DIRECT TESTIMONY

OF

SUSETTE N. CASSIDY

MISSOURI PIPELINE COMPANY

CASE NO. GR-92-314

Q. Please state your name and business address.

A. Susette N. Cassidy, Suite 330, 906 Olive Street, St. Louis, Missouri 63101.

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

A. I am employed by the Missouri Public Service Commission (Commission) as a Regulatory Auditor.

Q. Please describe your educational background.

A. I graduated from Central Missouri State University in May, 1990, with a Bachelor of Science degree in Business Administration, with a functional major in Accounting.

Q. What has been the nature of your duties while in the employ of this Commission?

A. I have, under the direction of the Manager of Accounting, assisted with audits and examination of books and records of utility companies operating within the state of Missouri.

Q. Have you previously filed any testimony before the Commission?

A. Yes, I have filed testimony in Case No. EM-91-213, Kansas Power and Light Company; Case No. GR-91-291, Kansas Power and Light Company; and Case Nos. WR-92-207 and SR-92-208, Missouri Cities Water Company.

Q. With reference to Case No. GR-92-314, have you made an examination of the books and records of Missouri Pipeline Company (MPC or Company)?

A. Yes, with the assistance of other members of the Commission Staff (Staff).

Q. Please describe your principal areas of responsibility in this case.

A. My principal areas of responsibility are payroll and payroll taxes, payroll related cash working capital (CWC) lags, insurance and benefits/awards. I am also sponsoring Accounting Schedule 10, Income Statement and Accounting Schedule 11, Income Statement Adjustments.

Q. What Accounting adjustments are you sponsoring?

A. I am sponsoring Income Statement adjustments S-3-A, S-3-D, S-3-E, S-3-F, S-3-G, S-4-A, S-4-B, S-4-C, S-4-J, S-4-K, S-4-N, S-4-O and S-6-A. I will also be sponsoring an adjustment to Accounting Schedule 4, Adjustments to Plant in Service. This adjustment will disallow previously capitalized dollars associated with Incentive Compensation awards. The Staff is waiting for information from the Company in order to quantify this adjustment.

Q. Please describe the Accounting Schedules you are sponsoring.

A. Accounting Schedule 10 is the Income Statement. It contains the Company's per book amounts as of March 31, 1992 and the Staff's adjustments to those amounts. Accounting Schedule 11 presents the Staff's detailed adjustments to the Income Statement.

PAYROLL

Q. Please explain Adjustments S-3-A and S-4-A.

A. Adjustments S-3-A and S-4-A reflect the annualized level of payroll to be retained by the Company.

Q. Please describe how the Staff annualized payroll.

A. I utilized pay rates and employee levels as of the end of the Staff's update period of September 30, 1992. These amounts were used to calculate a full year of payroll expense at the current level. Additionally, I included in my payroll annualization all known changes in employee numbers that we became aware of during our fieldwork at MPC's Tulsa, Oklahoma offices. These changes are very significant to the Staff's ongoing payroll annualization because the Company is currently downsizing after completion of a construction project. This downsizing involves eliminating the positions of MPC's President, Vice President of Engineering and Operations and the Office Administrator. The Staff then applied a factor to the payroll amount to determine the amount appropriately allocable to MPC. The Staff distributed that annualized payroll total to the Transmission function and the Administrative and General (A&G) function as dictated by departmental codes.

Q. How did the Staff obtain the percentage of payroll to be allocated to the Company?

A. The employees of MPC also perform work for other affiliated companies. The Staff conducted interviews with key employees of the Company to determine the amount of time the employees spent on MPC duties. The responses to Staff Data Requests Nos. 92 and 121 confirmed the percentages provided by the Company in those interviews.

Q. Is there a direct relationship between the time an employee spends on MPC business and the amount of payroll and payroll related expenses that should be allocated to the Company?

A. Yes. MPC customers should only be charged for time employees spend working on MPC business.

Q. How did the Staff calculate the payroll adjustments?

A. The Staff subtracted actual test year recorded expense from the annualized level of payroll as discussed earlier. Adjustment S-3-A adjusts payroll functionalized as Transmission and adjustment S-4-A adjusts A&G expenses.

PAYROLL TAXES

Q. Please explain adjustment S-6-A.

A. Adjustment S-6-A adjusts the Company's payroll tax expense consistent with its annualization of payroll.

Q. What specific payroll taxes did the Staff annualize?

A. The Staff annualized FICA (social security), Federal Unemployment Tax Act (FUTA) and State Unemployment Tax Act (SUTA) taxes separately.

Q. How did the Staff annualize these taxes?

A. The annualization is based on the tax rates and the taxable salary levels in effect at September 30, 1992.

Q. How was the adjustment determined?

A. The Staff compared the combined annualized amount for all three taxes to the book level of the combined expenses to arrive at the adjustment amount reflected on Accounting Schedule 11.

<u>INCENTIVE COMPENSATION</u>

Q. Please explain Adjustments S-3-D and S-4-J.

A. Adjustments S-3-D and S-4-J propose to disallow the expense of the Company's incentive compensation plan from the test year.

Q. What is MPC's incentive compensation plan?

A. It is an award which may be given to employees each quarter as determined by MPC's management.

Q. What assurance does the Staff have that the incentive compensation awards will be given in the future by MPC?

A. None. The awards are completely discretionary.

Q. How are the amounts of the awards, if any, determined to be distributed?

A. Recommendations for awards are made by the MPC department heads with final approval by the president of MPC and the president of MPC's parent company, ESCO Energy, Inc., (ESCO).

Q. How does this award system compare to the merit increases given on January 1 of each year?

A. Merit increases are actual raises in salary, and are related to a formal performance appraisal that is completed annually and discussed with each employee. The response to Staff Data Request No. 65 states that "the supervisor/manager will determine if a merit increase is warranted at the time of the performance review".

Comparatively, incentive compensation awards are a one time bonus approved and distributed completely at the Company departmental heads and the Presidents' discretion.

Q. What performance goals are expected by the employer for merit increases and incentive compensation awards?

A. For the merit increases, the response to Staff Data Request No. 65 states that "the purpose of the review will be to provide employees feedback on their performance. It will also offer an opportunity to discuss ways of improving job performance and to discuss and establish future employment goals."

Regarding the incentive compensation awards, Staff Data Request No. 75 asked for documentation showing the relationship between employee's performance and the amount of the award. The Company responded that there is "no written documentation available".

Q. What criteria must be met by the employee for the merit increases and the incentive compensation?

A. The response to Staff Data Request No. 65 states that, "It is ESCO's policy to reward employees with merit increases in salary for dedication in their work, extra effort and better-than-average performance."

There is no written documentation for any criteria or performance expectations to be met for the incentive compensation award, as referenced in the response to Staff Data Request No. 75.

Q. How can the incentive compensation award provide "incentives" to the employees?

A. The American Heritage Dictionary (Second College Edition) defines "incentive" as "something, as the fear of punishment or the expectation of reward, that incites to action or effort." The Staff questions how receiving an incentive compensation award without the employee having knowledge of the criteria for receiving it and without the existence of clearly defined goals to measure performance levels can provide any "incentive" on the employees part to perform better. In other words, the Staff believes that for ratemaking purposes there should be specifically defined and appropriate goals for performance which employees must fulfill in order to receive such an award to be eligible for rate recovery.

Q. Has the Commission previously recognized this approach as the appropriate criteria for rate recovery of incentive plan expense?

A. Yes. In the Report and Order from Case No. EC-87-114, Union Electric Company, the Commission stated that "At a minimum, an acceptable management performance plan should contain goals that improve existing performance, and the benefits of the plan should be ascertainable and reasonably related to the incentive plan."

Q. Is the Staff dictating to the Company how it should reward its employees?

A. The Staff is not expressing an opinion as to whether an incentive compensation award should or should not be given, but rather is recommending the proper level of ongoing expense to include for ratemaking purposes. It is the Staff's belief that a discretionary, one time award not related to clearly set and appropriate performance goals, is not reflective of a proper level of ongoing expense to include in the cost of service. Also, the dollar amounts of future awards, which may or may not be given, are not known and measurable at this time.

Q. Have any incentive compensation amounts been actually distributed in 1992?

A. Even though the Company has been accruing an expense for incentive compensation awards on their books, there have been <u>no</u> incentive compensation awards given thus far in 1992.

Q. Does the mere accrual of expense for the incentive compensation plan meet the Commission criteria for inclusion in cost of service?

A. No. In Case No. WR-89-246, St. Louis County Water Company , the Commission stated in regard to the "supplemental pension costs" issue that the "policy is to reject recovery of expenses in rates unless it is sufficiently certain that such expenses will actually be incurred".

Q. What adjustment is the Staff proposing for incentive compensation.

A. The Staff believes that the test year expenses associated with incentive compensation awards should be disallowed. These awards are not based on specific or definable goals of the Company. Also, the Company cannot document that any awards will be given in the future. Finally, no awards have been given thus far in 1992.

The Company capitalized a portion of the incentive compensation amounts it accrued in the test year. Once the Staff obtains certain additional information concerning the capitalized incentive compensation, the Staff will propose a Plant adjustment to remove these amounts from plant in service.

<u>401K MATCHING ADJUSTMENT</u>

Q. Please explain adjustments S-4-B and S-3-F.

A. Adjustments S-4-B and S-3-F adjusts the 401K Company matching portion to an annualized amount.

Q. Please explain what a 401K Plan is.

A. The Company's 401K Plan is included in Edisto Resources Corporation's profit sharing plan. This plan is a "defined contribution" plan, and the Company has no other retirement plans for its employees.

Q. Please describe how the Staff calculated its annualized amount for 401K matching.

A. The Staff utilized the Company employees' ongoing salary level, as previously discussed in my testimony, and multiplied it by the matching percentage the Company contributes to the employees 401K Plan, as provided in the Company's response to Staff Data Request No. 133. MPC matches employee 401K contributions up to a maximum of 6% of the employee's salary or $1,738.25 per employee, whichever is lower. I then multiplied the contribution amount by the percentage allocated to MPC,as discussed in my testimony on payroll expense, to arrive at the annualized 401K Plan matching contribution. I then split this adjustment between the Transmission account and Administrative and General (A&G) account as recorded on the Company's books.

ADDITIONAL COMPANY CONTRIBUTION TO THE 401K PLAN

Q. Please explain adjustments S-3-G and S-4-C.

A. Adjustments S-3-G and S-4-C disallow the test year expense associated with the additional company contribution to the 401K Plan.

Q. Is the Company required to contribute more than the matching portion to the employees' 401K plan?

A. No.

Q. Is there a Company policy for how much additional dollars to contribute?

A. No. The total amount contributed above the matching portion, if any, is entirely discretionary as determined by the Edisto's Board of Directors (BOD).

Q. Does employee performance affect the amount of the additional Company contribution?

A. No. The response to Staff Data Request No. 77 states that "there is no relationship between employees performance and the amount of the additional contribution."

Q. If the BOD determines that an additional contribution will be made, how do they decide how to distribute the monies?

A. The response to Staff Data Request No. 109 states that the primary factor to distribute the money is based on "individual's total compensation for the period covered".

Q. Does the Company have any support that additional contributions will be made in the future?

A. In response to the question in Staff Data Request No. 109, the Company states that "no support is available - continuation of additional contributions must be approved annually by the Board of Directors."

Q. Is the 1992 level of 401K contributions representative of ongoing levels?

A. No. The Staff has not been provided with any assurance that the additional contributions will continue. Therefore, the Staff cannot quantify any known and measurable ongoing levels of additional 401K contributions.

Q. Wouldn't the Company be creating a more positive and thus more productive environment among its employees by contributing additional dollars?

A. Since there is no assurance that there will be any additional contributions and since any dollars contributed are not related to employee performance, the Staff believes that there is no proven direct link to the 401K contributions and improving employee motivation. Furthermore, the Company has not provided the Staff with any direct benefits from such a practice to justify the additional costs.

RESTRICTED STOCK AWARDS

Q. Please explain Adjustment S-4-K.

A. Adjustment S-4-K disallows the Company's restricted stock award from test year expenses.

Q. What is the criteria for receiving this award?

A. The response to Staff Data Request No. 75 states that 50% of the award relates to continued employment and 50% relates to Company performance.

Q. Who received restricted stock awards during the test year?

A. Only the MPC President and Vice-President Engineering and Operations received this award. Both of these individuals will soon be leaving the employ of the

Company, and the response to Staff Data Request No. 123 states that the restricted stock awards for these employees will not be awarded to any other employees.

Q. What is the Staff's proposed adjustment?

A. The Staff believes that a 100% disallowance is proper given that this will not be an ongoing award, and is therefore not reflective of an ongoing expense level.

CONTRACT LABOR EXPENSE

Q. Please explain Adjustment S-3-E.

A. Adjustment S-3-E disallows test year expenses that relate to a nonrecurring labor contract.

Q. Please describe why this adjustment is necessary.

A. During the test year, an outside contractor for MPC was hired as a full time Company employee. That employee's salary was included in the Staff's payroll annualization. Therefore, the Staff must remove the test year contract expense incurred prior to his employment by MPC to avoid overstating the ongoing level of expenses.

INSURANCE

Q. Please explain Adjustment S-4-N.

A. Adjustment S-4-N disallows from test year expense certain insurance policies.

Q. Please describe what these insurance policies are.

A. They are additional policies covering the Company's executives. They include Additional Insurance for Executives, Additional Group Long-Term Disability Insurance, Additional Insurance for Executives and Executive Health Insurance. The response to Staff Data Request No. 124 revealed that the policies in question covered only the President of MPC.

Q. Why is the Staff disallowing these policies?

A. This executive is leaving the employ of the Company and the policies will no longer be carried by the Company. The response to Staff Data Request No. 124 confirms the planned cancellation of these policies.

<u>INSURANCE ANNUALIZATION</u>

Q. Please explain Adjustment S-4-O.

A. Adjustment S-4-O annualizes the ongoing insurance policies of MPC including Medical/Dental and Life, Accidental Death and Dismemberment (AD&D), and Long Term Disability (LTD).

Q. Describe how the annualization was calculated.

A. The Staff obtained the current monthly rates through the response to Staff Data Request No. 116. For the medical/dental policy, I multiplied the monthly rates by the number of current participants, and then by twelve for the yearly premium. For the life, AD&D and LTD policies, the Staff multiplied the current monthly rate by twelve to obtain the yearly premium of insurance expense.

CASH WORKING CAPITAL LAGS

Q. What expenses lags did you prepare for Accounting Schedule 8, Cash Working Capital (CWC)?

A. I prepared the following expense lags: base payroll, tax withholding, 401K-matching, FICA-employer portion, and unemployment taxes.

Q. Please explain the base payroll expense lag on line 1 of Accounting Schedule 8.

A. The expense lag for base payroll reflects the time lapse between the average date the Company's employees earn compensation and the date payment is made by the Company.

Q. Please explain the tax withholding lag on line 2 of Accounting Schedule 8.

A. The tax withholding expense lag is an extension of the base payroll lag. The average number of days from the payroll payment date to the statutory deposit date for taxes withheld is, in effect, added to the base payroll lag. The withholding lag on Accounting Schedule 8 is a combined/weighted lag consisting of the federal, Oklahoma (OK), and Missouri (MO) income tax withholding lags.

Q. Please explain the lag for 401K Plan-matching from line 3 of Accounting Schedule 8.

A. The 401K Plan-matching expense lag was calculated using the same service period as the base payroll. The dollar amount used was the average of the total dollar amount of contributions during the test year that the Company matched to the employees contribution. The payment date used was the date the wire transfer of funds was effected.

Q. Please explain how the lag for FICA-employer portion on line 8 of Accounting Schedule 8 was calculated.

A. The expense lag for FICA-employer portion also follows the base payroll lag. The payment date used was the date the FICA taxes are required to be paid to the appropriate authority.

Q. Please explain the lag for unemployment taxes from line 9 of Accounting Schedule 8.

A. The lag for unemployment taxes was calculated based on the requirement that deposits be made quarterly by the Company on the last day of the month following the end of the quarter for which the taxes are due. The unemployment tax lag on the CWC Schedule was weighted/combined consisting of the OK SUTA, MO SUTA and FUTA lag calculations.

Q. Does this conclude your direct testimony?

A. Yes, it does.

BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF MISSOURI

In the matter of Missouri Pipeline Company for authority to file tariffs increasing rates for gas transportation services to customers within its service area.	))))	Case No. GR-92-314

AFFIDAVIT OF SUSETTE N. CASSIDY

STATE OF MISSOURI)
) ss.
COUNTY OF COLE)

Susette N. Cassidy, of lawful age, on her oath states: that she has participated in the preparation of the foregoing Direct Testimony in question and answer form, consisting of 16 pages to be presented in the above case; that the answers in the foregoing Direct Testimony were given by her; that she has knowledge of the matters set forth in such answers; and that such matters are true and correct to the best of her knowledge and belief.

Susette N. Cassidy
SUSETTE N. CASSIDY

Subscribed and sworn to before me this 10th day of December, 1992

Wanda J. King
Notary Public

My Commission expires: 9/4/95

OFFICIAL NOTARY SEAL
WANDA J KING
Notary Public State of Missouri
COLE COUNTY
My Commission Expires SEP 04,1995