

Exhibit No.:  
Issue: *Property Taxes*  
Witness: *Roy M. Boltz, Jr.*  
Sponsoring Party: *MoPSC Staff*  
Type of Exhibit: *True-up Surrebuttal Testimony*  
Case No.: *ER-2001-299*  
Date Testimony Prepared: *August 16, 2001*

**MISSOURI PUBLIC SERVICE COMMISSION**  
**UTILITY SERVICES DIVISION**

**TRUE-UP SURREBUTTAL TESTIMONY**  
**OF**  
**ROY M. BOLTZ, JR.**

**THE EMPIRE DISTRICT ELECTRIC COMPANY**

**CASE NO. ER-2001-299**

*Jefferson City, Missouri*  
*August 2001*

Exhibit No. 123  
Date 8/23/01 Case No. ER-2001-299  
Reporter KRM

1                                   **TRUE-UP SURREBUTTAL TESTIMONY**

2   **OF**

3   **ROY M. BOLTZ, JR.**

4   **CASE NO. ER-2001-299**

5                                   **THE EMPIRE DISTRICT ELECTRIC COMPANY**

6           Q.     Please state your name and business address.

7           A.     Roy M. Boltz, Jr., P.O. Box 360, Jefferson City, Missouri 65102.

8           Q.     By whom are you employed and in what capacity?

9           A.     I am a Regulatory Auditor with the Missouri Public Service Commission  
10   (Commission).

11          Q.     Are you the same Roy M. Boltz, Jr. who has previously filed direct,  
12   surrebuttal and true-up direct testimony in this case?

13          A.     Yes, I am.

14          Q.     What is the purpose of this true-up surrebuttal testimony?

15          A.     The purpose of this testimony is to respond to portions of the true-up  
16   rebuttal testimony filed by The Empire District Electric Company (Empire or Company)  
17   witness David W. Gibson regarding property taxes.

18          Q.     At page 1 of Mr. Gibson's true-up rebuttal testimony, he indicated that  
19   Empire disagrees with the Staff's amount of property tax expense included in the test  
20   year true-up audit. Do you agree with Mr. Gibson's criticism that the Staff's property tax  
21   annualization ignores proper matching of property tax expense to plant in service?

22          A.     No. The Staff calculated property taxes based upon the actual property tax  
23   payments at December 31, 2000, the end of the Staff's test year. This payment of tax is

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1 based on the value of the property owned as of January 1, 2000, which is the date  
2 property is assessed for taxing purposes. This relationship reflects how tax payments are  
3 actually determined by the taxing authorities.

4 Q. Why is the January 1 assessment date important?

5 A. The state and local taxing authorities use January 1 as the assessment date  
6 to determine the appraised value of the property which forms the basis of the property tax  
7 liability owed the state and political subdivisions for the calendar year. Any plant  
8 additions or property that are completed and booked to plant in service during the period  
9 of January 2 through December 31 of any given calendar year will not be assessed for  
10 property tax purposes until January 1 of the following year. In essence, the property tax  
11 liability associated with this plant is not due to the state and local taxing authorities until  
12 November-December of the subsequent year. Thus, unless the property was in-service on  
13 January 1, the taxes will not be owed until November-December of the following year.

14 As an example, any plant additions that Empire added to its plant in  
15 service on January 2, 2001, will not be assessed by the taxing authorities until January 1,  
16 2002, and property taxes thereon will not be due until November-December of 2002.

17 Q. Mr. Gibson states at page 2, lines 3 through 6 of his true-up rebuttal  
18 testimony that "The failure of the Staff to provide an updated amount of property tax in  
19 the cost of service to reflect this substantial property addition is, in my view, a clear  
20 violation of the matching principle whereby revenues are based or "matched" with their  
21 associated rate base and expenses." Do you agree?

22 A. No. Mr. Gibson is attempting to persuade the Commission that the Staff's  
23 calculation of property taxes is in some way a "mismatch" with Staff's normalizations

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1 and annualizations throughout the rest of its case. This is simply not true. The Staff has  
2 calculated the property tax annualization based upon how the taxing authorities assess  
3 and how Empire ultimately pays these taxes. Because of the unique nature of how  
4 property taxes are determined, the typical normalization and annualization process used  
5 by both the Company and the Staff for other expense items is not appropriate for property  
6 tax expense.

7           The previous example of plant additions included in plant in service on  
8 January 2, 2001, is an illustration of the unique nature of property taxes. Unlike a payroll  
9 or revenue annualization, which the Staff attempts to include through an end of the test  
10 year, the end of an update to the test year period, or the end of a true-up period, the  
11 January 2, 2001 plant in service balances will not be included in the Company's booked  
12 property tax expenses until January through December of 2002. Indeed, Empire will not  
13 accrue a property tax expense for any of the plant additions (including the State Line  
14 Combined Cycle (SLCC) unit) through June 30, 2001, the end of the Staff's true-up  
15 period, until January of 2002. This accrual will only be an estimate because the  
16 Company will not know the actual amount of property tax payments until late in 2002,  
17 when the tax bills are distributed by the taxing authorities, usually in November or  
18 December of that year.

19           Q.     Would it be appropriate to include an accrual/estimate of property taxes to  
20 be paid in 2002 in this rate case?

21           A.     No. No other expense item is being considered for inclusion in this case  
22 by the Staff or even Empire itself to go out to anytime in 2002. It is important to note  
23 that the property taxes that Empire will pay on or about December 31, 2001, represents

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1 the level of plant at January 1, 2001 which is the exact time period which the Staff used  
2 to calculate its property tax annualization in this case.

3 Q. Does Empire's proposal to include a level of property tax expense based  
4 upon plant in service as of June 30, 2001 violate the test year and update of the test year  
5 concept?

6 A. Yes. Empire's proposed level of property tax expense violates the test  
7 year and the true-up audit period in this case. This proposal does not represent a  
8 complete "package" of adjustments that appropriately reflects a consistent revenue-  
9 expense-rate base relationship at a point in time. As indicated previously, the property  
10 tax expense level proposed by Empire represents an estimated amount that the Company  
11 will not begin accruing on its books and records until January of 2002, and Empire will  
12 not know the exact amount payable for those property taxes until late in 2002. The actual  
13 property taxes themselves will not be paid until on or about December 31, 2002.  
14 Mr. Gibson has only considered one item of expense while not considering other items  
15 such as additional revenues from customer growth during 2002, property insurance,  
16 payroll annualizations, plant additions and retirements, depreciation reserve and possibly  
17 other items.

18 Q. Why is it important to maintain the proper relationship of the individual  
19 components that make up the revenue requirement?

20 A. It is very important that all elements of the revenue requirement be  
21 considered at a consistent point in time because events occur that result in constant  
22 changes in revenues, expenses and rate base that cause changes to the overall revenue  
23 requirements. Reflecting changes for only one element of the revenue requirement, in

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1 this case property taxes, without consideration of other offsetting changes in other  
2 revenue requirement components, will likely lead to setting a distorted level of rates.

3 Q. Has the Commission recognized the importance of maintaining the proper  
4 relationship between revenues, expenses and rate base in setting rates previously?

5 A. Yes. In its March 13, 1996 Suspension Order and Notice for Missouri Gas  
6 Energy, the Commission stated, "The Commission will not consider a true-up of isolated  
7 adjustments, but will examine only a "package" of adjustments designed to maintain the  
8 proper revenue-expense-rate base match at a proper point in time. *Re: Kansas City*  
9 *Power & Light Company, 26 Mo. P.S.C. (N.S.) 104, 110 (1983).*" Similar language has  
10 been used in many other rate proceedings by the Commission.

11 Q. Is Empire aware of the importance the Commission places on maintaining  
12 the proper relationship between revenues, expenses and rate base in setting rates?

13 A. Yes. In Case No. ER-97-81, The Empire District Electric Company, the  
14 Commission in its test year order rejected various true-up proposals and thus ordered:

15 . . . test year for use in this case as the twelve months  
16 ending September 30, 1996, with isolated adjustments,  
17 including consideration of State Line Unit II, through  
18 May 31, 1997. All isolated adjustments will be known and  
19 measurable, used and useful, and in-service prior to the  
20 adjustment cutoff date. In addition, the relationship  
21 between revenue, expense, and rate base will be maintained  
22 as accurately as possible in calculating any isolated  
23 adjustments.

24 Q. Is the Company's proposed level of property tax expense "known and  
25 measurable"?

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1           A.     No. Empire's proposed level of property tax expense is not a known and  
2     measurable expense, which can or should be included in the cost of service in this  
3     proceeding.

4           Q.     What does the term "known and measurable" mean?

5           A.     A "known and measurable" expense is an expense that is 1) "known,"  
6     meaning that the amount did or definitely will be an actually incurred cost and  
7     2) "measurable," meaning that the rate impact of the change (for example, property tax  
8     expense) can be calculated with a high degree of accuracy. The significance of this term  
9     is that historically the Commission has only reflected in rates those revenue requirement  
10    changes that were known and measurable at the time the rate decision was made.  
11    Certainly, property taxes that are not "known and measurable" until 2002 do not  
12    constitute a proper or appropriate inclusion into the cost of service in this case.

13          Q.     If the Company does not "know" what the actual amounts of property tax  
14    expense will be until late in a given year, how does Empire determine the level which it  
15    books to expense on a monthly basis?

16          A.     Each year the Company will attempt to estimate the appropriate expense  
17    level it believes will be incurred in that given year. It may change its estimate from time  
18    to time during the course of the year but, ultimately, when the actual property tax  
19    payment amount becomes known, Empire must book a "true-up" amount to make the  
20    actual property tax payment equal the level recorded for the year on its books and  
21    records. These "true-up" amounts are generally booked late in the year, usually in  
22    November or December. The actual amounts of property taxes associated with the  
23    June 30, 2001 plant levels (as well as any level of property tax on plant in service levels

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1 during 2001) will be estimated and booked as an expense beginning January 2002 and  
2 will not actually be known until November/December of that year. The property tax  
3 "true-up" adjustment to correct the earlier property tax estimates will not be until late  
4 in 2002, as it relates to 2001 additions. Thus, Empire's proposal regarding property taxes  
5 in this case would result in a "mismatch" of the "relationship between revenue, expense  
6 and ratebase."

7 Q. Is there a difference between the amounts charged to expense for property  
8 taxes for any given year and the property tax payments for that year?

9 A. Property taxes assessed on plant in service are expensed. Every year at the  
10 January 1 assessment date, there is also an amount of property taxes which is assessed on  
11 Empire's construction activities that is capitalized. The amount of property tax expensed  
12 are different than the total payment amounts because of the portion that is capitalized on  
13 the utilities books. In other words, the amount of property taxes expensed will be lower  
14 than the total property taxes paid because of the capitalized portion of property taxes.

15 Q. Mr. Gibson states at page 2, lines 9 through 10 of his true-up rebuttal  
16 testimony that Staff "has ignored the property taxes that will be paid as a direct result of  
17 this plant being built." Do you agree?

18 A. No. The Staff has not ignored the property taxes associated with the new  
19 SLCC plant. Those property taxes were appropriately capitalized and are included in the  
20 plant balances that Staff has recommended during the true-up audit through June 30,  
21 2001. Those property taxes were added to the applicable plant account balances which  
22 the Staff has included in its June 30, 2001 true-up revenue requirement. Empire will



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1 recover those property taxes in rates over the life of the asset through depreciation  
2 expense and a return component through rate base treatment.

3 Q. On page 4, line 21 of Mr. Gibson's true-up rebuttal testimony he states,  
4 "As can be seen from the preceding table, property taxes have increased since 1996."  
5 Do you wish to comment on this?

6 A. Yes. The preceding table he references is found on page 3 of his true-up  
7 rebuttal testimony. In that table, the line Electric represents the amounts that were  
8 expensed during the indicated period. The amount shown as being expensed for 1997  
9 related to Empire's electric operations decreased from the previous year 1996 and the  
10 amount for 2000 decreased from the previous year 1999 as well. Thus, it can be seen that  
11 the amounts of electric property tax expense for the Company both can increase and  
12 decrease over time which does not support the argument that property taxes can be  
13 accurately estimated for plant additions in future periods.

14 Q. On page 4, lines 12 through 19 of Mr. Gibson's true-up rebuttal testimony,  
15 he describes how he calculated the level of property tax expense that he is proposing. Do  
16 you agree with his calculation?

17 A. I agree that his mathematics are correct, but that calculation is not based  
18 on how property taxes are actually assessed. The December 31, 2000 or January 1, 2001  
19 plant balances are used to assess the property, not the June 30, 2001 plant balances. The  
20 June 30, 2001 plant balances will never be used for assessment purposes since that is not  
21 how the taxing authorities assess for property taxes. The June 30, 2001 balances will be  
22 included in the December 31, 2001 balances (or January 1, 2002 balances) for assessment  
23 purposes. The property tax payment amount will not be known until approximately

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1 November or December 2002 and the payment will not be actually due until  
2 December 31, 2002.

3 Q. Has this issue, or a similar issue, previously been tried before the  
4 Commission?

5 A. Yes, several times. In Case No. GR-96-285, Missouri Gas Energy (MGE)  
6 contended that the most current known and measurable plant balances should be used to  
7 calculate an ongoing level of property tax expense. Thus, MGE used a May 30, 1996  
8 plant balance in the annualization of property tax expense. The Staff's position was that  
9 the last actual property tax assessment should be used to determine property taxes for  
10 revenue requirement purposes. The Commission found in favor of the Staff's position on  
11 this issue. The Commission stated in its ruling that:

12 The Commission finds Staff witness Featherstone's persuasive where he  
13 states:

14 MGE will not accrue a property tax expense for any of the  
15 plant additions through May 31, 1996 identified in the  
16 Rebuttal Testimony of Mr. Kelly until January of 1997.  
17 This accrual will only be an estimate for which the  
18 Company will not know the actual amount of property tax  
19 payments until late in 1997, when the tax bills are  
20 distributed by the taxing authorities, usually in November  
21 or December of that year. (Ex. 73, p. 4)

22 The Commission finds that MGE's proposal would require  
23 waiting until the end of 1997 to account for an item of  
24 expense for inclusion in this case because this would be a  
25 violation of the test year, updated test year or true-up  
26 concepts. Staff's recommendation will be adopted.

27 In Case No. WR-2000-844, St. Louis County Water Company, that utility  
28 also argued that its property tax expenses should be based on the level of plant in service  
29 to be reflected in rates. The Commission in that case ruled:

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1 The Commission traditionally, and properly, allows  
2 recovery of cost increases that are projected to occur after  
3 the end of the test year (including any adjustment periods)  
4 only if those costs are known and measurable. A cost  
5 increase is "known" if it is certain to occur, and it is  
6 "measurable" if the Commission is able to determine the  
7 amount of the increase with reasonable precision. The  
8 Company's projected property tax increases are neither  
9 known nor measurable. While it is probable that the  
10 Company will experience an increase in property tax  
11 expense at the end of the year, it is by no means certain.  
12 Even more damaging to the Company's proposal is the fact  
13 that its best estimate of the amount of any increase is based  
14 on an assumption that finds no support in the record.  
15 Company's proposed property tax calculation assumes that  
16 the tax rates for 2000 will be the same as the tax rates for  
17 1999. Because any increase in the Company's property tax  
18 expense is not known and measurable, the Commission will  
19 not adopt the Company's proposal. Staff's proposal to use  
20 a known amount (the last amount actually paid), while  
21 probably not a perfectly accurate representation of the  
22 property taxes that will be paid in the future, at least avoids  
23 the speculation inherent in Company's proposal.

24 Q. Was the Staff aware that property tax expense on the SLCC plant going to  
25 be a true-up issue in this case?

26 A. No. At the Company's request, the Staff made a correction during the  
27 prehearing conference held during the week of April 16, 2001 for test year property tax  
28 expense, but no mention was ever made that property taxes related to the SLCC plant was  
29 going to be an issue. It was not listed as an issue under State Line Power Plant in the  
30 Company's Statement of Position on List of Issues filed May 15, 2001 nor was it listed in  
31 the Revised List Of Issues filed June 4, 2001. The Staff first learned that it was an issue  
32 on Friday, August 10, one workday prior to the Company's true-up rebuttal testimony  
33 being filed. While the Staff has not formally challenged the Company's true-up rebuttal  
34 testimony on the issue of property taxes, the Staff believes this issue could have and

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1 should have been presented to the Commission during the initial hearings for this  
2 proceeding in May-June 2001.

3 Q. Does this conclude your true-up surrebuttal testimony?

4 A. Yes, it does.

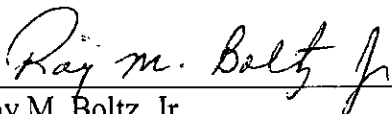
**BEFORE THE PUBLIC SERVICE COMMISSION**  
**OF THE STATE OF MISSOURI**

In the Matter of the Application of the Empire     )  
District Electric Company for a General Rate     )     Case No. ER-2001-299  
Increase     )

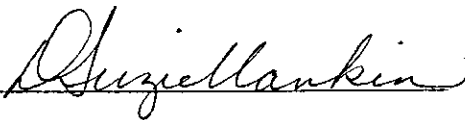
AFFIDAVIT OF ROY M. BOLTZ, JR.

STATE OF MISSOURI     )  
                                   )     ss.  
COUNTY OF COLE     ).

Roy M. Boltz, Jr., being of lawful age, on his oath states: that he has participated in the preparation of the foregoing True-Up Surrebuttal Testimony in question and answer form, consisting of 11 pages to be presented in the above case; that the answers in the foregoing True-Up Surrebuttal Testimony were given by him; that he has knowledge of the matters set forth in such answers; and that such matters are true and correct to the best of his knowledge and belief.

  
\_\_\_\_\_  
Roy M. Boltz, Jr.

Subscribed and sworn to before me this 17<sup>th</sup> day of August 2001.

  
\_\_\_\_\_

D SUZIE MANKIN  
NOTARY PUBLIC STATE OF MISSOURI  
COLE COUNTY  
MY COMMISSION EXP. JUNE 21, 2004