



Kentucky Department of Revenue Reclassifies All Transmission Pipelines

Jun 02, 2023

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In a recent email notification to taxpayers filing Kentucky Public Service Company ("PSC") tax returns and publication on its [website](#), the Kentucky Department of Revenue (the "Department") alerted PSCs owning transmission pipelines (oil, gas, and water) that the Department is reclassifying the tax treatment of all transmission pipelines for PSC tax purposes.

The notification provides that although the Department has historically classified transmission pipelines as real property, beginning for tax year 2023, the Department has re-classified such transmission pipelines as tangible property; notably, the announcement was made *after* the 2023 tax return filing due date. The Department provides in its notification that this reclassification is in response to a recent Kentucky Court of Appeals decision, *Department of Revenue v. Marathon Pipe Line LLC*, 653 S.W. 3d 104 (Ky. App. 2022) (discretionary review denied by the Kentucky Supreme Court, Oct. 12, 2022).

In *Marathon Pipe Line*, the classification of the taxpayer's pipeline was one of several issues in dispute. In Kentucky, 103 KAR 8:090 provides the classification for various PSC properties, including all oil, gas and water transmission pipelines, as real property. Based on the evidence presented therein, the Kentucky Court of Appeals ruled that the taxpayer's pipeline was appropriately classified as tangible property instead of real property.

This change in policy by the Department raises a number of questions for PSCs operating pipelines. In terms of the PSC tax, first and foremost, the tangible property tax rate in Kentucky is higher than the real property rate; thus, this reclassification could result in a higher PSC tax burden for these taxpayers.

But the reclassification also raises interesting issues. For example, if the pipelines are classified as tangible property instead of real property, would the manufacturing exemption perhaps apply,

making the overall tax rate less than the real property tax rates used previously? Manufacturing personal property is exempt from all local tax and carries a very favorable state-level tax rate.

Another consideration is whether there will be an impact on how quickly the property can be depreciated if classified as tangible property instead of real property, regardless of whether manufacturing property or not.

Outside of the context of the PSC tax, there are still other tax implications that may result from this reclassification of pipelines. If manufacturing tangible property, might these pipelines be afforded other Kentucky tax benefits, such as sales tax exemptions for manufacturing-related tangible property purchases, as well as other sales tax-related statutes, such as economic development incentives?

Ultimately, the Department's reclassification of all pipelines based on the Kentucky Court of Appeals' decision for one (1) pipeline could change the entire taxing scheme of the utilities and manufacturing industries in many ways.

We will continue to monitor information and guidance provided by the Department in response to this administrative notification and the consequences thereof. For more on PSC tax and other Kentucky tax news, visit Frost Brown Todd's [Tax Law Defined Blog](#).

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