



RISK MANAGEMENT INFORMATION
ESTABLISHING BUILDING AND DEVELOPMENT FEES

Introduction

Over the past few years, there have been several legislative, administrative, and legal developments that have put the spotlight on municipal building and development fees. Builders have claimed that city fees are excessive and they have undertaken several initiatives to make municipal officials more accountable.

In light of those initiatives and challenges, we thought it important to review the relevant statutes, rules and legal filings, and make some recommendations about what cities can do to minimize their exposure to lawsuits.

Statutes and Rules

The first statute worth reviewing is Minn. Stat. 16B.685 that reads as follows:

16B.685 Annual Report

Beginning with the first report filed on June 30, 2003, each municipality shall annually report by June 30 to the department, in a format prescribed by the department, all construction and development-related fees collected by the municipality from developers, builders, and subcontractors, if the cumulative fees collected exceeded \$5,000 in the reporting year. The report must include:

- (1) The number and valuation of units for which fees were paid;*
- (2) The amount of building permit fees, plan review fees, administrative fees, engineering fees, infrastructure fees, and other construction and development-related fees; and*
- (3) The expenses associated with the municipal activities for which fees were collected.*

This statute requires cities to annually report fee revenue, but more importantly, it requires cities to identify “the expenses associated with municipal activities for which fees were collected.” Because other statutes and regulations discussed below require that fees be “fair, reasonable and proportionate” to the cost associated with the service provided, it is imperative that cities give careful thought to filling out the reporting form and do a good job of identifying “all” related expenses. Cities with fee revenue well in excess of reported expenditures could be susceptible to challenge.

The next two laws relate to the requirement that fees be “fair, reasonable, and proportionate . . .” Specifically, with regard to development fees, Minn. Stat. 462.353 subd. 4(a) and (b) reads:

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Consult your attorney for advice concerning specific situations.

Subd. 4. Fees

- (a) *A municipality may prescribe fees sufficient to defray the costs incurred by it in reviewing, investigating, and administering an application for an amendment to an official control established pursuant to sections [462.351](#) to [462.364](#) or an application for a permit or other approval required under an official control established pursuant to those sections. Except as provided in subdivision 4a, fees as prescribed must be by ordinance. **Fees must be fair, reasonable, and proportionate and have a nexus to the actual cost of the service for which the fee is imposed.***
- (b) *A municipality must adopt management and accounting procedures to ensure that fees are maintained and used only for the purpose for which they are collected. Upon request, a municipality must explain the basis of its fees.*

Regarding building permit fees, Section 1300.0165 subp. 2 of the State Building Code reads:

Subp. 2. Fees commensurate with service.

*Fees established by the municipality must be by ordinance and must be **fair, reasonable, and proportionate to the actual cost of the service for which the fee is imposed.***

Finally, it is instructive to review the “purpose” section of the building code to see that the code is intended to accomplish a fairly broad set of goals.

1300.0030 Purpose and Application

Subp. 1. Purpose.

The purpose of the code is to provide minimum standards to safeguard life and limb, health, property, and public welfare, by regulating and controlling the design, construction, quality of materials, use and occupancy, location, and maintenance of all structures and equipment specifically covered by the code in a jurisdiction that adopts and enforces the code.

Legal Challenges

At least three cities have been sued challenging the amount of fees being collected by the cities. The two most recent suits brought against the cities of Shakopee and Elk River by the Builders Association of the Twin Cities and the Builders Association Minnesota, claim that the cities charged excessive fees. The following are excerpts from the complaints in the two suits.

“To the extent that Elk Rivers[/Shakopees] building permit fees have exceeded the cost of reviewing, investigating and administering applications for building permits, the City has charged an unreasonable and unauthorized charge on builders.”

“As such building permit fee applicants from 1998 to 2004 are entitled to a full refund of all building permit fees charged by the City that exceed the cost of reviewing, investigating and administering applications for building permit . . .”

“Elk Rivers[/Shakopees] collection, retention and use of building permit fee revenue that exceeds its costs of reviewing, investigating and administering applications for building permits constitutes a taking of private property under the Fifth and Fourteenth Amendment of the United States Constitution and Article 1, Section 13 of the Minnesota Constitution.”

Recommendations

In light of these legal requirements we suggest that the cities adopt the following practices:

- 1) Cities should review, evaluate, and adopt their fees on an annual basis in order to make sure the fees are “fair, reasonable, and proportionate to the actual cost of the service for which the fee is imposed.”
- 2) Prior to filing the city’s annual report with the Department of Administration, the city should consult with its finance department and possibly its auditor, to make sure that all expenses reasonably associated with building code administration and enforcement, and development activity are adequately captured on the reporting form. (See, Methodology below)
- 3) In adopting building and development fees, cities should not blindly rely on boilerplate fee schedules that may have been established without closely reviewing the costs associated with the services provided.

Methodology for establishing defensible fees

Step 1

Identify all direct cost associated with the building code administration activities. These would include:

- most, if not all, of the salary and benefits associated with staff involved directly in the building code administration function;
- the annualized cost of supplies, equipment and materials associated with the building code administration function.

Step 2

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

Step 3

Interview the other city departments to determine what percentage of those departments’ time is reasonably related to supporting building codes administration activities. Once that "time spent" evaluation is completed, allocate a percentage of the cost of those department budgets to the building codes administration function. The following departments are likely to devote at least some time to support the code administration function:

- Planning, zoning and development
- Engineering and Public works
- Public safety (police and fire)
- Park and recreation

Step 4

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

Step 5

Since building permit fees must be based on valuation, you then have to make an estimate of potential valuation and set your fees accordingly, to generate sufficient revenue to cover all or a portion of the costs calculated in Step 4.

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