

STATE OF MINNESOTA
OFFICE OF ADMINISTRATIVE HEARINGS
FOR THE MINNESOTA DEPARTMENT OF REVENUE

In the Matter of the Proposed
Rules of the Department of
Revenue Governing the Valuation
and Assessment of Electric, Gas
JUDGE
Distribution and Pipeline
Companies (Utility Companies)

REPORT OF THE
ADMINISTRATIVE-LAW

The above-entitled matter came on for hearing before Administrative Law Judge Peter C. Erickson at 9:00 a.m. on Tuesday, October 24, 1989 in the Eighth Floor Conference Room, Minnesota Department of Revenue Building, 10 River Park Plaza, St. Paul, Minnesota. This Report is part of a rule hearing proceeding, held pursuant to Minn. Stat. §§ 14.131 - 14.20 to determine whether the agency has fulfilled all relevant substantive and procedural requirements of law, whether the proposed rules are needed and reasonable, and whether or not the rules, if modified, are substantially different from those originally proposed.

Patrick J. Finnegan, Staff Attorney, Appeals and Legal Services Division, Mail Station 2220, St. Paul, Minnesota 55146-2220, appeared on behalf of the Minnesota Department of Commerce. Alan Whipple, Manager of the State Assessed Property Section, and Gerald Garski, Assistant Director of the Local Governmental Services Division, testified in support of the proposed rules on behalf of the Department. The hearing continued until all interested groups and persons had had an opportunity to testify concerning the adoption of the proposed rules.

This Report must be available for review to all affected individuals upon request for at least five working days before the agency takes any further action on the rule(s). The agency may then adopt a final rule or modify or

withdraw its proposed rule. If the Commissioner of the Department of Revenue makes changes in the rule other than those recommended in this report, he must submit the rule with the complete hearing record to the Chief Administrative Law Judge for a review of the changes prior to final adoption. Upon adoption of a final rule, the agency must submit it to the Revisor of Statutes for a review of the form of the rule. The agency must also give notice to all persons who requested to be informed when the rule is adopted and filed with the Secretary of State.

Based upon all the testimony, exhibits, and written comments, the Administrative Law Judge makes the following:

FINDINGS QF FACT

Procedural Requirements

1. On August 9, 1989, the Department filed the following documents with the Chief Administrative Law Judge:

- (a) A copy of the proposed rules certified by the Revisor of Statutes.
- (b) The Order for Hearing.
- (c) The Notice of Hearing proposed to be issued.
- (d) A Statement of the number of persons expected to attend the hearing and estimated length of the Agency's presentation.
- (e) The Statement of Need and Reasonableness.

2. On September 18, 1989, a Notice of Hearing and a copy of the proposed rules were published at 14 State Register pp. 713-22.

3. On September 15, 1989, the Department mailed the Notice of Hearing to all persons and associations who had registered their names with the Department for the purpose of receiving such notice.

4. On September 27, 1989, the Department filed the following documents with the Administrative Law Judge:

- (a) The Notice of Hearing as mailed.
- (b) The Agency's certification that its mailing list was accurate and complete.
- (c) The Affidavit of Mailing the Notice to all persons on the Agency's list.
- (d) An Affidavit of Additional Notice.
- (e) The names of Department personnel who will represent the Agency at the hearing together with the names of any other witnesses solicited by the Agency to appear on its behalf.
- (f) A copy of the State Register containing the proposed rules.
- (g) All materials received following a Notice of Intent to Solicit Outside Opinion published at 13 State Register page 2050 (February 21, 1989) and a copy of the Notice.

The documents were available for inspection at the Office of Administrative Hearings from the date of filing to the date of the hearing.

5. The period for submission of written comment and statements remained open through November 13, 1989. The hearing record closed on November 16, 1989, at the end of the third business day following the close of the comment period.

Statutory Authority

6. Statutory authority to promulgate the proposed rules is found at Minn. Stat. § 270.06 (14) which clearly states that the Commissioner of Revenue shall "promulgate rules . . . for the administration and enforcement of the property tax

Nature Of the Proposed Rules

7. The Department of Revenue is proposing five revisions to the existing ad valorem valuation and assessment rules for utility property. The first proposed change increases the amount of depreciation which will be allowed as a reduction of the cost of the utilities' property. The proposed rule will then more closely approximate the replacement cost for the utilities' property and also operate as a hedge against inflation. The second proposed change adjusts the valuation method for electric utility generating plants to take into account the effect of inflation on the property value. The third proposed change deletes the reference to prior years' capitalization rates and specifies that a separate rate will be computed for electric companies, gas distribution companies and pipelines. The fourth change adds a definition of "qualifying construction work in progress" and a clarification that "work in progress" is not taxable until the parts are installed to the utility property. The fifth proposed change adjusts the method of apportioning the Minnesota portion of the unit value to the taxing districts in Minnesota by using the current original cost as a method to apportion value.

8. Generally, the utility companies support the proposed rules because the greater depreciation allowance will lessen the amount of property taxes they will have to pay. However, the companies would favor a rule that would permit the use of full book depreciation to make tax savings even greater. Local units of government oppose the proposed rules because, pursuant to their taxing authority, less property taxes will be collected if the greater depreciation allowance is permitted. In some instances, public utility company property constitutes a significant portion of the taxable property in a county, municipality, or other taxing district. The Department emphasizes that the proposed rules focus on proper valuation, not taxation.

9. Several of the proposed rule provisions received no negative public

comment and were adequately supported by the Statement of Need and Reasonableness. The Judge will not specifically address those rules in the discussion below and finds that the need for and reasonableness of those provisions has been demonstrated.¹ The Judge will primarily discuss below specific issues concerning the need for, reasonableness of, or statutory authority for the proposed rules.

Modifications-Made-by-the Department-After- the Rearing

10. Subsequent to the hearing, and after a review of the oral testimony and written comments submitted, the Department modified the proposed definition of "qualifying construction work in progress" as follows:

¹In order for an agency to meet the burden of reasonableness, it must demonstrate by a presentation of facts that the rule is rationally related to the end sought to be achieved. *Broen Memorial Home v. Minnesota Department of Human-Services*, 364 N.W.2d 436, 440 (Minn. App. 1985). Those facts may either be adjudicative facts or legislative facts. *MANufactured Housing institute v. Pettersen*, 347 N.W.2d 238, 244 (Minn. 1984). The agency must show that a reasoned determination has been made. *Manufactured Housing Institute* at 246.

Subp. 14a. Qualifying construction work in progress.
"Qualifying construction work in progress" means the cost of materials and associated charges which are not yet placed in a permanent site.

As initially proposed, the definition imposed a requirement of "attachment" to the utility property rather than "placement in a permanent site" as is now suggested. The Department contends that this modification will clarify the definition and be significantly easier to implement at the time of assessment. The Judge finds that the need for and reasonableness of the proposed modification has been demonstrated and concludes that it is not a substantial change to the rules as initially proposed.

Discussion of the Proposed Rules

11. The Sherburne County Assessor and an Association of "Local Governments" argue that the proposed rules should be modified by including a provision which requires all utilities to submit annually to the Department of Revenue a report containing information to assist the Department in the proper valuation of utility property. The Judge specifically finds that a provision such as this is not required to make the rules either reasonable or needed, however, the Department may wish to consider this proposal in the future depending upon the successful implementation of the proposed rules. Adoption of the modification at this time would constitute a substantial change to the rules as initially proposed.

12. The "Local Governments" Association also argues that the rules should be modified to provide for the structured input from local units of government and other taxing districts. The Association contends that it is only through that kind of structured approach that the interests of local governments and the State of Minnesota can both be met. The Department states that there presently is a mechanism for input from local units of government, however, participation has been minimal in the past. The Department welcomes the input of local taxing

districts within the informal structure presently in use by the Department.

Although adoption of this modification would not constitute a substantial change to the rules as initially proposed, it is not required to make the rules either needed or reasonable. The record in this case shows that a mechanism presently exists for input by local government units as they are now requesting through formal rule modification.

13. As stated above in Finding 8, the initial thrust of the "local governments" opposition to the proposed rule is the fact that the liberalized depreciation allowance would result in less property taxes for local taxing districts. The City of Monticello estimates that it will lose approximately \$26,000 in 1990 and in each succeeding year. The Department estimates that the effect of the change in depreciation allowance will be to reduce the valuation and tax of electric companies by 1.21% per year and all utility companies by 1.07% per year. Due to the Commissioner's broad and clear authority to regulate the assessment and valuation of utility properties, and the "small" impact the greater depreciation allowance will have on local units of government, the Judge finds that the Department has demonstrated the reasonableness of the proposed new depreciation allowance.

Based upon the foregoing Findings of Fact, the Administrative Law Judge makes the following:

CONCLUSIONS

1. That the Minnesota Department of Revenue gave proper notice of the hearing in this matter.

2. That the Department has fulfilled the procedural requirements of Minn. Stat. §§ 14.14, and all other procedural requirements of law or rule.

3. That the Department has documented its statutory authority to adopt the proposed rules, and has fulfilled all other substantive requirements of law or rule within the meaning of Minn. Stat. §§ 14.05, subd. 1, 14.15, subd. 3 and 14.50 (i) and (ii).

4. That the Department has demonstrated the need for and reasonableness of the proposed rules by an affirmative presentation of facts in the record within the meaning of Minn. Stat. §§ 14.14, subd. 2 and 14.50 (iii).

5. That the additions and amendments to the proposed rules which were suggested by the Department after publication of the proposed rules in the State Register do not result in rules which are substantially different from the proposed rules as published in the State Register within the meaning of Minn. Stat. § 14.15, subd. 3, Minn. Rule 1400.1000, Subp. 1 and 1400.1100.

6. That any Findings which might properly be termed Conclusions and any Conclusions which might properly be termed Findings are hereby adopted as such.

7. That a finding or conclusion of need and reasonableness in regard to any particular rule subsection does not preclude and should not discourage the Department from further modification of the rules based upon an examination of the public comments, provided that no substantial change is made from the proposed rules as originally published, and provided that the rule finally adopted is based upon facts appearing in this rule hearing record.

Based upon the foregoing Conclusions, the Administrative Law Judge makes the following:

RECOMMENDATION

It is hereby recommended that the proposed rules be adopted consistent with the Findings and Conclusions made above.

Dated this 22 day of November, 1989.

PETER C. ERICKSON
Administrative Law Judge