

Rocky Mountain Power
Docket No. 10-035-124
Witness: Erich D. Wilson

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF UTAH

ROCKY MOUNTAIN POWER

Rebuttal Testimony of Erich D. Wilson

Labor and Benefits

June 2011

1 **Q. Are you the same Erich D. Wilson who submitted direct testimony in this**
2 **proceeding?**

3 A. Yes.

4 **Q. What is the purpose of your rebuttal testimony?**

5 A. The purpose of my rebuttal testimony is to explain why the Commission should
6 reject certain labor related adjustments proposed by the Division of Public
7 Utilities witness Mr. Mark E. Garrett, Utah Association of Energy Users
8 Intervention Group witness Mr. Kevin C. Higgins and the Office of Consumer
9 Services witness Ms. Donna Ramas. Specifically, I address:

- 10 • The proposed removal, or adjustment, of incentive expense would result in
11 below-market compensation.
- 12 • The Company's base wage expense is reasonable and consistent with the
13 competitive market in which the Company competes for labor throughout its
14 service territory.
- 15 • The Company continues to closely manage its workforce and allocates the
16 resources prudently. The Company's incentive program is not a "bonus." It is
17 an integral part of each employee's market-based compensation package and
18 is based on the employee's satisfactory achievement of individual goals. Each
19 employee's goals associated with the incentive portion of compensation are
20 related to factors other than the Company's revenues and net income. The
21 achievement of the goals provides benefits or avoids costs to customers
22 consistent with Commission precedent.
- 23 • The company measures productivity through various efforts such as

24 equivalent availability, customer service standards and surveys, safety and
25 reliability to point to a few of the many. These measures have been trending
26 positively since 2006 and linking to and disallowing salary and benefit
27 expense is neither reasonable nor a prudent approach.

- 28 • The medical benefits expense in this filing is forecasted consistently with the
29 approach the Company has taken historically and has been accepted by this
30 commission. The Company continues to manage and adjust the plan design
31 and cost sharing to remain market competitive. The trend rates for our
32 industry remain in the 8-10 percent range given the demographics of the
33 workforce and the nature of the work performed in support of our customers.

34 **Compensation Philosophy and Background**

35 **Q. Please briefly review the Company's compensation philosophy.**

36 A. As I explained in my direct testimony, the Company's primary objective in
37 establishing employee compensation is to provide total compensation (salary and
38 incentive) at the market average. Compensation at the market average
39 (competitive level) is critical to attracting and retaining qualified employees
40 necessary to support our customers' needs.

41 I also explained in my direct testimony that the Company's belief that, in
42 order to encourage superior performance a certain percentage of each employee's
43 market compensation must be "at risk." The Company's Annual Incentive Plan is
44 structured so that each employee has the opportunity to receive total
45 compensation at the market average, so long as the employee performs at an
46 acceptable level. In exceptional performance years, an employee's incentive may

47 be more than target and in low performance years may be below target, but on
48 average, the incentive is generally at the guideline level. If the individual fails to
49 earn the full guideline incentive, that individual will be paid less than the
50 competitive total cash compensation in the marketplace for that year. Central to
51 the Company's approach to total compensation is that, while certain employees
52 may be paid more than or less than market in a given year as a result of the
53 incentive portion of compensation, on an overall basis the base compensation and
54 incentive will result in a level of compensation commensurate with the market.
55 Stated another way, in the unlikely event every employee performed at exactly the
56 same level, each employee would be paid only at the market average.

57 **Q. Has the Company's general compensation philosophy and approach changed**
58 **in any material way in the last five years?**

59 A. No. Since MidAmerican Energy Holdings Company (MEHC) acquired
60 PacifiCorp in 2006, PacifiCorp's compensation philosophy has not changed. The
61 Company only seeks recovery for compensation at the market level, consistent
62 with this Commission's prior orders.

63 **Incentive Compensation**

64 **Q. Is a compensation structure that includes an incentive element to reach**
65 **competitive pay levels consistent with Commission policy?**

66 A. Yes. The Company's level and structure of compensation reflect the market and
67 an overall level of pay that is at the market average. The Commission has
68 previously ruled in Docket No. 07-035-93 that "we are persuaded the total
69 compensation, including both base pay and incentive compensation, is reasonably

70 targeted to the market average of total compensation.” (order at 62) Because the
71 Company’s compensation structure has not changed, and remains reasonable, we
72 again ask the Commission to approve it.

73 **Q. Please describe Mr. Garrett’s proposed adjustment to the incentive portion**
74 **of PacifiCorp’s total compensation package.**

75 A. Mr. Garrett proposes to adjust the Company filing to actual incentive paid and
76 limits this to the average of the actual payments made for the period of 2008
77 through 2010. This would result in incentive compensation of \$28,842,195 and a
78 reduction of \$1,414,163 on a Utah allocated basis.

79 Mr. Garrett supports his position by unfairly viewing the incentive plan as
80 based solely on the discretion of senior management, to apply criteria he alleges is
81 not clearly defined.

82 **Q. Do you agree with Mr. Garrett’s perceptions of the incentive plan award**
83 **determination?**

84 A. No. I do not agree with Mr. Garrett’s view of the incentive plan award
85 determination.

86 My disagreement with his view that the plan is solely discretionary and
87 unclear comes from knowing how the plan actually operates. Not discretionarily
88 but rather more quantitatively, at the beginning of each year each employee, along
89 with their manager, assesses the direction and goals of the business/department
90 and set forth clear and defined goals that the employee will be measured on.
91 These goals and the performance against them, frame the decision and incentive
92 award allocation made by the manager. It is clearly defined.

93 **Q. Do you agree in concept with Mr. Garrett's proposed adjustment using the**
94 **average of actual incentives paid during the test year?**

95 A. Yes. As I've stated, in appreciation of the recent economic challenges all parties
96 have faced, and also in recognition that the actual incentive award payments made
97 by the Company to its employee's have been set with these challenges in mind, I
98 would support the concept of an averaging for the amount of annual incentive
99 expense to be included in this case. I will explain the calculation on this average
100 further on in my testimony.

101 **Q. Please describe Ms. Ramas's proposed adjustment to the incentive portion of**
102 **PacifiCorp's total compensation package.**

103 A. Ms. Ramas proposes to adjust the Company filing to actual incentive paid and
104 limits this to the average of the actual payments made for the period of 2009
105 through 2010. In her proposal, she also proposes to escalate the result of the two
106 year average by the planned 2011 merit increase and 50 percent of the planned
107 2012 merit increase. This would result in incentive compensation of \$29,536,612
108 and a reduction in the filing of \$1,212,727 on a Utah allocated basis.

109 **Q. Do you agree with Ms. Ramas's proposed adjustment?**

110 A. Yes, with qualifications. Ms. Ramas is not disallowing incentive costs per se, but
111 rather attempting to adjust to a normalized level of incentive for rate making
112 purposes. Ms. Ramas elects to use two years (2009 and 2010) as her variables,
113 which were the two lowest years relative to budget. More importantly, the two
114 most recent years she uses reflect significant economic challenges.

115 The concept of averaging of certain expenses that tend to fluctuate from

116 year to year is an acceptable approach in rate making for some situations. While
117 only two data points (2009 and 2010) is insufficient for a proper average, the
118 Company is willing to support a three year historical average calculated by
119 comparing the actual AIP payout rate as compared to payroll (regular time,
120 overtime, and premium pay) for years 2008 to 2010, multiplied by June 2012 test
121 period wages. This adjustment would result in an average expense of \$30,078,000
122 on a total Company basis. Company witness Mr. Steve R. McDougal has
123 included the impact of adjusting incentive compensation to the three-year average
124 level in Exhibit RMP____(SRM-2R). The Company's proposal reduces revenue
125 requirement by approximately \$2,698,184 on a total Company basis, or
126 \$1,130,603 on a Utah allocated basis.

127 **Base Wages**

128 **Q. Please describe Mr. Garrett's proposed adjustment to the base wage portion**
129 **of PacifiCorp's total compensation package.**

130 A. Mr. Garrett approaches wages under the header of payroll and related expenses.
131 Mr. Garrett's position is that the Company has only considered a single element
132 of payroll costs in its proposed payroll adjustment (pay increases). He goes on to
133 state that the Company has failed to consider an adjustment for the levels of
134 productivity improvements that should also be attained during this same
135 performance period. He takes the position that productivity gains should offset
136 payroll increases with a simple average of 1.5 percent per year. Therefore, his
137 adjustment reduces payroll expenses by \$9,556,113 on a total Company basis and
138 \$3,822,820 on a Utah allocated basis.

139 **Q. Do you agree with Mr. Garrett's proposed adjustment to use a nine year**
140 **average for payroll expense?**

141 A. No. First and most importantly, Mr. Garrett does not disagree with the levels of
142 market competitive merit levels the Company has included in this filing.
143 However, his assessment and recommendation that productivity should offset or
144 neutralize the merit increases provided to employees for their performance is
145 unreasonable and not a competitive practice. Improved employee performance,
146 and the reward and recognition for that performance, are fundamental to any
147 company being successful. Reducing the payroll expense based on a perceived
148 statistical value is a disincentive and results in less than market compensation.

149 Along with the performance of our employees, we have implemented
150 technological changes and most importantly sound management and business
151 practices which are the key overall drivers to productivity advancement.
152 Therefore, I don't support in any way an adjustment to our filed wage expense
153 under the argument of productivity offset.

154 **Q. In Mr. Garrett's testimony, he presents what he claims is a corrected version**
155 **of the labor costs per kWh table from my direct testimony with the actual**
156 **June 2010 wage and benefit cost substituted for the prior rate case**
157 **projection. Does his table present an accurate representation of June 2010**
158 **labor costs per MWh?**

159 A. No. Mr. Garrett updates the table with actual wage and benefit expense from the
160 12 months ended June 2010, but he fails to update the table with total Company
161 load from that same time period. Below I show a correct version of Mr. Garrett's

162 table with total Company load from the 12 months ending June 2010. The
163 corrected table shows that projected labor costs as filed for the test period are
164 slightly lower on a cost per MWh than during the June 2010 period. With the
165 labor related adjustments the Company is including in our rebuttal filing, the
166 comparison would show a larger reduction in cost per MWh.

	12 Months Ending June 2012	12 Months Ending June 2010	Change
Wage & Benefit Expense	\$520,029,165	\$485,175,759	7.2%
Total Load - MWH	61,585,034	57,390,884	7.3%
\$/MWH	\$8.44	\$8.45	-0.1%

167 **Q. Please describe Mr. Higgins’s proposed adjustment to the wage and benefit**
168 **portion of PacifiCorp’s total compensation package.**

169 A. Mr. Higgins proposes to remove a portion of the wage and benefit compensation
170 package, resulting in an overall \$8.5 million disallowance. Mr. Higgins argues
171 that the Company’s proposed wage and benefit expense is 7.2 percent greater than
172 the actual expense for the 12 months ending June 2010. He conveys the increases
173 in expense are based on pension (\$10.3 million) and medical benefits (\$5.8
174 million). He also refers to an increase in the annual incentive plan of 7.1 million
175 and regular wage expense increasing by 16.4 million.

176 **Q. Do you agree with Mr. Higgins’s proposed adjustment?**

177 A. No. Mr. Higgins inappropriately groups a variety of items. He does not
178 demonstrate why any of the costs are unreasonable, and he uses two arguments in
179 support of his position which are neither applicable nor valid to Utah customers.

180 The first argument he makes suggests that the Commission follow a recent
181 order of the Idaho commission wherein that commission refused to recognize the
182 Company's actual compensation expense. The Idaho commission referenced its
183 belief that the Idaho economy was somehow worse than the economy elsewhere
184 in the states where the Company has employees. The Company strongly disagrees
185 with the rationale of the Idaho commission and notes that, even if the Idaho
186 commission were correct, the same situation does not exist in Utah. According to
187 the Utah Department of Workforce Services, the Utah unemployment was 7.3
188 percent in May 2011 as compared to a national average of 9.1 percent.

189 One of the impacts of the recent recession was that wage increases have
190 been very modest. Compared to the past couple of decades, wage increases over
191 the last couple of years were markedly lower. In 2010, Rocky Mountain Power's
192 total wages actually increased only 0.4 percent versus 2009, as wage increases
193 were limited because certain goals were not met. In contrast the Utah Economic
194 Summary reports that the average wage increase in 2010 among all employers in
195 Utah was 1.6 percent. With the cost of living trending upward, it is expected that
196 wages will rise more than was the case during the recession. IHS Global Insights,
197 a global information company, projects Utah wages will increase 2.8 percent in
198 2011.¹ The wage increase at Rocky Mountain Power that is part of this rate
199 request is equivalent to 1.8 percent annually.

200 Additionally as I have shown, our compensation philosophy is to provide
201 compensation at the market average. The 2010 wage increases for non-

¹ Total Non-farm Average Annual Wage, Utah, IHS Global Insight, States, Core Data, released June 14, 2011

202 represented employees were based on a detailed market analysis of the actions
203 being taken in the labor market. From this assessment, and also factoring in the
204 economic climate and conditions facing our customers, the Company
205 implemented 2010 wage increases slightly below market practices. Further, only
206 those employees who received a base compensation below \$100,000 were eligible
207 for an increase. For 2011, the Company continued with its practice of assessing
208 the labor market and provided the opportunity for a 1.96 percent wage adjustment
209 that was effective December 26, 2010, for the 2011 performance period.

210 **Q. Does Mr. Higgins's proposed adjustment take into account present and**
211 **future circumstances?**

212 A. No. Mr. Higgins understates the future. He suggests wages and employee benefit
213 costs might only rise 0.75 percent in 2011. This perspective is not supported by
214 actual wage increases required by union labor contracts in 2011 or by the
215 informed projections of human resource experts. We have carefully managed to
216 control expenses during the recession and continuously strive on a regular basis to
217 make improvements. But, wages and employee benefit expenses are now
218 expected to rise at a faster rate than was experienced during the recession. Mr.
219 Higgins suggests that because wage and benefit increases over the past couple of
220 recession years have been modest, the 2011 increase should be the same.
221 Increases to wages and benefits will be modest, but there are solid reasons these
222 expenses will increase more than the level suggested by Mr. Higgins. Those
223 reasons include the following.

224 • The contract with IBEW Local 57, which represents many of the

- 225 Company's employees in Utah, will raise wages by 1.75 percent this year.
- 226 • The actual wage increase for non-union employees in January 2011 was
- 227 1.96 percent.
- 228 • Health care costs at Rocky Mountain Power are expected to increase
- 229 approximately 8 percent in 2011 and 2012, which is very favorable
- 230 compared to the level of increase many other employers anticipate.
- 231 • Pension related expenses, are now anticipated to increase at an annualized
- 232 rate of 3.8 percent during the test period, largely due to recent program
- 233 changes.

234 The second argument Mr. Higgins makes is focused on the challenging

235 economic times and that "utilities should not be exempt from the belt-tightening

236 that its customers must endure during challenging economic circumstances." As I

237 have testified, the Company has reduced and in some cases eliminated wage

238 increases and, in fact, is in danger of not having compensation at market levels.

239 The market levels already reflect the impact of the general reduction in

240 compensation growth and further reducing the market data would double-count

241 the impact of the recession.

242 **Q. Why do you recommend the Commission reject Mr. Higgins' flawed**

243 **assumptions?**

244 The Company firmly believes that the prudent approach to compensation

245 is to apply a consistent philosophy based on total compensation market data in

246 both good and bad economic times. The Company does not include an adder

247 above market survey data when economic conditions are positive and no

248 subcontractor should be included when economic times are less favorable.

249 Mr. Higgins' approach of taking a performance period of 2010 and
250 adjusting by a set percentage without considering the actual data and results that
251 are evident in the market, is neither fair nor reasonable for either the customer or
252 the Company's employees. I therefore encourage the Commission to reject the
253 proposed adjustments brought forth by Mr. Higgins on behalf of UAE.

254 **Q. Please describe Ms. Ramas's proposed adjustment to the wage and benefit**
255 **portion of PacifiCorp's total compensation package.**

256 A. Ms. Ramas proposes a negative 1.27 percent be applied to the Company's filing
257 of regular, overtime and premium pay. Ms. Ramas cites that this reduction is
258 appropriate and addresses an over projection as the Company has not accounted
259 for the actual FTE's in the base year and subsequent period. This adjustment
260 reduces the filing by \$4,342,863 on a total Company basis and \$1,818,516 on a
261 Utah allocated basis.

262 **Q. Do you agree with Ms. Ramas's proposed adjustment?**

263 A. Yes, with qualifications. Ms. Ramas correctly points out that there has been an
264 adjustment in FTE's over the last few years. This change in FTE levels was
265 neither planned nor is it a level that is expected to continue as the Company
266 moves forward. A key element of this discussion point not raised by Ms. Ramas
267 in her testimony is that at the same time these changes were occurring, the
268 Company was similarly recruiting for these open positions and also moving
269 forward with adding apprentices during this period to support customer needs.
270 Although we have seen signs of improvement in the economy, it is still very

271 unstable and therefore difficult to truly convey confidence that the Company will
272 be able to fill all its open positions without seeing a degree of offset in
273 terminations. Therefore, for this filing only, the Company accepts the proposed
274 FTE adjustment made by Ms. Ramas and the related adjustment to the filing. The
275 Company has recalculated Ms. Ramas adjustment to also remove the associated
276 payroll tax as shown in Exhibit RMP____(SRM-2R), Adjustment 12.8. The
277 Company's proposed adjustment reduces test period wages by \$4,648,102 on a
278 total Company basis and \$1,947,665 on a Utah allocated basis.

279 **Health and Welfare (Benefits) Background**

280 **Q. Please briefly review the Company's approach to providing health and**
281 **welfare benefits to its employees.**

282 A. The primary objective in establishing employee health and welfare benefits is to
283 provide a total benefits package at the market average. Benefits provided at the
284 market average (competitive level) is critical to attracting and retaining qualified
285 employees to support the business and our customers.

286 **Q. Please describe Mr. Garrett's proposed adjustment to the medical expense**
287 **included in this filing.**

288 A. Mr. Garrett argues that a study he has reviewed, provided by the consulting firm
289 of Towers Watson, projects health care cost for U.S employers will increase an
290 average of 6.34 percent in 2011. He also notes in his testimony that this Towers
291 Watson report takes the position that health care cost have reached a plateau
292 ranging from 6-7 percent. Based upon this source of general information, Mr.
293 Garrett proposes to average the results of the Towers Watson general data with

294 the companies plan and industry data as provided by Aon Hewitt to derive a
295 resulting reduction in medical expense of \$473,789 on a total Company basis and
296 \$198,393 on a Utah allocated basis.

297 **Q. Do you agree with Mr. Garrett's proposed adjustment?**

298 A. No. The demographics of our industry and more specifically our employee
299 workforce do not lend itself to comparing across general data results. The
300 information and consultation from Aon Hewitt on our medical cost trend is
301 derived by a comprehensive assessment of our plan design, workforce and most
302 importantly, our claims experience. For example, the first quarter 2011 is showing
303 a trend of 16 percent and is due in part to a large number of high cost claims
304 brought forth year to date (ex. cancer claims).

305 While I accept that the Towers Watson source is a credible resource, for
306 trending purposes it does not account for the specifics of our workforce and is not
307 a comprehensive result thereby providing confidence in using for decision
308 making. Therefore, I recommend that the commission not accept Mr. Garrett's
309 proposed adjustment to average two different data sources.

310 **Q. Are there any adjustments the Company deems appropriate?**

311 A. Yes. The Company has included adjustments to test period labor costs in its
312 rebuttal filing that address the specific issues raised by DPU witness Mr. Garrett
313 and OCS witness Ms. Ramas. These adjustments are more fully addressed by Mr.
314 Steve McDougal. In addition, the Company has replaced its original estimates of
315 2011 expense for pension and post retirement related costs to reflect the most
316 recent actuarial studies available (which will determine the actual 2011 expense).

317 The Company's adjustments reduce test period labor expenses by approximately
318 \$6.1 million on a Utah allocated basis. With these adjustments included in the
319 Company's rebuttal case, further adjustment to total compensation or benefits are
320 unwarranted and should not be accepted by this Commission.

321 **Q. Does this conclude your rebuttal testimony?**

322 A. Yes.