48,000
148	Employee education & training	15,000	14,500	15,600
245	Telephones	12,000	12,800	12,500
280	Travel expense	5,000	6,000	5,200
311	Office supplies	4,000	4,200	4,200
326	Uniforms	20,000	18,000	2,080
331	Gas and oil	22,000	23,000	23,000
332	Vehicle parts & repair	19,000	20,000	20,000
510	Liability insurance	30,000	30,000	31,200
790	Miscellaneous	10,000	11,000	10,000
	Subtotal	**$782,900**	**$796,165**	**$814,500**
900	Capital outlay	66,000	50,000	66,000
	Total Police Department	**$848,900**	**$846,165**	**$880,500**

Sample Budget Narrative continued

CITY OF EVERYWHERE, TENNESSEE
2003-2004 FISCAL YEAR BUDGET
FUND 110 - GENERAL FUND

		2001-2002 Actual	2002-2003 Year End Est.	2003-2004 Proposed
110 GENERAL FUND EXPENDITURES				
42200	**FIRE DEPARTMENT**			
111	Salary	$550,000	$540,000	$572,000
141	FICA	42,075	41,310	44,000
148	Employee education and training	20,000	13,000	20,000
240	Utilities	7,000	6,500	7,400
245	Telephone	4,000	3,800	4,200
264	Equipment maintenance	28,000	29,000	30,000
280	Travel	5,000	4,000	5,200
326	Uniforms	16,000	16,000	16,800
331	Gas and oil	15,000	15,200	15,600
510	Liability insurance	20,000	20,000	20,800
790	Miscellaneous	10,000	6,000	10,000
	Subtotal	**$717,075**	**$694,810**	**$746,000**
900	Capital outlay	50,000	50,000	80,000
	Total Fire Department	**$767,075**	**$744,810**	**$826,000**
43100	**STREETS**			
111	Salaries	$400,000	$410,000	$416,000
141	FICA	30,600	31,365	32,000
268	Repair and maintenance	54,000	53,000	55,000
331	Gas and oil	20,000	21,000	22,000
350	Material and supplies	50,000	49,000	52,000
790	Miscellaneous	15,000	12,000	15,000
	Subtotal	**$569,600**	**$576,365**	**$592,000**
900	Capital outlay	0	0	0
931	Street contract/paving	60,000	58,000	80,000
	Total Streets	**$427,200**	**$634,365**	**$672,000**

Sample Budget Narrative continued

TENNESSEE
2002-2003 FISCAL YEAR BUDGET
FUND 110 - GENERAL FUND

110 GENERAL FUND EXPENDITURES		2001-2002 Actual	2002-2003 Year End Est.	2003-2004 Proposed
44400	**PARKS AND RECREATION**			
111	Salary	$450,000	$460,000	$468,000
141	FICA	35,000	35,190	36,000
230	Publicity, subscriptions	16,000	15,500	16,000
240	Utilities	50,000	52,000	52,000
265	Contract svcs, - Grounds maint.	25,000	25,000	26,000
300	Supplies	20,000	18,000	20,800
330	Repair and maintenance supplies	16,000	16,500	16,700
790	Miscellaneous	15,000	15,000	16,600
	Subtotal	**$627,000**	**$637,190**	**$651,100**
900	Capital outlay	10,000	0	0
937	Park/recreation improvement	10,000	4,000	10,000
	Total Parks and Recreation	**$647,000**	**$641,190**	**$661,100**
	TOTAL GENERAL FUND	**$4,913,175**	**$4,886,130**	**$5,112,800**

Appendix C: MUNICIPAL REVENUES

Real Property Tax

Revenue Class: Local Taxes
Fund: General **Account No.:** 31111

Description: *Ad valorem* taxes levied within the municipality based on the following assessment ratios:

1. Residential and farm real property - 25 percent of the appraised value;
2. Commercial and industrial real property - 40 percent of the appraised value.

Authorization: Article II, Section 28 of the Tennessee Constitution, *T.C.A.* 67-5-101 et seq.; *T.C.A.* 67-1-701 et seq. and *T.C.A.* 67-1-801 et seq.

Requirements or Restrictions: Reference *T.C.A.*

Current Rate: Article II, Section 28 of the Tennessee Constitution and *T.C.A.* 67-5-801 provide that the following percentages of full value be used to determine assessments:

- Public utility real property, 55 percent;
- Industrial and commercial real property, 40 percent;
- Residential and farm real property, 25 percent.

Frequency of Payment: Annually, between the first Monday in October and before the following March 1, unless the municipality is authorized to establish other due dates.

Late Pay Penalty: See Interest and Penalties – Property Tax, Account #31300.

Exemptions: All government, religious, charitable, scientific, literary and educational properties are exempt (Article II, Section 28 of the Tennessee Constitution and *T.C.A.* 67-5-201 et seq.). Tax relief is offered to certain disabled and elderly home owners (*T.C.A.* 67-5-701).

Collection: Property taxes are usually paid directly to the municipality. Some counties collect taxes for their municipalities, as in *T.C.A.* 67-1-702.

Use Restrictions: None.

Personal Property Tax

Revenue Class: Local Taxes
Fund: General **Account No.:** 31112

Description: *Ad valorem* taxes levied on personal property used for business purposes within incorporated municipal limits, based on the following assessment ratios:

1. Public utility tangible property - 55 percent of the appraised value;
2. Commercial and industrial tangible property - 30 percent of the appraised value.

Authorization: Article II, Section 28 of the Tennessee Constitution, *T.C.A.* 67-5-901 et seq.; *T.C.A.* 67-1-701 et seq. and *T.C.A.* 67-1-801 et seq.

Requirements or Restrictions: Reference *T.C.A.*

Current Rate: Article II, Section 28 of the Tennessee Constitution and *T.C.A.* 67-5-901 provide that the following percentages of full value be used to determine assessments:

- Public utility tangible personal property, 55 percent;
- Industrial and commercial tangible personal property, 30 percent; and
- Other tangible personal property, five percent.

Frequency of Payment: Annually, between the first Monday in October and before the following March 1, unless the municipality is authorized to establish other due dates.

Late Pay Penalty: See Interest and Penalties – Property Tax, Account #31300.

Exemptions: Inventories of merchandise held by merchants and businesses for sale and exchange by persons taxable under *T.C.A.* 67-4-701.

Collection: Personal property schedules mailed out no later than February 1st by municipality; completed and returned by March 1; collection same as real property tax.

Use Restrictions: None.

Public Utility Property Tax

Revenue Class: Local Taxes
Fund: General **Account No.:** 31120

Description: Taxes levied by the municipality on those corporations that provide public utilities (i.e., telephone, railroads, gas, airlines, etc.) and that are subject to government regulation. Assessment ratio is 55 percent of appraised value.

Authorization: *T.C.A.* 67-5-801 et seq. and *T.C.A.* 67-5-901 et seq.

Requirements or Restrictions: Reference *T.C.A.*

Current Rate: Public utility real property and tangible personal property, 55 percent.

Frequency of Payment: Annually, between the first Monday in October and before the following March 1, unless the municipality is authorized to establish other due dates.

Late Pay Penalty: See Interest and Penalties – Property Tax, Account #31300.

Exemptions: Some classes of business have successfully challenged in court their classification as a "Public Utility." Specifically, trucking companies are no longer considered public utilities. Exceptions to the public utility definition can be found in *T.C.A.* 65-4-101.

Collection: The public utilities tax roll is established and maintained by the state. Complete tax roll and tax bills are mailed to the municipality at the beginning of each calendar year, which in turn re-mails the tax bill to individual taxpayers.

Use Restrictions: None.

Property Taxes: Prior Years

Revenue Class: Local Taxes
Fund: General **Account No.:** 31200

Description: Many people do not pay their property taxes on the due date. This represents property tax payments from previous years that are received by the municipalities.

Authorization: Article II, Section 28 of the Tennessee Constitution, *T.C.A.* 67-5-2001 et seq.; *T.C.A.* 67-5-801 et seq.; *T.C.A.* 67-05-901 et seq.; *T.C.A.* 67-01-701 et seq. and *T.C.A.* 67-01-801 et seq.

Requirements or Restrictions: N/A

Current Rate: Article II, Section 28 of the Tennessee Constitution provides that the following percentages of full value be used to determine assessments:

- Public utility real and tangible personal property – 55 percent;
- Industrial and commercial real property – 40 percent;
- Industrial and commercial tangible personal property – 30 percent;

- Residential and farm real property – 25 percent;
- Other tangible personal property – five percent.

(Article II, Section 28 and *T.C.A.* 67-5-801 et seq., and *T.C.A.* 67-5-901 et seq.).

Frequency of Payment: Variable.

Late Pay Penalty: See Interest and Penalties – Property Tax, Account #31300.

Exemptions: N/A

Collection: There are several options for collecting delinquent property taxes, including publishing a list of delinquent taxpayers in a local newspaper, turning the delinquent list over to a tax attorney, distraint, garnishment and a tax sale. See *T.C.A.* 67-5-2001 et seq. for a complete list and procedures.

Use Restrictions: N/A

Interest and Penalties: Property Tax

Revenue Class: Local Taxes
Fund: General **Account No.:** 31300

Description: Revenue received from interest and penalties on delinquent property tax payments.

Authorization: *T.C.A.* 67-5-2010; *T.C.A.* 67-1-701 et seq. and *T.C.A.* 67-1-801 et seq.

Requirements or Restrictions: N/A

Current Rate: Penalty of one-half percent and interest of one percent imposed on March 1 and on the first day of each additional month, except as otherwise provided in reference to municipal taxes.

Frequency of Payment: N/A

Late Pay Penalty: N/A

Exemptions: For cities in any county having a population of not less than 24,600 nor more than 24,700 according to the 1980 federal census or any subsequent federal census, upon approval of two-thirds of the governing body, the rate of penalty and interest may be reduced to an amount not less than 12 percent per year in the aggregate.

Collection: Penalty and interest are collected, along with delinquent property taxes. See *T.C.A.* 67-5-2001 et seq.

Use Restrictions: None.

Payments in Lieu of Taxes: Electric Utilities

Revenue Class: Local Taxes
Fund: General **Account No.:** 31511

Description: Revenue received as payment in lieu of tax on electric system property and operations that represents the utility's fair share of the cost of local government. Payments are based upon the plant value of the electrical system. It applies only to municipalities that own an electrical distribution system.

Authorization: *T.C.A.* 7-52-301 et seq. (Municipal Electric System Tax Equivalent Law of 1987).

Requirements or Restrictions: Payments cannot be made to the municipality unless the following expenses are paid or provided for: operating expenses, debt payments, reasonable reserves or contingencies, and cash working capital adequate to cover operating expenses for a reasonable number of weeks. Cities that have private act or home rule charters that differ from these requirements should continue with their formulas for calculations until the tax equivalent payments exceed the tax equivalent amount paid in the fiscal year ending June 30, 1987. At that point the charter provisions are repealed and become subject to the *T.C.A.* requirements.

Current Rate: In-lieu-of-tax payments are computed under *T.C.A*. 7-52-304.

Frequency of Payment: Varies (in accordance with the resolution passed by the governing body – *T.C.A.* 7-52-304(4)).

Late Pay Penalty: None.

Exemptions: All underground equipment and all substation transmission lines are exempt.

Collection: Payments are transferred from the electric fund in accordance with a resolution passed by governing body (*T.C.A.* 7-52-307).

Use Restrictions: Twenty-two and one-half percent of the total tax equivalent payment is distributed to the county or counties that the system serves. Likewise, other cities that the system serves receive an amount equal to the equalized property tax rate of the other cities' taxing jurisdictions, multiplied by the net plant value of the electric plant plus the book value of materials and supplies located within the other cities' boundaries, multiplied by the assessment ratio, minus reductions required by *T.C.A.* 7-52-304(3) and (4).

Payments in Lieu of Taxes: Water Utilities

Revenue Class: Local Taxes
Fund: General **Account No.:** 31512

Description: A payment in lieu of tax that cannot exceed the amount of taxes payable on privately owned property of similar nature.

Authorization: *T.C.A.* 7-34-115 (a)(9)

Requirements or Restrictions: Must be authorized by resolution.

Current Rate: Varies by municipality.

Frequency of Payment: Established in authorizing resolution.

Late Pay Penalty: Not specified.

Exemptions: None.

Collection: Payment is made by water utility to municipality pursuant to authorizing resolution.

Use Restrictions: None.

Payments in Lieu of Taxes: Sewer Utilities

Revenue Class: Local Taxes
Fund: General **Account No.:** 31513

Description: A payment in lieu of tax that cannot exceed the amount of taxes payable on privately owned property of similar nature.

Authorization: *T.C.A.* 7-34-115 (a)(9)

Requirements or Restrictions: Must be authorized by resolution.

Current Rate: Varies by municipality.

Frequency of Payment: Established in authorizing resolution.

Late Pay Penalty: Not specified.

Exemptions: None.

Collection: Payment is made by sewer utility to municipality pursuant to authorizing resolution.

Use Restrictions: None.

Payments in Lieu of Taxes: Natural Gas Utilities

Revenue Class: Local Taxes
Fund: General **Account No.:** 31514

Description: Revenue received as payment in lieu of tax on the gas system property and operations that represents the utility's fair share of the cost of local government. Payments are based on the value of the gas system and gas operations. It applies only to municipalities that own a gas system.

Authorization: *T.C.A.* 7-39-401 et seq. (Municipal Gas System Tax Equivalent Law).

Requirements or Restrictions: Payments cannot be made to the municipality unless the following expenses are paid or provided for: operating expenses, debt payments, reasonable reserves or contingencies, and cash working capital adequate to cover operating expenses for a reasonable number of weeks.

Current Rate: In-lieu-of-tax payments are computed under *T.C.A.* 7-39-404 (1).

Frequency of Payment: Varies (in accordance with resolution passed by governing body – *T.C.A.* 7-39-404(4)).

Late Pay Penalty: None.

Exemptions: Retail sales or use taxes on gas energy at the same rates applicable generally to sales or use of personal property or services are not included in the calculations.

Collection: Payments are transferred from the gas fund in accordance with resolution passed by governing body (*T.C.A.* 7-39-405).

Use Restrictions: None.

Payments in Lieu of Taxes: Industry

Revenue Class: Local Taxes
Fund: General **Account No.:** 31520

Description: Property in this category is not subject to *ad valorem* taxes as the corporation is declared to be performing a public function on the behalf of the municipality. The corporation's lessee may make payments in lieu of *ad valorem* taxes to the municipality, provided that these payments do no exceed *ad valorem* taxes otherwise due where the leased property is owned by an entity subject to taxation.

Authorization: *T.C.A.* 7-53-305

Requirements or Restrictions: Cannot permit payment in-lieu-of taxes to be waived or otherwise not assessed for a period of more than 20 years from the date of agreement or contract unless both the commissioner of economic and community development and the comptroller have made a written determination that it is in the best interest of the state to do so.

Current Rate: N/A

Frequency of Payment: Usually annually.

Late Pay Penalty: See Interest and Penalties – Property Tax, Account #31300.

Exemptions: N/A

Collection: Payment schedule is the same as Real Property Taxes, Account #31111.

Use Restrictions: None.

Local Option Sales Tax: Countywide

Revenue Class: Local Taxes
Fund: General **Account No.**: 31610

Description: Receipts from countywide local option sales tax that is levied within the municipality.

Authorization: *T.C.A.* 67-6-701 et seq. (1963 Local Option Revenue Act)

Requirements or Restrictions: Tax can be increased only by ordinance after voters approve by referendum (*T.C.A.* 67-6-706). Tax is applicable only to the first $1,600 on the sale or use of any single article of personal property (*T.C.A.* 67-6-702).

Current Rate: Varies according to county and municipality; maximum rate is two and three-quarters percent.

Frequency of Payment: Monthly.

Late Pay Penalty: N/A

Exemptions: Same as statewide sales tax, plus electricity and fuels. See *T.C.A.* 67-6-704. Cable or wireless cable television services are exempted up to $27.50 per month (*T.C.A.* 67-6-714).

Collection: State collects (and keeps a small percentage for administrative expenses), forwards the remainder to the county, and the county distributes 50 percent for school purposes and 50 percent to the jurisdiction where collected or as contracted between jurisdictions.

Use Restrictions: None for the 50 percent returned to municipality, unless contracted differently.

Local Option Sales Tax: Municipality

Revenue Class: Local Taxes
Fund: General **Account No.:** 31620

Description: Receipts from municipal local option sales tax.

Authorization: *T.C.A.* 67-6-701 et seq. (1963 Local Option Revenue Act).

Requirements or Restrictions: Where county tax exists, municipality may levy a tax equal to the difference between the county tax and the maximum rate of two and three-quarters percent (*T.C.A.* 67-6-703). Tax can be increased only by ordinance after voters approve by referendum (*T.C.A.* 67-6-706). Tax is applicable only to the first $1,600 on the sale or use of any single article of personal property (*T.C.A.* 67-6-702).

Current Rate: Varies, but cannot exceed two and three-quarters percent.

Frequency of Payment: Monthly.

Late Pay Penalty: N/A

Exemptions: Same as statewide sales tax, plus electricity and fuels. See *T.C.A.* 67-6-704. Cable or wireless cable television services are exempted up to $27.50 per month (*T.C.A.* 67-6-714).

Collection: State collects, forwards to municipality where collected.

Use Restrictions: None.

Wholesale Beer Tax

Revenue Class: Local Taxes
Fund: General **Account No.:** 31710

Description: State authorized tax on wholesale sales of beer, 100 percent of which is retained by the municipality. Wholesale beer deliveries to retail outlets in a city or county are taxed at 17 percent of wholesale prices (excluding state and federal privilege taxes levied after May 3, 1983). The tax is paid by each beer wholesaler directly to the city or county, and monthly reports on such sales are made to the state Department of Revenue and to each city and county. A city should check that tax payments are being received from beer wholesalers serving the area based on deliveries to all retail beer outlets in the city. If there is doubt about administration of the tax, an investigation by the Department of Revenue may be requested.

Authorization: *T.C.A.* 57-6-101 et seq. (Wholesale Beer Tax Act)

Requirements or Restrictions: N/A

Current Rate: 17 percent minus three and one-half percent of total (three percent retained by wholesalers, one-half percent to the state) per case or barrel (31 gallons).

Frequency of Payment: Monthly.

Late Pay Penalty: City may institute legal action for collection (*T.C.A.* 57-6-107(b)).

Exemptions: Wholesalers may deduct this amount from their gross receipts tax liability (*T.C.A.* 67-4-711 (b)(5)). Sales are tax-free if sold to U.S. armed forces (*T.C.A.* 57-6-111).

Collection: Beer wholesalers remit monthly, directly to the municipality on state-prescribed forms.

Use Restrictions: None.

Wholesale Liquor Tax

Revenue Class: Local Taxes
Fund: General **Account No.:** 31720

Description: State authorized tax on wholesale sales of liquor; the municipality retains 95 percent of the revenue.

Authorization: *T.C.A.* 57-3-501 et seq.

Requirements or Restrictions: As delineated in *T.C.A.*

Current Rate: Depending upon the size of municipality's county, the municipality levies by ordinance a five percent or eight percent inspection fee that is collected by the wholesalers from the retailer during distribution. The wholesalers then retain five percent of the fee for performing the collection. The fee cannot exceed eight percent of the wholesale price of alcoholic beverages sold in municipalities located in counties having a population of less than 60,000; and cannot exceed five percent for municipalities located in counties having a population more than 60,000.

Frequency of Payment: Monthly.

Late Pay Penalty: A penalty of 10 percent is assessed after 20th of each month (*T.C.A.* 57-3-503(b)).

Exemptions: None.

Collection: Revenues remitted by wholesalers to municipality monthly on municipal-prescribed form.

Use Restrictions: None.

Mixed Drink Taxes

Revenue Class: Local Taxes
Fund: General **Account No.:** 31730

Description: Tax on the sale of alcoholic beverages for consumption on the premises.

Authorization: *T.C.A.* 57-4-301 (c) and 57-4-306

Requirements or Restrictions: N/A

Current Rate: Fifteen percent of the sales price of all alcoholic beverages sold for consumption on the premises, of which 25 percent of the collections return to municipality where it is collected.

Frequency of Payment: Monthly.

Late Pay Penalty: N/A

Exemptions: Not applicable to charitable, nonprofit, or political organizations selling alcohol under a special occasion license (*T.C.A.* 57-4-301 (e)).

Collection: State remits municipal share monthly.

Use Restrictions: For premier tourist resorts, the municipality's percentage must be expended for schools (*T.C.A.* 57-4-306 (3)).

Minimum Business Tax

Revenue Class: Local Taxes
Fund: General **Account No.:** 31810

Description: The business tax is levied in addition to all other privilege taxes and is intended by the legislature to be in-lieu-of any other *ad valorem* tax on "inventories of merchandise held for sale or exchange" (*T.C.A.* 67-4-701 (b)).

Authorization: *T.C.A.* 67-4-701 et seq.

Requirements or Restrictions: Businesses are required to file tax returns with the city tax collector on forms furnished by the collector listing the gross amount of sales tax owed to the state, the amount of deductions for sales tax purposes, and the total gross sales, accompanied by the appropriate business tax payment.

Current Rate: A minimum of $15 dollars is required for each person for each fixed place, location or outlet from which a business is operated. The city tax collector may, in certain circumstances, charge a fee of no more than $5 for collecting and recording the business tax (*T.C.A.* 67-4-717). In addition, the state has established different classifications of businesses and gross receipt rates assessed to the different classifications. The classifications and rates are listed in detail in *T.C.A.* 67-4-709. The rates range from one-tenth of one percent to three-eighthieths of one percent. Some examples are:

- One-tenth of one percent of all retail sales of the business for businesses classified under *T.C.A.* 67-4-708 (1);
- One-fortieth of one percent of all wholesale sales of the business by people classified under *T.C.A.* 67-4-708 (1)(A);
- Three-eightieths of one percent of all wholesale sales of the business by people classified under *T.C.A.* 67-4-708 (1)(B) and (1)(C), *T.C.A.* 67-7-708 (2) and *T.C.A.* 67-4-708 (3);
- One-twentieth of one percent of all wholesale sales of the business by people classified under *T.C.A.* 67-4-708 (1)(D);
- Transient vendors must pay a minimum tax of $50 for each 14-day period of business in a municipality, but they are not subject to the percent of the gross receipts portion of the tax (*T.C.A.* 67-4-709 (a)(6)).

Frequency of Payment: Annually. The local collector is required to pay the state 15 percent of the local business tax and 100 percent of the state business tax collected. Due dates for different business classifications are listed under *T.C.A.* 67-4-714.

Late Pay Penalty: The provision is made for hiring an attorney or collection agency and for collecting delinquent taxes after the due and delinquent dates by using distress warrants in accordance with the procedures for collecting delinquent *ad valorem* taxes (*T.C.A.* 67-4-215). Penalty is five percent per month (not to exceed 25 percent).

Exemptions: Exemptions are listed under *T.C.A.* 67-4-712. Businesses may deduct the amount of their beer wholesale tax (*T.C.A.* 67-4-711 (b)(5)) and personal property tax (*T.C.A.* 67-4-713) (limited to local business tax portion) from their gross receipts liability.

Collection: Collected by municipal officials.

Use Restrictions: Fifteen percent of local gross collections to the state. One hundred percent of the state gross collections to the state.

Amusement Tax

Revenue Class: Local Taxes
Fund: General **Account No.:** 31860

Description: A tax levied at the same rate for tangible personal property on the gross receipt sales of dues or fees for membership to recreational clubs, admission ticket sales, entrance fees, and charges made for the privilege of using tangible personal property for amusement, sports, entertainment or recreational activities.

Authorization: *T.C.A.* 67-6-212 and *T.C.A.* 67-6-330

Requirements or Restrictions: Free or complimentary tickets or admissions are to be computed at equivalent values and included as sales.

Current Rate: Municipalities receive 99 percent of 4.5925 percent of the assessed six percent state sales tax. All increased revenues from the 2002 state sales tax rate from six percent to seven percent go to the state general fund (Public Acts, 2002 Chapter 856, Section 4(f)).

Frequency of Payment: Monthly.

Late Pay Penalty: N/A

Exemptions: Excluded is the sale or transfer of real or tangible property. There are 22 other exemptions listed in *T.C.A.* 67-6-330 that include admissions to K-12 school activities, fairs, the first $150 of dues or memberships per year, dues to 501(c) organizations, and admissions to various nonprofit organizations' events.

Collection: The state collects the tax and distributes to municipalities.

Use Restrictions: None.

Natural Gas Franchise

Revenue Class: Local Taxes
Fund: General **Account No.:** 31911

Description: Municipalities can impose a franchise fee and other conditions upon the operation of a gas company within their corporate limits.

Authorization: *T.C.A.* 6-54-109; *T.C.A.* 65-4-107 and *T.C.A.* 65-26-101

Requirements or Restrictions: The franchise agreement is subject to the approval of the Tennessee Regulatory Authority (*T.C.A.* 65-4-107). The franchise agreement is passed by municipal ordinance.

Current Rate: Variable; there is no maximum franchise fee.

Frequency of Payment: Annually.

Late Pay Penalty: N/A

Exemptions: N/A

Collection: N/A

Use Restrictions: N/A

Cable TV Franchise

Revenue Class: Local Taxes
Fund: General **Account No.:** 31912

Description: Cable franchise fee levied by the municipality. Procedure and right to levy may be affected by federal law (Cable Communications Act of 1984), depending upon the situation in each municipality.

Authorization: *T.C.A.* 7-59-101 et seq. and *T.C.A.* 7-59-201 et seq.

Requirements or Restrictions: Cannot grant any overlapping franchises that are more favorable or less burdensome to existing franchises (*T.C.A.* 7-59-203).

Current Rate: N/A

Frequency of Payment: Depends on terms of franchise agreement.

Late Pay Penalty: N/A

Exemptions: None.

Collection: Pursuant to franchise license.

Use Restrictions: None

Room Occupancy Tax

Revenue Class: Local Taxes
Fund: General **Account No.:** 31920

Description: Occupancy tax on hotel or motel room rentals, imposed by private act. Rates vary from one and one-quarter percent to five percent.

Authorization: *T.C.A.* 67-4-1401 et seq.; *T.C.A.* 6-55-102; and various private acts

Requirements or Restrictions: Tax must be approved by ordinance by two-thirds vote of the governing body at two consecutive regularly scheduled meetings; or be approved by referendum, and tax cannot exceed five percent (*T.C.A.* 67-4-1402). City cannot assess the tax if the county has already levied an occupancy tax *(T.C.A.* 67-4-1425 (a)(2)).

Current Rate: Cannot exceed five percent. Hotel operator is allowed to retain two percent for collecting the tax (*T.C.A.* 67-4-1405 (b)).

Frequency of Payment: Monthly.

Late Pay Penalty: Interest is charged at 12 percent per annum plus a penalty of one percent for each month taxes are delinquent.

Exemptions: N/A

Collection: Monthly.

Use Restrictions: None unless the governing body specifies such in the authorizing ordinance (*T.C.A.* 67-4-1403).

Special Assessments

Revenue Class: Local Taxes
Fund: General **Account No.:** 31930

Description: Municipalities have the power to design and execute construction and improvement or reconstruction and re-improvement of any street, avenue, alley, highway or public place and assess not less that two-thirds of the cost or expense of the work against the property abutting or adjacent to the street, avenue, alley, or any other public place that is improved. If property owners petition for the work to be done, 100 percent of the cost of the project can be assessed.

Authorization: *T.C.A.* 7-32-101 et seq.

Requirements or Restrictions: The municipality needs to adopt an ordinance and hold a public hearing prior to making the improvements. The ordinance should describe in detail the nature of the intended work. After apportionments are made, the municipality must hold another hearing on objections to the assessments. Appeals to the assessment may be made to the circuit court.

Current Rate: Depends upon the cost of the project and the number of properties involved.

Frequency of Payment: Payments are due 30 days after the assessment is made final.

Late Pay Penalty: At the request of the property owner, the assessment may be paid in five annual installments, and shall bear interest at the rate of six percent per annum, interest payable semiannually (*T.C.A.* 7-31-133). If any property owner makes default in the payment schedule, all of the installments with interest and an additional sum equal to one-half the annual interest, shall become immediately due and payable (*T.C.A.* 7-32-137). After 60 days delinquency, the city recorder turns the collection over to the city attorney who may then attach a lien on the property (*T.C.A.* 7-32-138).

Exemptions: The total assessment made against any lot or parcel of land shall not exceed one-half of the cash value of the lot and improvements (*T.C.A.* 7-32-116).

Collection: Collected by the municipal tax collector following the assessment.

Use Restrictions: N/A

Automobile Registration

Revenue Class: Licenses and Permits
Fund: General **Account No.:** 32110

Description: Municipalities may require by ordinance an automobile registration or inspection fee for all vehicles owned or operated by residents.

Authorization: *T.C.A.* 6-55-501 et seq. and *T.C.A.* 7-51-701 et seq.

Requirements or Restrictions: Non-residents cannot be required to pay such fees.

Current Rate: Varies.

Frequency of Payment: Usually annually.

Late Pay Penalty: N/A

Exemptions: Varies.

Collection: Varies. The municipality may pass a resolution authorizing an agreement with the county clerk to collect the wheel tax license or motor vehicle regulatory license at the same time the clerk sells a state license.

Use Restrictions: Some municipalities dedicate revenue to streets and highways, but this is not required by *T.C.A.*

Taxicab Licenses

Revenue Class: Licenses and Permits
Fund: General **Account No.:** 32130

Description: Under the Tennessee Passenger Transportation Services Act, municipalities have the authority to license, control and regulate by ordinance or resolution passenger-for-hire vehicles providing transportation services within its jurisdiction. Municipalities in counties with populations greater than 500,000 also have the authority to regulate entry into the business of providing passenger transportation services.

Authorization: *T.C.A.* 7-51-1001 et seq.

Requirements or Restrictions: Allowable regulations include:

- Entry into the transportation services business through licensing;
- Rates charged;
- Safety and insurance requirements;
- Establishment of stands;
- Limited or exclusive access to airports or other facilities within the municipality;
- Regulations concerning the drivers;
- Routes and stops of fixed routes;
- Any other regulation that ensures safe and reliable passenger transportation service.

Current Rate: Variable.

Frequency of Payment: Not specified by *T.C.A.*

Late Pay Penalty: Not specified by *T.C.A.*

Exemptions: Does not apply to government entities in counties with a population of between 287,700 and 287,800.

Collection: Not specified by *T.C.A.*

Use Restrictions: N/A

Beer Licenses

Revenue Class: Licenses and Permits
Fund: General **Account No.:** 32210

Description: Revenue received from beer permits sold to individuals selling beer at retail establishments.

Authorization: *T.C.A.* 57-5-101 et seq.

Requirements or Restrictions: Business must operate within and comply with municipal and/or county ordinances.

Current Rate: Applicants pay $250, and each permit holder pays $100 per year for renewal of the privilege tax. New applicants shall be required to pay the privilege tax on a prorated basis for each month or portion thereof remaining until the next tax payment date.

Frequency of Payment: $250 fee is imposed upon application, and the annual renewal fee of $100 is due on January 1.

Late Pay Penalty: Permit may be revoked for nonpayment. If a permit holder does not pay the tax by January 31 or within 30 days after written notice of the tax was mailed, whichever is later, then the city shall notify the permit holder by certified mail that the tax payment is past due. If a permit holder does not pay the tax within 10 days after receiving notice of its delinquency by certified mail, then the city may suspend or revoke the permit or impose a civil penalty pursuant to *T.C.A.* 57-5-108 (*T.C.A.* 57-5-104 (b)(3)).

Exemptions: None

Collection: Not specified by *T.C.A.*

Use Restrictions: None

Liquor Licenses

Revenue Class: Licenses and Permits
Fund: General **Account No.:** 32220

Description: This is a privilege tax on those who engage in the business of selling at retail alcoholic beverages for consumption on the premises. The tax varies by the type of establishment that sells the liquor by the drink.

Authorization: *T.C.A.* 57-4-301

Requirements or Restrictions: These same privilege taxes are paid twice by the businesses; once to the county and once to the municipality.

Current Rate: Municipalities are allowed to levy a privilege tax on the sale of alcoholic beverages for consumption on the premises. The taxes, paid annually, are:

- Private club – $300
- Hotel and motel – $1,000
- Convention center – $500
- Premiere type tourist resort – $1,500
- Restaurant*, according to seating capacity, on licensed premises:
  a. 75-125 seats – $600
  b. 126-175 seats – $750
  c. 176-225 seats – $800
  d. 226-275 seats – $900
  e. 276 or more seats – $1,000
- Historical performing arts center – $300
- Urban park center – $500
- Commercial passenger boat company – $750
- Historic mansion house site – $300
- Historic interpretive center – $300
- Community theater – $300
- Zoological institution – $300
- Museum – $300
- Establishment in commercial airport terminal – $1,000
- Commercial airline travel club – $500
- Public aquarium – $300
- Motor speedway – $1,000
- Theater – $300

*If a restaurant is licensed to sell wine only, the privilege tax will be one-fifth of the amount specified.

Frequency of Payment: Annually.

Late Pay Penalty: N/A

Exemptions: No tax authorized or imposed by this section shall be levied or assessed from any charitable, nonprofit or political organization selling alcoholic beverages at retail pursuant to a special occasion license (*T.C.A.* 57-4-301 (e)).

Collection: The state notifies the municipality when renewal is due, then the municipality sends a letter to the establishment, which sends the revenue to the municipality.

Use Restrictions: None

Building Permits

Revenue Class: Licenses and Permits
Fund: General **Account No.:** 32610

Description: Revenue received from the sale of building permits and builder and contractor licenses. Municipalities are authorized and empowered to enact laws or ordinances to safeguard and protect the home owner or prospective home owner, commercial property owner or assembly building property owner by requiring the licensing of the residential, commercial or assembly builders and residential, commercial and assembly maintenance and alteration contractors.

Authorization: *T.C.A.* 6-54-501 et seq.; *T.C.A.* 7-62-101 et seq. and *T.C.A.* 7-62-201 et seq.

Requirements or Restrictions: City cannot issue more than 10 active building permits at one time to an unlicensed contractor (*T.C.A.* 7-62-202 (b)). Unlicensed contractors are required to post a cash bond with the city for a period of at least two years (*T.C.A.* 7-62-203.)

Current Rate: Variable.

Frequency of Payment: Upon issuance of permit.

Late Pay Penalty: N/A

Exemptions: N/A

Collection: N/A

Use Restrictions: None.

Electrical Permits

Revenue Class: Licenses and Permits
Fund: General **Account No.:** 32620

Description: Revenue received from permits for electrical work.

Authorization: *T.C.A.* 6-54-104 and *T.C.A.* 6-54-501 et seq.

Requirements or Restrictions: Permits issued only to contractors or appliance electricians licensed according to municipal ordinance or to a home owner doing personal work within his/her residence.

Current Rate: Variable.

Frequency of Payment: Upon issuance of permit.

Late Pay Penalty: N/A

Exemptions: N/A

Collection: N/A

Use Restrictions: None.

Plumbing Permits

Revenue Class: Licenses and Permits
Fund: General **Account No.:** 32630

Description: Revenue received from permits for plumbing work.

Authorization: *T.C.A.* 6-54-501 et seq.

Requirements or Restrictions: Permits issued only to licensed plumbing contractors or to a home owner doing personal work in his or her residence.

Current Rate: Variable.

Frequency of Payment: Upon issuance of permit.

Late Pay Penalty: N/A

Exemptions: N/A

Collection: N/A

Use Restrictions: None.

Zoning Permits

Revenue Class: Licenses and Permits
Fund: General **Account No.:** 32660

Description: Fees for zoning permits and, in some municipalities, subdivision plats and other plans.

Authorization: Various general law charters (*T.C.A.* 6-2-201; *T.C.A.* 6-19-101 and 102; *T.C.A.* 6-33-101); and *T.C.A.* 13-7-201 et seq.

Requirements or Restrictions: Changes to the zoning ordinance must be made by an amending ordinance.

Current Rate: Varies.

Frequency of Payment: Upon issuance of permit.

Late Pay Penalty: N/A

Exemptions: N/A

Collection: N/A

Use Restrictions: None.

Federal Community Development Grants

Revenue Class: Intergovernmental Revenue
Fund: General **Account No.:** 33110

Description: Authorized by the Housing and Community Development Act of 1974 (42 USC 5301) replacing several community development categorical grant programs, Community Development Block Grants (CDBG) provide eligible metropolitan cities and urban counties (called "entitlement communities") with annual direct grants that they can use to "revitalize neighborhoods, expand affordable housing and economic opportunities, and/or improve community facilities and services, principally to benefit low- and moderate-income persons."

Authorization: *T.C.A.* 6-54-124 and 42 USC 5301

Requirements or Restrictions: *T.C.A.* 6-54-124 requires municipalities that receive community development block grants and municipalities or industrial development corporations that are a party to an in-lieu-of property tax agreement to make a report addressing the expenditures of such funds. In addition, the municipality must place a copy of such report in the main branch of the municipality's public library or place the report on the Internet.

Current Rate: N/A

Frequency of Payment: N/A

Late Pay Penalty: N/A

Exemptions: N/A

Collection: N/A

Use Restrictions: N/A

Housing Authority in-Lieu-of Tax

Revenue Class: Intergovernmental Revenue
Fund: General **Account No.:** 33310

Description: Payment in-lieu-of taxes from local housing authority, based on gross rent receipts. Housing authorities "shall agree" to pay in-lieu-of taxes or special assessments not to exceed the cost of services, improvements, or facilities provided. A similar requirement provided that nonprofit housing corporations providing low-cost housing for elderly or handicapped people must agree to make in-lieu-of-tax payments for any project exceeding 12 units occupied after January 1, 1990. Bonds and notes of a housing authority are issued for a public purpose and together with the interest shall be exempt from taxation.

Authorization: *T.C.A.* 67-5-206; and *T.C.A.* 67-5-207

Requirements or Restrictions: Subject to federal housing law and regulations. There also are several qualifications for nonprofit housing corporations that must be met to be eligible for the payment in-lieu-of-taxes listed under *T.C.A.* 67-5-207.

Current Rate: Varies.

Frequency of Payment: Varies.

Late Pay Penalty: N/A

Exemptions: N/A

Collection: Varies.

Use Restrictions: None.

State Shared Sales Tax

Revenue Class: Intergovernmental Revenue
Fund: General **Account No.:** 33510

Description: The Retailers' Sales Tax is applied to the sale, use, consumption, distribution, lease, or rental of tangible personal property and selected services, of which cities receive a population-based share of a portion of the total statewide collections. Additional money is available to cities that have sports authorities that have secured professional major league baseball, football, basketball or hockey franchises. Premier type tourist resorts that meet specified requirements (*i.e.*, golf courses, ski slopes, theme parks, etc.) are entitled to additional distributions per *T.C.A.* 67-6-103 (1)(3)(B).

Authorization: *T.C.A.* 67-6-101 et seq.

Requirements or Restrictions: Municipalities may conduct only two special censuses after the decennial census to increase their population-based share (*T.C.A.* 67-6-103(a)(3)(C) and (D)). Special options exist for "premiere type tourist resort" cities, cities that have a major league sports team, and others as noted in *T.C.A*.

Current Rate: 99 percent of 4.5925 percent of five and one-half percent of the statewide seven percent sales tax. The one percent is retained by the state and sent to the University of Tennessee to partially fund the Municipal Technical Advisory Service (MTAS).

Frequency of Payment: Monthly

Late Pay Penalty: N/A

Exemptions: Revenues from fuel sales used for aviation, railways or water carriers are placed in the transportation equity fund.

Collection: Revenue is distributed monthly by the state.

Use Restrictions: None

State Shared Income Tax (Hall Income Tax)

Revenue Class: Intergovernmental Revenue
Fund: General **Account No.:** 33520

Description: State taxes levied on the earnings of stock dividends and interest on bonds earned by individuals, partnerships, associations, trusts and corporations. The municipality's share depends upon residence of taxpayers; i.e., if he/she resides within the corporate limits of the municipality.

Authorization: *T.C.A.* 67-2-101 et seq.

Requirements or Restrictions: N/A

Current Rate: Six percent of earnings with 37.5 percent of the earnings going to the municipality in which the taxpayer resides.

Frequency of Payment: Annually.

Late Pay Penalty: N/A

Exemptions: There are 20 exemptions listed in *T.C.A.* 67-2-104. The most common exemptions include the first $1,250 of an individual's return and the first $2,500 of income for a joint return; people 65 or older whose income is less than $16,200 ($27,000/couple); blind people; pension trusts; profit-sharing trusts; and all income derived from government bonds and securities.

Collection: State forwards municipalities' share annually.

Use Restrictions: None.

State Shared Beer Tax

Revenue Class: Intergovernmental Revenue
Fund: General **Account No.:** 33530

Description: State tax on the manufacture, sale, and transportation of beer, of which the municipalities receive a share of 10.05 percent of the total taxes, distributed based on population.

Authorization: *T.C.A.* 57-5-201 et seq.

Requirements or Restrictions: None.

Current Rate: $4.29 per 31 gallon barrel; returns are based upon population. Revenue generated from the increase from $3.40 to $3.90 is allocated to the state highway fund.

Frequency of Payment: Semi-annually.

Late Pay Penalty: 10 percent interest and penalty is collected by the state (*T.C.A.* 57-5-204).

Exemptions: Beer and ale sold for consumption at U.S. military installations.

Collection: State forwards municipality's share semi-annually.

Use Restrictions: None

State Alcoholic Beverage Tax

Revenue Class: Intergovernmental Revenue
Fund: General **Account No.:** 33540

Description: Any seized intoxicating liquors or vehicles associated with the production or transport of illegal intoxicating liquors are turned over to the Alcoholic Beverage Commission for public sale as contraband by the Commissioner of General Services. A portion of the revenue from sales of these contraband items goes to the municipality in which the officer who made the seizure works.

Authorization: *T.C.A.* 57-9-115 and *T.C.A.* 59-9-201

Requirements or Restrictions: None

Current Rate: Ninety percent of proceeds from the sale of seized liquor and 50 percent of proceeds from the sale of seized vehicles, aircraft and boats.

Frequency of Payment: Periodic. Depends on the frequency of seizures by cities and sales by the state.

Late Pay Penalty: N/A

Exemptions: N/A

Collection: The Commissioner of General Services collects the money at the time of the sale then forwards it to municipalities.

Use Restrictions: N/A

State Gasoline and Motor Fuel Tax

Revenue Class: Intergovernmental Revenue
Fund: State Street Aid **Account No.:** 33551

Description: Local share of state gasoline and other motor fuel taxes comprising the Gasoline Tax, the Diesel Tax, the Liquified Gas Tax on vehicles, the Compressed Natural Gas Tax, and the Prepaid User Diesel Tax. Distribution to municipalities is based upon population.

Authorization: *T.C.A.* 67-3-1301; *T.C.A.* 67-3-2001; *T.C.A.* 67-3-1302; *T.C.A.* 67-3-2005; *T.C.A.* 67-3-2008; *T.C.A.* 67-3-2202; *T.C.A.* 67-3-2206; *T.C.A.* 67-3-2213; *T.C.A.* 67-3-2409

Requirements or Restrictions: Special census counts are limited to two in addition to the decennial census.

Current Rate:

- Gasoline Tax – Of the 20 cent tax per gallon, municipalities receive 99 percent (one percent is retained by the state for administration) of 14.3 percent of the first 11 cents (minus 0.1074 percent designated for boating safety); 33.33 percent of an additional two cents from increases in 1985 and 1986 (minus 0.1074 percent designated for boating safety); and 33.33 percent of an additional one cent increase in 1989.
- Diesel Tax – Of the 17 cents tax per gallon, municipalities receive 12.38 percent of 12 cents.
- Liquified Gas – Of the 14 cents tax per gallon, municipalities receive 14.14 percent of the first 11 cents and 99 percent of 33.33 percent of an additional one cent increase in 1986.
- Liquified Gas Tax on Vehicles – Municipalities receive 14.14 percent of a flat rate that varies depending on the classification of the vehicle (by gross vehicle weight). The rate varies from $70 to $114.
- Compressed Natural Gas – Of the 13 cents tax per gallon, municipalities receive 12.38 percent.
- Prepaid User Diesel Tax – Municipalities receive 12.38 percent of a flat rate ($56 – $159) for farmers whose use of diesel fuel is mostly for agricultural purposes yet who own diesel powered passenger cars or trucks.

Frequency of Payment: Monthly.

Late Pay Penalty: N/A

Exemptions: As noted in *T.C.A.*

Collection: Monthly checks are mailed to the municipality or deposited directly into the municipality's bank account.

Use Restrictions: Outlined in *T.C.A.* 54-4-204. Funds can be spent on street improvements; principal and interest payments for street improvement project loans; the costs of acquiring rights-of-way for approaches to bridges and tunnels; the city's share of grade eliminations; one-third of the total costs of rights-of-way for state or federal highways; paying another municipality, county or TDOT for doing road improvements; and up to 22.22 percent can be spent on funding mass transit.

State Streets and Transportation

Revenue Class: Intergovernmental Revenue
Fund: General **Account No.:** 33552

Description: This represents what is referred to as the Special Privilege Tax or the Petroleum Special Products Tax/Gas Inspection Fee and the Export Tax. The Special Privilege Tax establishes a local government fund created by a tax of one cent per gallon on all petroleum products. The export tax is a tax of one-twentieth of one cent per gallon of petroleum product that is stored in Tennessee or stored in Tennessee and then exported. If the special privilege tax has already been paid, then nineteen-twentieths of the Special Privilege Tax can be credited on the Export Tax return. The local share is distributed to municipalities based on population.

Authorization: *T.C.A.* 67-3-1303; *T.C.A.* 67-3-1305 and *T.C.A.* 67-3-2006

Requirements or Restrictions: As noted in *T.C.A.*

Current Rate: The state distributes $619,833 per month to cities on a population basis. Before the money is distributed to cities, the state retains $10,000 per month and allocates it to The University of Tennessee Center for Government Training.

Frequency of Payment: Monthly.

Late Pay Penalty: N/A

Exemptions: As noted in *T.C.A.* 67-3-1501 et seq. Some of the exemptions include government agencies, products used for agricultural purposes, exported products, kerosene, and aviation fuels.

Collection: Monthly checks are mailed to the municipality or deposited directly into the municipality's bank account.

Use Restrictions: Although this money is general fund revenue, it is limited in the same manner as the state gasoline and motor fuel tax (to fund city street projects).

Gross Receipts: TVA

Revenue Class: Intergovernmental Revenue
Fund: General **Account No.:** 33591

Description: TVA pays five percent of gross power sales proceeds to the state in lieu of taxes. Forty-eight and one-half percent of the increase in TVA payments made to the State of Tennessee above the amount received in the base year (1977-1978) is distributed to county and municipal governments. Thirty percent of this amount is distributed to municipalities based on population.

Authorization: *T.C.A.* 67-9-101 et seq. and 16 USC 831i

Requirements or Restrictions: Before making the 48.5 percent distribution to cities and counties, the state deducts $4,462 monthly and appropriates it to the Tennessee Advisory Commission on Intergovernmental Relations (TACIR).

Current Rate: Thirty percent of 48.5 percent collected above the base rate set in 1978 to cities based upon population.

Frequency of Payment: Quarterly.

Late Pay Penalty: N/A

Exemptions: N/A

Collection: State remits municipality's share quarterly.

Use Restrictions: None

Special Impact Area Funds: TVA

Revenue Class: Intergovernmental Revenue
Fund: General **Account No.:** 33592

Description: Three percent of the increase in gross power sales paid by TVA as payments in-lieu-of property taxes since June 30, 1978, is paid to municipalities where TVA is performing construction activity on facilities to produce electric power.

Authorization: *T.C.A.* 67-9-101 et seq.

Requirements or Restrictions: TVA designates the construction activity areas. Payments are made during the time of construction and for one year after the construction activity is completed. For the next three fiscal years, payments are made in decreasing amounts based on the last year of the entitlement. The first year yields 75 percent of the payment based on the last year of the entitlement, the second year yields 50 percent, and the third year yields 25 percent (*T.C.A.* 67-9-102 (b)(2)).

This impact allocation cannot exceed 10 percent of funds received under the normal distribution of the TVA gross receipts tax (*T.C.A.* 67-9-102 (b)(1)).

Current Rate: Three percent of the increase in gross receipts tax from the fiscal year ended June 30, 1978.

Frequency of Payment: Quarterly.

Late Pay Penalty: N/A

Exemptions: If in any fiscal year no areas are impacted by TVA construction activity, then no more than 30 percent of the impact funds are allocated to The University of Tennessee for the County Technical Assistance Service (CTAS), and no more than 40 percent of the impact funds are allocated to TACIR in two 20 percent increments. Any money remaining after these allocations follows the normal distribution of TVA gross receipts tax.

Collection: State remits municipality's share quarterly.

Use Restrictions: None.

Corporate Excise Tax

Revenue Class: Intergovernmental Revenue
Fund: General **Account No.:** 33593

Description: The state corporate excise tax collected from banks is shared with municipalities and counties.

Local tax rates determine the payment allocation between the county and the city, so a city must levy a property tax to receive any funds. Another formula is prescribed for allocating such revenue if a bank has branches in more than one city and/or in more than one county (*T.C.A.* 67-4-2017 (a)(1)(B)).

Authorization: *T.C.A.* 67-4-2017

Requirements or Restrictions: As noted in *T.C.A.*

Current Rate: The tax is three percent of net earnings (excluding interest from state bonds), less seven percent of *ad valorem* taxes, divided between counties and municipalities based on property tax rates.

Frequency of Payment: Annually in the third quarter.

Late Pay Penalty: N/A

Exemptions: None.

Collection: State forwards revenue to municipalities in third quarter of each year.

Use Restrictions: None.

Appendix D: DELINQUENT TAX TABLE

Penalties and Interest by Month					
	Year(s) Delinquent				
Current Month	**1 Year**	**2 Years**	**3 Years**	**4 Years**	**5 Years**
March 1	1.5%	19.5%	37.5%	55.5%	73.5%
April 1	3.0%	21.0%	39.0%	57.0%	75.0%
May 1	4.5%	22.5%	40.5%	58.5%	76.5%
June 1	6.0%	24.0%	42.0%	60.0%	78.0%
July 1	7.5%	25.5%	43.5%	61.5%	79.5%
August 1	9.0%	27.0%	45.0%	63.0%	81.0%
September 1	10.5%	28.5%	46.5%	64.5%	82.5%
October 1	12.0%	30.0%	48.0%	66.0%	84.0%
November 1	13.5%	31.5%	49.5%	67.5%	85.5%
December 1	15.0%	33.0%	51.0%	69.0%	87.0%
January 1	16.5%	34.5%	52.5%	70.5%	88.5%
February 1	18.0%	36.0%	54.0%	72.0%	90.0%

Appendix E: TECHNICAL BULLETIN ON SITUS REPORTS

Get Your Share of the Local Option Sales Tax and the Hall Income Tax: Request a *Situs* Report

by M. Michael Tallent, Assistant Director
April 19, 1991

Many municipalities annually do a *situs* report to ensure they receive their fair share of the local option sales tax. The situs report makes sure the Tennessee Department of Revenue has been furnished with the correct *situs* code (location number) for every business within the corporate limits. An incorrect *situs* code means the municipality's share of the local option sales tax will go to the county or to another municipality. In 1989, MTAS prepared a publication explaining the importance of filing a *situs* report; it is available upon request.

Since cities have just one year to recover money incorrectly distributed, it is important to check *situs* status annually. Another incentive for timely filing of the report now is tax reform under consideration by the legislature. Efforts are being made to hold cities harmless for any lost state and local sales tax revenues. If successful, the hold harmless formula presumably will be constructed around a "base" year. Therefore, it is important to verify *situs* codes annually so that all "base" years are as correct as possible. Karen Blackburn, manager of financial controls with the Department of Revenue, responds to *situs* report requests from mayors. The same general policies for income tax will also apply for local sales tax.

Income Tax

The same law (*T.C.A.* 67-l-1704) that allows for a *situs* report on sales tax also allows one on the Hall Income Tax. Each year citizens of Tennessee are required to report and pay a six percent state tax on income from investments such as stocks and bonds. Three-eighths of that six percent is returned to the local government where the taxpayer resides. The taxpayer makes that determination through an apportionment code (each city and county has its own apportionment code number). If this number is incorrect, then the local distribution will also be incorrect. In fact, if an apportionment code is not placed on the return, the local distribution automatically defaults to the county for a first-time taxpayer or to the apportionment code on prior year returns for a taxpayer of record.

Requesting a *Situs* Report

To request a *situs* report on the Hall Income Tax and/or the local sales tax, a municipality should follow the established policies of the Department of Revenue. Those policies are:

Step 1. Forward a written request to the Department of Revenue for income tax *situs* reporting. All requests should come from the mayor and be sent to:

Karen Blackburn
Manager of Financial Controls
Tennessee Department of Revenue,
Accounting Division
Room 409, Andrew Jackson State Office Building
Nashville, TN 37242-1299

Step 2. *Situs* reports are sent to the mayor as soon as possible.

Step3. Mayors have the responsibility of researching these reports and identifying incorrect listings.

Step 4. Notification to the department is required by returning the report, marking any *situs* code account errors. Any taxpayer not accounted for on this report should be identified by name and address on a separate attachment. The mayor is responsible for notifying the department by letter, requesting necessary adjustments.

Step 5. Adjustments are only made during July due to the annual disbursement of income tax funds.

Step 6. Adjustments are only made for the previous year.

Step 7. The State Financial Control Unit notifies the Income Tax Division of any needed *situs* changes that would affect the following year's allocation.

Step 8. *Situs* reports are handled on a first come, first served basis.

When requesting *situs* reporting for income tax, a municipality needs to request the report for its municipality, its county, and any adjoining municipality. Unlike sales tax (every business must have a sales tax license), every citizen is not required to file a state income tax return. When doing an income tax *situs* report, a municipality is simply being sure that those taxpayers used the correct *situs* code. Therefore, a municipality should check the *situs* of taxpayers in the county and other cities, too; they may be residents of the city and marked the wrong code.

The same reasons for timely action on the sales tax also apply to timely action on the income tax. In fact, if your municipality submits its request for an income tax *situs* report the day it receives this bulletin, it wouldn't be too early.

For Further Information

If you have questions about *situs* codes and tax information, contact Karen Blackburn in Nashville at (615) 741-1028, or call your local MTAS Management Consultant.

Tenn. Op. Atty. Gen. No. 99-225
Office of the Attorney General
State of Tennessee

Opinion No. 99-225
December 3, 1999

Pledge of City Appropriations to Nonprofit Organization

Honorable Curtis Person, Jr.
State Senator
Suite 308, War Memorial Building
Nashville, TN 37243-0031

Question

Is the City of Millington authorized to make a commitment to appropriate funds to a nonprofit organization for 15 years without a public referendum?

Opinion

The City of Millington is not authorized, either under its charter or [under] any provision of general law, to make a binding commitment to appropriate funds to a nonprofit organization for 15 years.

Analysis

This opinion concerns the authority of the City of Millington to make a commitment to appropriate funds to a nonprofit organization for 15 years. Our opinion is confined to this question and does not address any other legal issues that the proposed transaction might present.

Our opinion is based on the following facts as presented in the opinion request: The YMCA is planning to build a new center in the City of Millington. It has been proposed that the City of Millington would donate 10 acres of land, presumably owned by the city, to the YMCA for the project. The city would "pledge" $150,000 to the YMCA each year for the next 15 years, beginning in 1999, for the construction of the Millington YMCA. The city would sign a "letter of commitment" addressed to the YMCA stating that the city is committed to the YMCA and desires that construction begin as soon as financing can be finalized. The city would waive all costs associated with fees and permits generally required by the City of Millington for the construction project. The board of directors of the YMCA would sign an agreement stating that, in the event the Millington YMCA decides to close in the future, the building and property will revert to the City of Millington. The lender providing the funds for construction would accept these conditions.

The request does not specify the form of the city's commitment to appropriate funds or the purpose the commitment is intended to serve. Based on the request, it appears that the city's "pledge" to appropriate funds is intended to provide some incentive for the YMCA to obtain a loan to finance construction of the new facility. We therefore address whether the city may enter into a commitment to appropriate funds for this purpose, either from current or from future city revenues, that could be enforced by a proposed recipient or a third party such as a lender. Generally, municipalities may exercise those express or necessarily implied powers delegated to them by the legislature in their charters or under statutes. *City of Lebanon vs. Baird*, 756 S.W.2d 236, 241 (Tenn. 1988);

Professional Home Health & Hospice, Inc. vs. Jackson-Madison County General Hospital District, 759 S.W.2d 416, 419 (Tenn.Ct.App. 1988), p.t.a. denied (1988), reh'g denied (1988); *City of Chattanooga vs. Tennessee Electric Power Co.*, 172 Tenn. 524, 533, 112 S.W.2d 385, 388 (1938) (a municipal corporation may exercise only such powers "as are expressly granted in its charter or arise by necessary implication in order to carry out the declared objects and governmental purposes for which the corporation was created"). Neither the Millington City Charter, nor any general law, expressly authorizes such a commitment.

Under *T.C.A.* 12-2-301 et seq., a city may lease property to or from a not-for-profit corporation. Based on the facts included in the request, however, the proposed transaction does not appear to fall within this statutory scheme. Cities are generally authorized to appropriate city funds for the financial aid of civic and charitable organizations under the limitations set forth in *T.C.A.* 6-54-111. Depending on the facts and circumstances, the beneficiary of an appropriation made in compliance with this statute may have the right to enforce its disbursement in accordance with its terms. But that statute does not authorize a city to make a binding commitment or pledge to appropriate funds either from current or from future revenues, nor is such a transaction "necessarily implied" by any of the powers granted in the Millington City Charter or general law.

Therefore the City of Millington is not authorized, either under its charter or any provision of general law, to make a binding commitment to appropriate funds to a non-profit organization for fifteen years.

Paul G. Summers, Attorney General and Reporter
Michael E. Moore, Solicitor General
Ann Louise Vix, Senior Counsel

Tenn. Op. Atty. Gen. No. 91-106
Office of the Attorney General
State of Tennessee

Opinion No. 91-106
December 23, 1991

Municipally Owned Electrical Systems and Electric Cooperatives — Funding Economic and Community Organizations

Phillip E. Pinion
109 War Memorial Building
Nashville, TN 37243

Question

Can municipally owned electrical systems and electric cooperatives legally put money into economic and community organizations?

Opinion

It is the opinion of this office that municipally owned electrical systems may be barred, and electric cooperatives are barred, by the statutes which govern their operations from using their revenues to fund economic and community organizations; further, each may be barred from such use of revenues by documents executed in connection with the issuance of any bonds to finance or refinance the system notwithstanding the lack of any specific bar to such action in the governing statutory scheme.

Analysis

Both municipally owned electrical systems and electric cooperatives are creatures of statutes and it is to those statutes to which we must look, at least in part, for the answer to the question posed. Moreover, for purposes of this opinion, we assume that the phrase "economic and community organizations" means those organizations which are customarily thought of as tax-exempt or charitable organizations and that any appropriation by a municipality would be made in accordance with *T.C.A.* 6-54-111, which provides guidelines for a municipality's appropriating money for the financial aid of any nonprofit charitable organization or any nonprofit civic organization. In addition, we assume that the question posed is concerned with the use of surplus system revenues from operations and not with the use of bond proceeds.

The Tennessee judiciary has held that, in the absence of statutory prohibition, a municipality may divert its profits from the sale of a public works commodity to other municipal purposes. *Killion vs. City of Paris*, 192 Tenn. 466, 241 S.W.2d 524 (1951). In Killion, the city of Paris issued its general obligation debt to construct and acquire a water works system. Subsequently, the city passed an ordinance providing that a portion of the water works fees would be applied to retire debt service on all of the city's bonded indebtedness. Water customer Killion sued to have the ordinance stricken.

The court noted that if the water works system were acquired under the authority of *T.C.A.* 7-35-401 et seq., then surplus revenues would have to be applied exclusively to the improvements, extensions or additions to the water works system pursuant to *T.C.A.* 7-35-417, 418. However, plaintiff in Killion did not allege application of the above cited statutes. Consequently, the Court held these statutes to be wholly inapplicable, and in the absence of any statutory prohibition, "a municipality may divert its profits from the sale of water to its customers to municipal purposes other than those of the water works enterprise." 192 Tenn. at 453.

Also, we have opined previously that a municipality owning a gas system could apply surplus revenues from that system to other municipal purposes where the gas system was financed pursuant to the Municipal Recovery and Post War Aid Act of 1945, *T.C.A.* 7-36-101 et seq. (repealed effective July 1, 1988, but not as to bonds issued before that date, 1988 Tenn. Public Acts Ch. 750, Sections 22 and 71). Op. Tenn. Atty. Gen. No. 87-03 (January 9, 1987); Op. Tenn. Atty. Gen. No. U87-47 (April 24, 1987).

In examining the statutory scheme governing the organization and operation of municipally owned electrical systems, we find that a municipally owned electrical system may be governed by one of a number of statutes. Some of these statutory schemes have been repealed and no longer govern municipally owned electrical systems, except in those cases where bonds were issued prior to the repeal of the statutes to finance or refinance the system.

Under current law, a municipality may organize a municipally owned electrical system pursuant to the Municipal Electric Plant Law of 1935, *T.C.A.* 7-52-101 et seq., and issue its debt for the acquisition and improvement of the system pursuant to the Local Government Public Obligations Act of 1986, *T.C.A.* 9-21-101 et seq. ("LGPOA"). Neither the Municipal Electric Plant Law of 1935 nor the LGPOA contains prohibitions against the municipality's applying revenues from the municipally owned electrical system to economic and community organizations. Therefore, absent restrictive covenants in any bond documents executed in connection with financing or refinancing of the electrical system, the decision in Killion should permit a municipally to apply revenues from a municipally owned electrical system to economic and community organizations.

In addition, a municipality can organize and finance its municipally owned electrical system pursuant to the Revenue Bond Law, *T.C.A.* 7-34-101 et seq. The Revenue Bond Law restricts the municipality in its use of surplus system revenues to fund economic and community organizations and provides that all surplus revenues can be used only to reduce rates (*T.C.A.* 7-34-103(b) and 7-34-115).

Under law prior to July 1, 1988, a municipality could both organize and finance a municipally owned electrical system under the Municipal Electric Plant Law of 1935. The portions of that law dealing with financing municipally owned electrical systems have now been repealed pursuant to 1988 Tenn. Pub. Acts, Ch. 750. However, prior to that repeal, *T.C.A.* 7-52-130 (now repealed) states that the supervisory body of the municipally owned electric plant shall devote all moneys in the electric plant fund derived from any source other than the issuance of bonds to or for certain listed items of expenditure (not including funding economic and community organizations) and that any surplus thereafter remaining, after the establishment of proper reserves, if any, shall be devoted solely to the reduction of rates (the use of bond proceeds is governed by *T.C.A.* 7-52-129 (now repealed), which also precludes the use of bond proceeds to fund economic and community organizations).

Tenn. Pub. Acts, Ch. 750, Section 71, states that nothing in the act affects the validity or enforceability of any bond, note or other obligation legally issued by a local government under any law existing prior to the effective date of the act. If bonds were issued pursuant to the Municipal Electric Plant Law of 1935 prior to its repeal, we interpret the repealing act to mean that the restrictions on the use of system revenues or bond proceeds could survive the repeal until the bonds were retired. If those restrictions affected the "enforceability" of the payment of the bonds, then we think they would survive the repeal. For example, if the system revenues were pledged for payment of the bonds, then we think the restrictions would survive since diversion of these revenues could affect the enforceability of the bonds by affecting the money available for payment of the bonds. However, we caution that each bond financing is unique and we cannot opine as to any one financing without reviewing it. If no such bonds are outstanding, then the use of system revenues would be governed by the Municipal Electric Plant Law of 1935 as now in effect (which as earlier noted does not contain restrictions precluding the use of system revenues to fund economic and community organizations).

In contrast to the multiple statutes which could govern a municipally owned electrical system, electric cooperatives are organized pursuant to and their operations governed by the Rural Electric and Community Cooperative Law, *T.C.A.* 65-25-201 et seq. Revenues in excess of those necessary to pay certain listed items of expenditure are required by *T.C.A.* 65-25-212 to be distributed by the cooperative to its patrons in the form of refunds or general reduction of rates. The permitted uses of revenues listed in the statute do not include payments to economic or community organizations and, therefore, such excess moneys must be distributed to the patrons in the form of refunds or general reduction of the rates. Although the statute permits a cooperative, prior to reducing rates or making refunds to patrons, to provide a "fund for education in cooperation and for the dissemination of information concerning the effective use and conservation of electric power and energy and concerning any other services made available by the cooperative," we do not think that this provision would permit a payment to the organizations with which we are concerned. Thus, we conclude that an electric cooperative organized pursuant to this law cannot use its revenues to make payments to economic and community organizations.

In conclusion, for both municipally owned electrical systems and electric cooperatives, restrictions on funding economic and community organizations with surplus system revenues may be imposed by the statutes which govern their organization, financing and operation. Restrictions on such use of surplus system revenues may also be imposed by documents executed in connection with bonds issued to finance or refinance the construction of the electrical system. We cannot emphasize enough the importance of examining carefully those statutes and documents.

Sincerely,
Charles W. Burson, Attorney General
and Reporter
John Knox Walkup, Solicitor General
H. Phillip Carnes, Assistant Attorney General

Tenn. Op. Atty. Gen. No. 91-52
Office of the Attorney General
State of Tennessee

Opinion No. 91-52
May 29, 1991

Filing Annual Audit Under *T.C.A.* 6-54-111(c)

Ronnie Davis
117 War Memorial Building
Nashville, Tennessee 37243-0111

Question

Whether *T.C.A.* 6-54-111(c) may be satisfied by submission of an annual report in lieu of an audit.

Opinion

It is the opinion of this Office that *T.C.A.* 6-54-111(c) requires a nonprofit organization receiving financial assistance from a municipality to file an annual report of its business affairs, including a copy of its annual audit, with the city clerk. Thus, the statute cannot be satisfied by filing an annual report which does not include an annual audit. However, the statute does not require that such audit be prepared by an independent certified public accountant or an independent public licensed accountant. The type of audit that will satisfy the requirement may vary, depending on the size of the non-profit corporation and the complexity of its finances. The financial officers of the municipality, or other appropriate officials, might be consulted in this regard. Guidelines established by the municipal legislative body could also clarify the requirement.

Analysis

This opinion concerns an interpretation of the power of a municipality to appropriate funds for nonprofit organizations. This power, and the restrictions on it, are described in *T.C.A.* 6-54-111.

T.C.A. 6-54-111(c) provides as follows:

> *Any nonprofit organization which desires financial assistance from a municipality shall file with the city clerk a copy of an annual report of its business affairs and transactions which includes, but is not limited to, a copy of an annual audit, its program which serves the residents of the municipality and their proposed use of the municipal assistance. Such report will be open for public inspection during regular business hours of the city clerk's office.*

T.C.A. 6-54-111(c) (1985) (emphasis added).

Thus, the statute, by its terms, clearly requires such a non-profit corporation to file an annual report which includes a copy of its annual audit. A report which does not contain such an audit would clearly not satisfy this requirement. The statute contains no further definition of "annual audit." Pursuant to *T.C.A.* 6-54-111(b), each legislative body of a municipality appropriating funds under this statute must devise guidelines directing for what purpose such funds may be spent. Reference should be made to applicable municipal guidelines to determine whether they contain any more detailed description of the required documentation.

In addition, the Comptroller is authorized to devise standard procedures to assist a municipality in the disposition of such funds. *T.C.A.* 6-54-111 (b) (1985). The Comptroller has promulgated regulations describing standard procedures for appropriating and disbursing municipal funds to non-profit charitable organizations, which appear at Tennessee Rules and Regs Ch. 0380-3-7 et seq. These regulations, however, contain no more detailed description of an "annual audit" to be filed under the statute.

The Tennessee Supreme Court has defined an "audit" as "... the methodical examination of records with intent to verify their accuracy." *National Health Corporation vs. Snodgrass*, 555 S.W.2d 403, 405 (Tenn.1977). *Black's Law Dictionary* defines "audit," in part, as a "[s]ystematic inspection of accounting records involving analysis, tests, and confirmations." *Black's Law Dictionary*, 120 (5th Ed.1979). An audit may be independent or internal, depending on whether it is conducted by an outside firm, or by inside personnel. Id.

The statute nowhere specifies the appropriate auditor to conduct the audit, or the level of formality of the report to be submitted. The statute contains no requirement that such audit be prepared or certified by a certified public accountant or a licensed public accountant. Whether any particular report would contain sufficient financial information and be prepared with sufficient formality to satisfy the requirement of *T.C.A.* 6-54-111(c) would appear to depend upon a variety of facts and circumstances surrounding the organization and the appropriation of municipal funds. Municipal guidelines could address this issue. In the absence of such guidelines, it is suggested that the municipality consult with its own financial officers or independent financial consultants for further guidance.

Charles W. Burson, Attorney General and Reporter
John Knox Walkup, Solicitor General
Ann Louise Vix, Assistant Attorney General

Tenn. Op. Atty. Gen. No. 98-214
Office of the Attorney General
State of Tennessee

Opinion No. 98-214
November 23, 1998

Appropriation of Municipal Funds to Nonprofit Charitable Organizations Providing "year-round services"

The Honorable Bobby Sands
State Representative
War Memorial Building, Suite 110
Nashville, Tennessee 37243

Question

Does a nonprofit day care center or similar child care facility, which does not operate all 12 months of the year, meet *T.C.A.* 6-54-11(a)(2)(A)'s requirement that a nonprofit charitable organization provide "year-round services" in order to qualify for appropriated funds from a municipality?

Opinion

No. A nonprofit charitable organization, including a day care center or similar child care facility, must operate during the entire year in order to meet the "year-round" services requirement of *T.C.A.* 6-54-111(a)(2)(A).

Analysis

The inquiry to this office requests a legal opinion regarding *T.C.A.* 6-54-111(a)(2)(A). The specific question is the definition of "year- round services benefiting the general welfare" and whether a nonprofit day care center or similar child care facility which does not operate all 12 months of the year meets the requirement of providing "year-round services."

T.C.A. 6-54-111(a) provides:

(a)(1) The legislative body of each municipality may appropriate funds for the financial aid of any nonprofit charitable organization or any nonprofit civic organization in accordance with the guidelines required by subsection (b).

(2)(A) For the purposes of this section, a nonprofit charitable organization is one in which no part of the net earnings inures or may lawfully inure to the benefit of any private shareholder or individual and which provides year-round services benefiting the general welfare of the residents of the municipalities.

T.C.A. 6-54-111(a) (emphasis added).

"The rule of statutory construction to which all others yield is that the intention of the legislature must prevail." *City of Caryville vs. Campbell County*, 660 S.W.2d 510, 512 (Tenn. App. 1983), perm. app. denied (1983). Legislative intent is "derived from a reading of the statute in its entirety and within its statutory context." *Crown Enterprises, Inc. vs. Woods*, 557 S.W.2d 491, 493 (Tenn.1977).

Whenever possible, legislative intent and purpose are "ascertained primarily from the natural and ordinary meaning of the language used, when read in the context of the entire statute, without any forced or subtle construction to limit or extend the impact of the language." *Worrall vs. Kroger Co.*, 545 S.W.2d 736, 738 (Tenn. 1977). *City of Caryville vs. Campbell County*, 660 S.W.2d 510, 512 (Tenn. App.), perm. app. denied (1983). If legislative intent is without contradiction or ambiguity, "there is no room for interpretation or construction, and the judges are not at liberty, on consideration of policy or hardship, to depart from the words of the statute; ... they have no right to make exceptions or insert qualifications, however abstract justice or the justice of a particular case may require it." *Carson Creek Vacation Resorts, Inc. vs. Woods*, 865 S.W.2d 1, 2 (Tenn. 1993) (citations omitted). The ordinary and common meaning of a word may be established by its definition in a recognized dictionary. *Edelman vs. State*, 62 Wis.2d 613, 620, 215 N.W.2d 386 (1974).

The term "year-round" is not defined in *T.C.A.* 6-54-111. The term is not used or defined in the regulations promulgated by the Comptroller of the Treasury pursuant to *T.C.A.* 6-54-111(b). (Tenn. Admin. Comp. 0380-3-7-.01 et seq., Rules of Comptroller of the Treasury.) Tennessee courts have not addressed the meaning of the term "year-round" in *T.C.A.* 6-54-111(a).

Black's Law Dictionary defines "year" but not "year-round."[1] English language dictionaries define the term "year-round." It means "[e]xisting, active, or continuous throughout the year; during all seasons." American Heritage Dictionary, p. 1400 (2d college ed. 1985). The Webster Dictionary defines the adjective "year-round" as "occurring, effective, employed, staying, or operating for the full year: not seasonal" and gives "a year-round resort" as an example. Webster Dictionary (Internet dictionary based on Merriam-Webster Collegiate Dictionary, 10th ed. 1998), entry for "year-round" as adjective, at http://www.m-w.com.

Based on the common, unambiguous meaning of "year-round," a day care or similar child care facility must operate continuously throughout the year, during all seasons, in order to qualify as a "a nonprofit charitable organization ... which provides year-round services benefiting the general welfare of the residents of the municipalities" within the meaning of Tenn. Code Ann. 6-54-111(a)(2)(A).[2]

John Knox Walkup, Attorney General and Reporter
Michael Moore, Solicitor General
Margaret M. Huff, Assistant Attorney General

[1] "Year" is "[t]he period in which the revolution of the earth round the sun, and the accompanying changes in the order of nature, are completed. Generally, when a statute speaks of a year, twelve calendar, and not lunar, months are intended.... When the period of a "year" is named, a calendar year is generally intended, but the subject-matter or context of statute or contract in which the term is found or to which it relates may alter its meaning." *Black's Law Dictionary* (6th ed. 1998).

[2] The term "year-round" is found, but not defined, in four other Tennessee statutes. In these statutes, as well as the statute at issue, the legislature has used the term "year-round" in a consistent way to mean during the entire year or continuously throughout the year and during all seasons. *T.C.A.* 54-5-705, regarding eligibility of historic sites for interstate highway directional signs, requires that a historic site be "open to the public on a year-round basis." *T.C.A.* 68-221-703(19)(B)(i) of the Safe Drinking Water Act defines "Community water system" as "a public water system which serves at least fifteen (15) service connections used by year-round residents ..." A provision in the Education Finance Act at *T.C.A.* 49-3-317(b), regarding adjustments to reflect local changes, states, "Whenever the schools in any LEA are conducted on a year-round basis, such shall not operate to reduce the level of state support to the LEA ..." *T.C.A.* 49-6-101(f)(2), regarding special services for preschools, states, "Programs should strive to assist families by providing full-day, year- round services ...."

Appendix G: CHARITABLE CONTRIBUTIONS SAMPLE RESOLUTION

RESOLUTION NO. __________

A RESOLUTION pursuant to the authority granted by section 6-54-111 of the *Tennessee Code Annotated*, and in accordance with the *Internal Control and Compliance Manual for Tennessee Municipalities* authorizing appropriations for financial aid of _____(Name of Charitable Organization)________ , a nonprofit charitable or nonprofit civic organization whose services benefit the general welfare of the residents of this municipality.

WHEREAS, _______(Name of Charitable Organization)______ is a nonprofit charitable or nonprofit civic organization whose year-round services benefit the general welfare of the residents of this municipality; and

WHEREAS, section 6-54-111 of *Tennessee Code Annotated* authorizes appropriation of funds for financial aid of such nonprofit charitable or nonprofit civic organizations; and

WHEREAS, the *Internal Control and Compliance Manual for Tennessee Municipalities* Title 4, Chapter 3, Section 1, requires that a special resolution be adopted for each such nonprofit charitable or nonprofit civic organization which is to receive such funds.

NOW, THEREFORE, BE IT RESOLVED by the ___________(Governing Body)___________ of the _____(City/Town)________ of ________________(Name)____________________, Tennessee, that:

Section 1. The __________(Governing Body)__________ may appropriate funds from time to time, in such amounts as is deemed proper, for the financial aid of __________(Name of Charitable Organization)__________ , a nonprofit charitable or nonprofit civic organization whose year-round services benefit the general welfare of the residents of this municipality.

Section 2. Such funds appropriated by the municipality for use by ______(Name of Charitable Organization)______ shall be spent for the following purposes:

1. ____

2. ____

All such funds shall be used to promote the general welfare of the residents of this municipality.

Section 3. ______(Name of Charitable Organization)______ shall comply with all requirements of section 6-54-111 of *Tennessee Code Annotated* and Title 4, Chapter 3, Section 1 of the *Internal Control and Compliance Manual for Tennessee Municipalities*, particularly with regard to submission of an annual report of its business affairs and transactions and the proposed use of the municipal assistance.

Section 4. This resolution shall take effect upon its passage, the public welfare requiring it.

PASSED: ______________________ ______________________

Date Mayor

____

Recorder

Appendix H: REFERENCES

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Riley, S.L., and Colby P.W. 1991. *Practical Government Budgeting: A Workbook for Public Managers.* Albany, NY: State University of New York Press.

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