

**BEFORE THE STATE CORPORATION COMMISSION  
OF THE STATE OF KANSAS**

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**REBUTTAL TESTIMONY OF**

**ROBERT W. HRISZKO**

**ON BEHALF OF  
KANSAS CITY POWER & LIGHT COMPANY**

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**IN THE MATTER OF THE APPLICATION OF  
KANSAS CITY POWER & LIGHT COMPANY  
TO MODIFY ITS TARIFFS TO BEGIN THE  
IMPLEMENTATION OF ITS REGULATORY PLAN**

**DOCKET NO. 06-KCPE-828-RTS**

1 **Q: Would you please state your name, occupation and business address?**

2 A: My name is Robert W. Hriszko. I am a managing director in the firm of  
3 PricewaterhouseCoopers LLP. My business address is One North Wacker Drive,  
4 Chicago, IL 60606.

5 **Q: Would you please describe the firm of PricewaterhouseCoopers (“PwC”)?**

6 A: PwC is an international firm of independent public accountants with offices  
7 throughout the United States and in many countries. We have as clients a large  
8 number of both publicly and privately owned companies. The firm performs audits of  
9 financial statements, prepares and reviews income tax returns for all types of  
10 businesses, and consults with businesses regarding financial, accounting and tax  
11 matters. PwC audits a significant number of the electric, gas and telecommunications  
12 companies in the United States.

1 PwC also performs financial and accounting consultation services for utility clients  
2 and consults with utility clients on a variety of tax matters, including income tax  
3 issues raised in utility rate cases.

4 **Q: Would you please describe your professional background and qualifications to  
5 testify as an expert in this proceeding?**

6 A: I am a graduate of St. Mary's College in Winona, Minnesota, from which I obtained a  
7 Bachelor of Arts degree in Accounting and Economics in 1964. I am also a graduate  
8 of Northwestern University School of Law from which I obtained a Juris Doctor  
9 degree in 1967. I am a member of the American Institute of Certified Public  
10 Accountants, the Illinois CPA Society, and the Tax Committee of the American Bar  
11 Association.

12 **Q: What experience have you personally had in the utility field?**

13 A: I have spent my entire career working with utility companies on industry issues.  
14 After a 35-year career at Arthur Andersen LLP, I presently assist in directing the PwC  
15 tax practice for the utility industry in the U.S. and head the central region utility tax  
16 practice. I have been with PwC for four years. I am also responsible for technical  
17 matters involving federal income tax and related ratemaking issues. My  
18 responsibilities also include consulting with our offices throughout the world on tax  
19 matters relating to utility clients. In addition, I am responsible for the tax training  
20 programs the firm offers in the utility industry.

21 **Q: Have you previously testified before regulatory agencies?**

22 A: Yes. I have testified before the Public Utility Commission of Texas, the Illinois  
23 Commerce Commission, the Ohio Public Utility Commission, the Wisconsin Public

1 Utility Commission and the U.S. Treasury Department. My testimony has addressed  
2 the normalization requirements of the Internal Revenue Code as applied to various  
3 factual settings and various other tax issues in ratemaking proceedings. In addition to  
4 my personal testimony, I have reviewed testimony prepared by my present and  
5 predecessor firms and/or their clients on numerous occasions.

6 **Q: Have you previously testified in this docket?**

7 A: No. I have not.

8 **Q: What is the purpose of your testimony?**

9 A: The purpose of my testimony is to rebut certain aspects of the testimony of  
10 Mr. Jeffrey D. McClanahan of the Kansas Corporation Commission (“KCC”) Staff as  
11 it relates to the Contribution In Aid of Construction (“CIAC”) mechanism.

12 **Q: Do you agree with Mr. McClanahan that the CIAC should be grossed up for**  
13 **income taxes?**

14 A: Yes. The CIAC mechanism will result in additional book deductions in cost of  
15 service in the nature of additional book depreciation. However, no additional tax  
16 deductions will be available as a result of the CIAC. Thus, KCPL will have to pay  
17 additional taxes on its tax return on the revenue generated from the CIAC. The  
18 income tax gross-up is necessary for KCPL to have enough cash to satisfy the cash  
19 flow formula under the CIAC mechanism.

20 **Q: Mr. McClanahan indicates that he has a concern that the Staff of the Missouri**  
21 **Public Service Commission has proposed that the CIAC amount in Missouri not**  
22 **be grossed up for income taxes. Do you share that concern?**

1 A: Yes. I am filing rebuttal testimony in KCPL's Missouri case (on September 8, 2006)  
2 that disagrees with the Missouri Staff's contention that the CIAC amount should not  
3 be grossed up for income taxes. If no gross-up occurs in Missouri, KCPL will fall  
4 short of its cash flow requirements under the Missouri formula.

5 **Q: What is the nature of your disagreement with Mr. McClanahan's testimony?**

6 A: First, let me say that I agree with Mr. McClanahan that a tax gross-up is required. I  
7 also agree with the tax gross-up computed on the base CIAC amortization indicated  
8 by Mr. McClanahan, as well as the future net rate base effects of both. My  
9 disagreement centers around two items: first, Mr. McClanahan's discussion (see pp. 8  
10 and 9 of his testimony) of the deferred tax asset created by the CIAC and gross-up,  
11 and second, Mr. McClanahan does not include the tax gross-up as part of the CIAC  
12 amortization expense.

13 **Q: If you agree with Mr. McClanahan's computations and the resulting revenue**  
14 **requirement would not change, why would any disagreement on the deferred tax**  
15 **asset and the gross-up matter?**

16 A: The reason that the deferred tax asset and the gross-up must be treated correctly is to  
17 accurately reflect all aspects of the CIAC in KCPL's financial statements.

18 **Q: Please explain.**

19 A: As Mr. McClanahan notes on p. 7 of his testimony (lines 1-5), the Stipulation and  
20 Agreement, approved by the Commission in Docket No. 04-KCPE-1025-GIE, treats  
21 accumulated CIAC amounts as increases to the depreciation reserve. Thus, CIAC is  
22 in the nature of additional book depreciation. When there is additional book  
23 depreciation with no corresponding tax depreciation, a timing difference is created.

1 Because, in this instance, there is a book deduction that is greater than the  
2 corresponding tax deduction, the effect of the timing difference is a reduction of  
3 deferred tax expense and thus a reduction of accumulated deferred income taxes, or  
4 the creation of a deferred tax asset. Under either view, the answer is the same; i.e.,  
5 the reduction of a deferred tax liability versus the creation of a deferred tax asset has  
6 the exact same effect on rate base.

7 **Q: If Mr. McClanahan ignores the deferred tax effects of CIAC and does not treat**  
8 **the gross-up as additional CIAC, what happens on KCPL's financial**  
9 **statements?**

10 A: As I have previously mentioned, KCPL needs to reflect the CIAC appropriately in its  
11 financial statements. On Exhibit RWH-1 I have portrayed the effects of the CIAC  
12 under the method proposed by Mr. McClanahan (termed KCC Staff) and under the  
13 method advanced by KCPL.

14 Under the KCC Staff method, there is an effective tax rate on CIAC of 100%. This is  
15 a result of not reflecting the gross-up for taxes as additional amortization expense and  
16 of not reflecting the deferred tax effects of the CIAC. In order to force the numbers  
17 to work under the KCC Staff method, the tax effect of the original amortization  
18 expense would be flowed through and treated as a permanent item. The results of this  
19 methodology would skew the income tax expense amounts in the financial statements  
20 and be misleading.

21 The KCPL methodology more accurately reflects the CIAC and tax gross-up and will  
22 not distort taxes in the financial statements.

1 **Q: Should Mr. McClanahan object to the KCPL method of reflecting the CIAC and**  
2 **gross-up?**

3 A: I do not believe so. I think Mr. McClanahan has a concern that the KCPL accounting  
4 may result in a different revenue requirement now or in the future. But it does not.  
5 Revenues, operating expenses and rate base, I believe, would be the same under either  
6 methodology. KCPL is merely trying to avoid showing a higher effective tax rate  
7 than should be shown.

8 **Q: Mr. Hriszko, does this conclude your testimony?**

9 A: Yes, it does.

**Kansas City Power & Light Co.  
Docket No. 06-KCPE-828-rts**

Income Statement Example

	<u>KCC Staff</u>	<u>KCPL</u>
Revenue	5,000,000	5,000,000
Amortization Expense	<u>(3,250,000)</u>	<u>(5,000,000)</u>
Book Income Before Tax	<u>1,750,000</u>	<u>0</u>
Current Tax Expense	1,750,000	1,750,000
Deferred Tax Expense	0	(1,750,000)
Total Tax Expense	<u>1,750,000</u>	<u>0</u>
Book Income After Tax	<u>0</u>	<u>0</u>
Effective Tax Rate	100%	0%
 Rate Reconciliation		
Book Income Before Tax	1,750,000	0
Statutory Rate	35%	35%
Taxes @ Statutory Rate	612,500	0
Flow through of Amortization Expense (3,250,000 x 35%)	1,137,500	0
Total Tax Expense as Reported	<u>1,750,000</u>	<u>0</u>
 <u>Rate Base Impact</u>		
Reserve for Amortization	(3,250,000)	(5,000,000)
Deferred Tax (Liability)/Asset	0	1,750,000
Net Future Effect on Rate Base	<u>(3,250,000)</u>	<u>(3,250,000)</u>

