Property Taxation 101

INFORMATION MEMO

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The property tax system

This is a description of the basics of Minnesota's property tax system. Local governments will collect just over $11 billion in 2023 to help fund the services of schools, counties, cities, townships, and special districts. The state also collects property tax from certain seasonal and commercial properties.

One of the challenges of trying to understand this system is the complex array of terms involved. A glossary at the end of the page has short definitions of key terms.

Assessment and classification

The property tax system is a continuous cycle, but it effectively begins with local assessors estimating property market values. Assessors try to determine the approximate selling price of each parcel of property based on current market conditions.

A property class is also assigned to each parcel of property based on the use of the property. For example, property that is owner-occupied as a personal residence is classified as a residential homestead.

The classification is important because the Minnesota system assigns a weight to each class of property. Generally, properties associated with income production (e.g., commercial and industrial properties) have a higher classification weight than other properties.

The tax capacity of each parcel is a percentage of each parcel's market value.

That is: [parcel market value] * [class rate] = [parcel tax capacity]

For example, a $75,000 home classified as a residential homestead has a class rate of 1.0% and therefore a tax capacity of $75,000 x .01 or $750.

View class rates on the Minnesota House Research Department website

Local levies

The next step is to determine each local unit of government's property tax levy. Each year, the city, county, school district, and any special property taxing authorities must establish how much property tax they want to collect in the following year by Dec. 28.

For cities, the property tax levy is set after the consideration of all other revenues, including state aids like local government aid (LGA).

That is: [city budget] – [all non-property tax revenues] = [city levy]

For many cities within the seven-county Twin Cities metropolitan and on the Iron Range, the levies are reduced by an amount of property tax revenue derived from the metropolitan and range area fiscal disparities programs.

View information on the fiscal disparities program

View the latest fiscal disparities data for metro and Iron Range cities

Local tax rates

Local governments do not set a tax rate. The tax rate is a function of the levy and the total tax base. To compute the local tax rate, a county must determine the total tax capacity to be used for spreading the levies. The county:

- Aggregates the tax capacities of all parcels within the city.
- Makes several adjustments to this total because not all tax capacity is available for general tax purposes.

The result of this calculation is the taxable tax capacity, which is used to determine the local tax rates.

The county calculates the city tax rate by dividing the city levy (minus the fiscal disparities distribution levy, if applicable) by the taxable tax capacity.

That is: [city levy] / [taxable tax capacity] = [city tax rate]. The tax rate is expressed as a percentage.

This same calculation is completed for the county based on the county's levy and tax base, the school district, and all special taxing authorities. The sum of the tax rates for all taxing authorities that levy against a single property produces the total local tax rate. The county uses the total local tax rate to determine the overall tax burden for each parcel of property.

Parcel tax calculations

The property tax bill for each parcel of property is determined by multiplying the parcel's tax capacity by the total local tax rate.

That is: [parcel tax capacity] * [total local tax rate] = [tax capacity tax bill]

The tax statement for each individual parcel itemizes the taxes for the county, municipality, school district, and any special taxing authorities.

To complicate the tax calculations, voter-approved referenda levies are applied to the market value of each parcel, not tax capacity. As a result, each identically valued parcel, regardless of the property's use, pays the same amount of referenda taxes (with the exception of certain agricultural and seasonal recreational properties, which are exempted from referenda taxes).

That is:

- [parcel market value] * [market value tax rate] = [market value tax bill]
- [tax capacity tax bill] + [market value tax bill] = [total tax bill]

Typically, only a handful of counties and cities collect these referenda levies. Most school districts do so.

State property tax

The state collects property tax on all commercial, industrial, seasonal recreational, and utility real property. The proceeds are deposited in the state general fund.

Property tax credits

Several tax credits for various types of properties are available in certain instances. These amounts are subtracted from the overall taxes for each parcel to determine the net tax bill for the individual owner. Minnesota provides additional property tax relief directly to individual homeowners, cabin owners, and renters through the circuit breaker and the targeting refund programs.

View details on state homeowner property tax relief programs

Property tax intricacies

The technical details of computing property taxes mask many other intricacies of the property tax system.

Over time, the system has become more complex and difficult for taxpayers to understand. Local officials must frequently explain how the system works and can only control local levy decisions. They have no direct ability to modify the overall structure of the tax system.

Many communities over the past several years have experienced situations where individual property taxes rise much faster than the increase in the levies that are certified by local units of government.

Change to estimated market value

The most common factor that results in an increase in an individual parcel's tax is the change in the parcel's estimated market value. Without any change in local levies, a property owner can experience a tax increase due almost exclusively to any valuation increase.

Legislative changes to the classification system

The Legislature sometimes makes changes the classification system. Changes to the classification system can shift property tax burdens from one type of property to another.

Legislative changes in state aid programs can also affect the revenue needed to be raised from the property tax. The Legislature has often made changes to the distribution formula for LGA and adjusted the total amount of funding available. The 2023 Legislature made some changes to the distribution formula for LGA and increased the total appropriation for cities to $644 million for 2024 and beyond.

Economic factors

Economic factors that may affect broad classes of property can also influence the overall tax changes for individual parcels of property. For example, in the early 1990s the metropolitan area experienced major declines in the valuation for commercial and industrial properties. These valuation declines shifted taxes from property classified as commercial and industrial to all other types of property. Valuation declines also may have accentuated the levy changes by local units of government.

Levy limits

Levy limits also impact local levy decisions when they are put in place by the Legislature Most recently, the 2013 Legislature implemented one-year levy limits for taxes payable in 2014 for cities over 2,500 in population.

Glossary of terms

- **Circuit breaker:** A state-paid property tax refund program for homeowners who have property taxes out of proportion with their income. A similar program is also available to renters.
- **Class rates:** The percent of market value set by state law that establishes the property's tax capacity subject to the property tax.
- **Fiscal disparities programs:** Local units of government in the Twin Cities metropolitan area and on the Iron Range participate in property tax base sharing programs. Under these two programs, a portion of the growth in commercial and industrial property value of each city and township is contributed to a tax base sharing pool. Each city and township then receives a distribution of property value from the pool based on market value and population in each city. View information on the fiscal disparities program.
- **Homestead Market Value Exclusion (HMVE):** Eligible homesteads will pay property taxes on only a portion of the value of their homes. The maximum exclusion, 40% of value, occurs at home value of $95,000 and phases out as home value grows. View information on the Homestead Market Value Exclusion.
- **Local government aid (LGA)**: A state government revenue sharing program for cities and townships that is intended to provide an alternative to the property tax. LGA is distributed using different formulae for cities over 2,500 and cities under 2,500. Those formulae include factors such as population, population change, and the share of households built before 1940. View information on how local government aid works.
- **Local tax rate**: The rate used to compute taxes for each parcel of property. Local tax rate is computed by dividing the certified levy (after reduction for fiscal disparities distribution levy and disparity reduction) by the taxable tax capacity.
- **Market value:** An assessor's estimate of what property would be worth on the open market if sold. The market value is set on Jan. 2 of the year before taxes are payable.
- **Property class:** The classification assigned to each parcel of property based on the use of the property. For example, owner-occupied residential property is classified as homestead.
- **Property tax levy:** The tax imposed by a local unit of government. The tax is established on or around Dec. 28 of the year preceding the year the levy will be paid by taxpayers.
- **Targeting refund:** A state paid property tax refund for homeowners whose property taxes have increased by more than 12%. A similar program is available to cabin owners.
- **Tax capacity:** The valuation of property based on market value and statutory class rates. The property tax for each parcel is based on its tax capacity.
- **Total tax capacity:** The amount computed by first totaling the tax capacities of all parcels of property within a city. Adjustments for fiscal disparities, tax increment, and a portion of the

powerline value are made to this total since not all tax capacity is available for general tax purposes.

- **Truth-in-taxation**: The "taxation and notification law" which requires local governments to set estimated levies, inform taxpayers about the impacts, and announce which of their regularly scheduled council meetings will include a discussion of the budget and levy. Taxpayer input is taken at that meeting.

Resources

View information on Paying for City Services

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