

Utility, Pipeline, and Railroad Operating Property: Current System

Property tax in Minnesota is an ad valorem tax. This means that property tax in Minnesota is based on a property's estimated market value. Each property owner pays their share of the local jurisdiction's levy based on the property's estimated market value, and tax capacity rate.

The department determines the market value of utility, pipeline, and railroad operating property, using unitary valuation.

Unitary valuation means we value all of the operating assets working together as an integrated unit. We do not value each asset individually.

We follow these steps:

1. Estimate the system value of the operating property
2. Allocate a portion of the value to Minnesota
3. Remove locally assessed and non-taxable property
4. Apportion the remaining value to operating property, by parcel and property type
5. Apply equalization

The sixth step is when the department certifies the apportioned, rounded, and equalized values to the counties and the counties use those values to calculate, bill, and collect property taxes.

We follow [Minnesota Rules 8100](#) for valuing utility and pipeline operating property and [Minnesota Rules 8106](#) for valuing railroad operating property.

We complete two types of valuations to estimate the value of the operating property:

1. Unit valuation

We complete cost, income, and market approaches to arrive at a range of indicated values. The market approach in most appraisal is based on sales.

As sales are limited for these properties, one of the market approaches we use is called the stock and debt method. It's based on the accounting equation for the balance sheet: assets = liabilities + stockholders' equity. We take the market value of liabilities (debt) and the market value of stock to estimate the market value of the assets.

The cost approach is the net cost of the company's assets used in its operations as reported on its balance sheet.

The income approach is a simplified discounted cash flows model, which assumes the same level of income into perpetuity, with a zero-growth assumption. For railroads, we estimate the level of income using an average of the past five year. For utilities and pipelines, we use a weighted average of the past three years, weighting the most recent years heavier.

The level of income divided by the yield capitalization rate equals the indicator of value. We develop a [capitalization rate study](#) each year to develop the rates for each market segment. We estimate how much it costs a market segment to finance operations with debt and equity and the percentage of debt and equity used by the market segment.

2. Cost-less-depreciation

This method starts with the original cost of the company's taxable operating property located in Minnesota and reduces it by 2.5% each year, up to a maximum reduction of 75%.

Cooperatives had an option to use this simple method or use the unit valuation method explained above. Companies which are non-regulated, are not common carriers, or do not operate in a traditional profit-making mode, should use this option.

Allocation and apportionment are separate mechanisms. Allocation assigns a portion of the system value to Minnesota. Apportionment assigns a portion of the taxable value of the operating property in Minnesota to each parcel with operating property, by property type.

Neither allocation nor apportionment develop market value. They simply assign the market value to Minnesota and to each parcel.

Watch our [Utility, Pipeline, and Railroad Valuation webinar](#) for a detailed overview of the process.

This document clarifies some aspects of the current system. If you have any questions, please contact us at sa.property@state.mn.us.

What is operating property?

For utility and pipeline companies, operating property is defined in [Minnesota Rules 8100.0100](#), subpart 11 and generally means the property integral to the operations of the company. Land is always non-operating, which means it is always locally assessed. If there is non-operating property on the same parcel as operating, it is all assumed to be operating related to utilities and pipelines.

For railroad companies, operating property is defined in [Minnesota Rules 8106.0100](#), subpart 13 and generally means property that is used on a regular and continual basis in the performance of railroad transportation services. The department includes land that is part of railroad operations as part of the state assessment. A portion of a building can be operating and a portion non-operating related to railroads. This means a portion a building can be locally assessed, and state assessed. Having a building assessed by two separate jurisdictions can cause confusion.

Original Cost

Original cost is the undepreciated cost recorded on the owner's accounting records and includes all hard and soft costs necessary to place the property into service. If a company purchases more plant, the cost

on the company's accounting records increases by the cost of the additional plant. If a company retires plant, the cost on the company's accounting records decreases by the cost of the retired plant.

We use original cost of a company's operating property at each parcel to assign a portion of the apportionable market value to each parcel for utility and pipeline companies.

We use original cost less depreciation as the cost indicator of value for utility, pipelines, and railroads. This is an oversimplification of the process but provides a high-level explanation of the cost indicator.

Estimated Taxes

The department calculated the estimated property taxes for utility, pipeline, and railroad operating property payable in 2024 at \$578 million.

We took the 2023 assessment year apportioned and equalized market values at each parcel and applied the city/township's effective tax rate. We used the public utility effective tax rate for utility and pipeline operating property and the railroad effective tax rate for railroad operating property. If a city/township did not have a rate available, we used the countywide average effective tax rate for the respective industry. The effective tax rates are for the 2023 payable year as the 2024 payable rates were not available at the time of analysis.

Electric Cooperatives

Electric cooperative companies, which are currently assessed by the department, could be included in this gross operating revenues tax mechanism if it moves forward. Electric cooperatives that pay a per-member tax do not pay property taxes on their distribution lines outside city limits. These cooperatives would have their revenues reduced by a factor of the cooperative's property outside city limits divided by its total operating property in Minnesota. For example, if an electric cooperative, paying the per-member tax, has 80% of its property outside of city limits, their revenues would be reduced by 80%.

Income Level and Relationship to Apportionable Market Value

In general, larger companies tend to pay a smaller portion of property taxes, when compared to their gross operating revenues, than smaller companies. Effective tax rates vary widely across the state. These facts, along with many other factors, make it difficult to change to a new system without causing shifts. These facts also highlight some equity issues in the current system.

When looking at companies for which we have access to full revenue data, we see an 11% increase per year, on average, since 2016 assessment year, averaged for all companies. That is, we took the average percent change for each year since 2016 assessment year and averaged that for each company and then took an average of each company's average. If we look at 2023 assessment year net operating income compared to 2016 assessment year, we see an increase of 67% based on an average of all companies. Same calculations but using gross operating revenues instead of net operating income, we see an average annual percent change for all companies of 15 % and an average change in 2023 assessment year over 2016 assessment year of 76%. The standard deviation in the annual percent change calculations is 0.687 for net operating income and 0.193 for gross operating revenues. This indicates the

percent change for gross operating revenues are less spread out than the percent change for net operating income.

The Minnesota Apportionable Value for the operating property of these same companies increased 49% for all companies combined in 2023 assessment year compared to 2016 assessment years. The average of each company's annual percent change is 3%.

This table shows the average annual percent change across all companies in gross operating revenues, net operating income, and apportionable market value. It also averages each company's change in 2023 compared to 2016 assessment years. Finally, it shows the standard deviation in the annual percent change, averaged for each company. These calculations only include companies for which we have full income data.

Table: Comparing 2023 Assessment Year to 2016 Assessment Year (2022 calendar year to 2015 calendar year)

	Net Operating Income	Gross Operating Revenues	Minnesota Apportionable Value
Average annual increase	11%	15%	3%
Average increase in 2022 AY compared to 2016 AY	67%	76%	49%
Standard deviation of annual percent change	0.687	0.193	0.179

This table shows the Minnesota Apportionable Values for the 2015 – 2023 assessment years for utility, pipeline, and railroad operating property combined (not just companies for which we have full income data).

Table: MN Apportionable Market Value by Assessment Year

Assessment Year	MN Apportionable Market Value	Percent Change
2015	15,145,076,816	
2016	14,771,333,441	-2.47%
2017	15,685,522,568	6.19%
2018	15,898,582,570	1.36%
2019	15,743,154,498	-0.98%
2020	17,401,517,650	10.53%
2021	18,106,726,247	4.05%
2022	20,630,037,451	13.94%
2023	20,912,939,590	1.37%
2023 minus 2015	5,767,862,774	38.08%

The Minnesota Apportionable Value is the taxable value of the company's operating property in Minnesota. It is the market value spread to each parcel with taxable operating property.

The 2023 assessment year Minnesota apportionable value is 38% greater than the 2015 assessment year valuation. This is for all companies, not those for which we have income data.

Company-Reported Financials

We currently rely on companies to report financial information to us. We audit/review data reported to us using publicly available information and verification provided to us by the company. Companies must certify the information they provide to us is true and complete. Making false statements on the returns companies submit to us is against the law. [Minnesota Statutes § 609.41](#) states that anyone giving false information in order to avoid or reduce their tax obligation is subject to a fine of up to \$3,000 and/or up to one year in prison.

Power Line Credit

This idea would repeal the [power line credit](#). The power line credit is a credit for some properties that are crossed by high voltage transmission lines.

For taxes payable in 2023, 4,091 parcels received the power line credit. The highest credit was \$1,965. The average credit was \$170.62. The minimum credit was \$10.03. There were 2,045 parcels with a credit below \$100. There were 282 parcels with a credit over \$500.

Pollution Control Property

Real or personal property that is used to primarily reduce or control air, water, or land pollution may qualify for a [pollution control exemption](#).

We remove property that has a pollution control exemption as part of the non-taxable property in the apportionable value calculation. We do not assign/apportion part of the value to property that has a pollution control exemption.

Battery Energy Storage Systems

In general, if the battery energy storage systems are not part of an electric generation, transmission, or distribution system, they will be exempt from property tax under [Minnesota Statutes § 272.02](#), subdivision 9. We are aware of several battery energy storage systems, which we do not consider to be part of an electric generation, transmission, or distribution system, and the local assessor determines which portion of the property is subject to property tax. [We have more information regarding the property tax treatment of battery energy storage systems on our website.](#)