Exhibit No.:
Issue: Property Taxes
Witness: Melissa K. Hardesty
Type of Exhibit: Surrebuttal Testimony
Sponsoring Party: Kansas City Power & Light Company
Case No.: ER-2016-0285
Date Testimony Prepared: January 27, 2017

MISSOURI PUBLIC SERVICE COMMISSION

CASE NO.: ER-2016-0285

SURREBUTTAL TESTIMONY

OF

MELISSA K. HARDESTY

ON BEHALF OF

KANSAS CITY POWER & LIGHT COMPANY

Kansas City, Missouri
January 2017

SURREBUTTAL TESTIMONY

OF

MELISSA K. HARDESTY

Case No. ER-2016-0285

Q: Please state your name and business address.

A: My name is Melissa K. Hardesty. My business address is 1200 Main Street, Kansas City, Missouri, 64105.

Q: By whom and in what capacity are you employed?

A: I am employed by Kansas City Power & Light Company and serve as Senior Director of Taxes for KCP&L and KCP&L Greater Missouri Operations Company ("GMO").

Q: On whose behalf are you testifying?

A: I am testifying on behalf of KCP&L.

Q: Are you the same Melissa K. Hardesty who filed Rebuttal Testimony in this proceeding?

A: Yes, I am.

Q: What is the purpose of your Surrebuttal Testimony?

A: The purpose of my testimony is to respond to Missouri Public Service Commission ("MPSC") Staff ("Staff") witness Karen Lyons testimony regarding the use of an annualized property tax expense amount based on an average of the 2017 and 2018 property tax expense budget and the use of a property tax tracker requested by Kansas City Power & Light Company ("KCP&L" or the "Company"). Specifically, my testimony addresses the assumption by Ms. Lyons that property taxes are a direct result of increases in plant additions.

Q: How are property taxes determined by the states of Kansas and Missouri for utilities?

A: By statute in both Kansas and Missouri, electric utilities like KCP&L, are valued at the State level instead of the county or local level for all property except rail cars, construction work in progress, vehicles, and certain real estate and personal property in Missouri. This is generally referred to as being "centrally assessed." Both states start by determining the fair market value of the Company (not the fair market value of the Company's assets or property). Once the fair market value of the Company is determined, then the value is allocated pro-rata to the counties based on miles of distribution and transmission lines ("pole miles") in each county in Missouri, and allocated to the counties based on the historical cost of property in each county in Kansas. Once each county has its allocated share of "fair market value" of KCP&L, it then applies the mill levy determined for that year and sends KCP&L a bill. For the non-central assessed rail cars, construction work in progress, vehicles, and certain real estate and personal property in Missouri, the fair market value of each asset is determined by each county and then the county applies the mill levy determined for that year and sends KCP&L a bill. The aggregate amount of these bills represents the total amount of property taxes paid by KCP&L in a year.

Q: Please explain how the fair market value is determined by the states for utilities in Kansas and Missouri.

A: The state appraisers use three standard appraisal methods for determining the fair market value of KCP&L, upon which the property tax assessments for KCP&L are based. The three methods used are the Cost Approach (based on the cost of plant placed in service), the Income Approach (based on an average of net operating income of the entity over a certain period of time) and the Market Approach (based on the stock value of the company). Once the three calculations are done, the appraisers determine a fair market value that in their opinion is in line with these three calculations. Certainly the addition of plant in service directly impacts the calculation of fair market value for the Cost Approach. However, neither Missouri nor Kansas appraisers rely solely on the Cost Approach to determine fair market value. In fact, over the last several years, KCP&L's fair market values as established by state assessment authorities have been very close to the value determined by the Income Approach. That is, state assessment authorities have placed more emphasis on the Income Approach than either the Cost Approach or the Market Approach for KCP&L.

Q: Does Staff consider these other standard appraisal methods in its analysis of property taxes?

A: No, the Staff has ignored the impact that increases in the stock price or net operating income of the Company may have on the amount of property taxes paid by KCP&L. Either one of these factors may occur without a corresponding increase in plant in service.

Q: Staff's witness Karen Lyons included a table on page 28 in her Rebuttal Testimony that identified actual plant in service values at January 1 of each year and actual property taxes paid by KCP&L as support to justify the increase in property taxes. Does KCP&L agree with this table?

A: In part. Although the table is accurate, the conclusion Ms. Lyons draws from the table is flawed. KCP&L agrees that plant in service and property tax expense has increased significantly since 2007, as demonstrated by the table. However, the table also shows that the increases in property tax are not necessarily in relation to increases in plant in service. In 2009, plant in service increased from 2008 by 3.8%, but property tax on her table decreased by 5.1%. Even in recent tax years, such as 2013 and 2014, the plant in service balance increased by 2% and 4%, but property taxes increased by 6.7% and 6.6%.

Q: What other factors impact future property taxes?

A: Other factors that will impact future property tax expense include mill levies, net operating income of the Company, and cost of capital in the markets. The property tax mill levy rates are set by each county and then applied to the assessments by the various taxing authorities. These mill levy rates are adjusted up or down annually depending on the revenue needed by the taxing jurisdictions. The mill levy rates will increase if the taxing jurisdictions need to increase tax revenues to offset other sources of revenue that may decrease due to the economy or other factors. Net operating income from the Company and the cost of capital are used for the Income Approach appraisal method and as income increases or cost of capital decreases, the fair market value of the Company increases. It is the estimated increase in net operating income, which will be significantly driven by the revenue increases to be authorized from KCP&L's ongoing rate case in Missouri, that the Company estimates will drive increases in property tax estimates in future years.

Q: How does all this impact the Company's request for a property tax tracker?

A: Company witness Tim Rush provides more detailed testimony regarding the Company's request for a property tax tracker. However, Ms. Lyon states on page 27, lines 10 - 12, that "As a result of these additions, as well as other plant additions, KCP&L's property taxes have increased over the course of the past several years." And she adds on page 29, lines 6-8, that "Although KCPL will continue to make plant additions, the level of magnitude of the construction projects is not expected to compare to its most recent projects such as those previously discussed." Based on these statements, increases in plant in service appear to be the only factor that Staff considered as drivers for increases in property taxes. She does not consider that an increase in net operating income (that will likely occur as a result of this rate case) or other factors such as mill levies will impact our property taxes.

Q: Specifically, how will revenue increases authorized for KCP&L in its ongoing rate case in Missouri impact future property taxes?

A: In the current ongoing rate case in Missouri, KCP&L is requesting revenue increases for several factors, including recovery of new investments made since the 2014 rate case, and other expenses, not the least of which is significantly higher property taxes. This revenue will begin to impact net operating income (or earnings) of KCP&L once rates become effective. This increase in net operating income will impact the state assessor's determination of fair market value using the Income Approach on January 1 of the year following the increase in net operating income. Because only a few months of additional revenue from the 2014 rate case were in 2015, the Company only saw a partial increase in property taxes in 2016 (based on a January 1, 2016 assessment date) related to the investment in LaCygne environmental equipment and WCNOC. It will likely be 2017 or later before the full impact of the net operating income generated by those new rates, not to mention the current rate case, will be represented in the State assessments. As you can see there is a significant delay in the increase in property taxes due to large investments made by the Company. This is the basis for Company witness Tim Rush testimony requesting an annualized level of property tax expense base on an average of 2017-2018 property tax budget.

Again, it is this increase in net operating income in future years that we believe will be the primary factor for continued increases in property taxes in future years.

Q: **On pages 30 of her Rebuttal Testimony, Staff witness Karen Lyons questions whether KCP&L would have an incentive to participate in the property tax appeal process in the future if tracker treatment is afforded. How do you respond?**

A: My understanding is that tracker is not a guarantee of rate recovery and that any costs deferred pursuant to the tracker would be reviewed for rate recoverability in a future rate case. Because the Company knows that cost recovery is at risk, KCP&L will act to protect its interests and those of its customers in property tax assessment matters as it has in the past. Certainly any significant change in KCP&L's conduct in this regard would be readily apparent in subsequent rate case proceedings. While KCP&L has not formally appealed any property tax assessments in recent years, the Company assuredly would continue with its informal appraisal discussions and would formally appeal any property tax assessment that is not supported by generally accepted appraisal practices with or without a tracker.

Q: Should the Commission not approve the Company's request to use an annualized property tax expense based on forecasted property taxes and a property tax tracker, would you consider the method to true-up property taxes, as explained in Rebuttal Testimony by Staff Witness Karen Lyons appropriate?

A: Yes. If the Commission does not approve the Company's request of an average of the 2017 and 2018 property tax expense budget for the annualized property tax expense in this case and the use of a property tax tracker, then the use of the "ratio" method to true-up property taxes, as described by Staff witness Karen Lyons in her Rebuttal Testimony, would be appropriate. Ms. Lyons indicated that Staff will use the same approach to true-up annualized property taxes that was used in Case No. ER-2014-0370. This approach uses the property tax ratio of actual 2016 property tax expense to in-service property at January 1, 2016 applied to actual in-service plant as of January 1, 2017 to compute the annualized property tax expense in this case.

Q: Does that conclude your Testimony?

A: Yes, it does.

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of KCP&L Greater Missouri Operations Company's Request for Authority to Implement A General Rate Increase for Electric Service	)))	Case No. ER-2016-0285

AFFIDAVIT OF MELISSA K. HARDESTY

STATE OF MISSOURI)
) ss
COUNTY OF JACKSON)

Melissa K. Hardesty, being first duly sworn on his oath, states:

1. My name is Melissa K. Hardesty. I work in Kansas City, Missouri, and I am employed by Kansas City Power & Light Company as Senior Director of Taxes.

2. Attached hereto and made a part hereof for all purposes is my Surrebuttal Testimony on behalf of Kansas City Power & Light Company consisting of seven (7) pages, having been prepared in written form for introduction into evidence in the above-captioned docket.

3. I have knowledge of the matters set forth therein. I hereby swear and affirm that my answers contained in the attached testimony to the questions therein propounded, including any attachments thereto, are true and accurate to the best of my knowledge, information and belief.

Melissa K. Hardesty

Melissa K. Hardesty

Subscribed and sworn before me this 27th day of January 2017.

Nicole A. Wehry

Notary Public

My commission expires: Feb. 4, 2019

NICOLE A. WEHRY
Notary Public - Notary Seal
State of Missouri
Commissioned for Jackson County
My Commission Expires: February 04, 2019
Commission Number: 14391200