

Exhibit No.:
Issue: Corporate Allocations
Incentive Compensation,
Pension Tracker
Witness: Keith Majors
Sponsoring Party: MoPSC Staff
Type of Exhibit: Surrebuttal Testimony
Case No.: GR-2014-0007
Date Testimony Prepared: April 3, 2014

MISSOURI PUBLIC SERVICE COMMISSION

**REGULATORY REVIEW DIVISION
UTILITY SERVICES - AUDITING**

SURREBUTTAL TESTIMONY

OF

KEITH MAJORS

**MISSOURI GAS ENERGY
A Division of Laclede Gas Company**

CASE NO. GR-2014-0007

*Jefferson City, Missouri.
April 3, 2014*

**** Denotes Highly Confidential Information ****

NP

**TABLE OF CONTENTS OF
SURREBUTTAL TESTIMONY OF
KEITH MAJORS
MISSOURI GAS ENERGY
CASE NO. GR-2014-0007**

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15

CORPORATE ALLOCATIONS 1

CORPORATE ALLOCATIONS – INFLATION ADDER 3

CORPORATE ALLOCATIONS – SHARED SERVICES 5

CORPORATE ALLOCATIONS – RETAINED SAVINGS FROM THE ACQUISITION 9

INCENTIVE COMPENSATION 25

INCENTIVE COMPENSATION – MGE’S NEW REBUTTAL ADJUSTMENT..... 40

PENSIONS 41

ON-GOING LEVELS OF PENSION COSTS FOR CASE NO. GR-2014-0007..... 60

RECOMMENDATIONS FOR PENSION COSTS 63

Surrebuttal Testimony of
Keith Majors

1 case, Case No. GM-2013-0254 (“Acquisition Case”), inflated by the Consumer Price
2 Index (CPI). Staff recommends an ongoing level of \$5,087,099, which is the stipulated cap
3 from the Acquisition Case, the same ceiling established in the Southern Union Company
4 acquisition by ETE in Case No. GM-2011-0412 (“ETE Acquisition”). Both these amounts are
5 before transfers to capital accounts, what is referred to as an Operations & Maintenance
6 (O&M) factor.

7 MGE has also recommended a new adjustment in Witness Buck’s rebuttal testimony
8 requesting and additional \$800,000 for “shared services” for corporate costs Laclede Gas
9 wants to allocate to MGE’s operations. I will address both issues in this testimony.

10 Q. What were the results of Staff’s analysis of MGE’s pro-forma corporate
11 allocations from Laclede Group and Laclede Gas?

12 A. As discussed at length in Staff’s Direct Filed Cost of Service Report
13 (“Staff Report”), MGE’s corporate allocations from Laclede Group and Laclede Gas are
14 estimated to be approximately \$11 million. This amount far exceeds the stipulated cap of
15 \$5.0 million from the Acquisition Case and the test year ending April 30, 2013 allocation
16 from Southern Union/ETE of \$5.2 million.

17 In effect, because of the acquisition of MGE by Laclede Gas, MGE’s corporate
18 allocations will more than double from the amount charged in the test year. This is what Staff
19 refers to as a “merger detriment.” But for the acquisition of MGE by Laclede Gas, the
20 corporate costs from Southern Union/ETE allocated to MGE and subsequently paid by its
21 customers would be \$5.2 million, less any adjustments Staff typically recommends, such as
22 short-term and long-term incentive compensation.

1 The results of Staff’s analysis concluded that MGE’s pro-forma corporate allocations
2 far exceeded the stipulated cap from the Acquisition Case; therefore, Staff adjusted MGE’s
3 corporate allocations to reflect the stipulated cap, less the amount to be charged to capital and
4 below-the-line accounts. This resulted in an *increase* of \$47,150 to corporate allocation
5 expense because the normalized amount charged to O&M was more than the amount in the
6 test year.

7 Q. Please define what you mean by corporate allocations.

8 A. For purposes of this surrebuttal testimony and that of my direct and rebuttal
9 testimonies, corporate allocations are identified as those costs relating to the management
10 overhead functions for services provided by Southern Union prior to the acquisition by
11 Laclede Gas, and the services that will be provided by Laclede Gas and Laclede Group after
12 the acquisition of MGE by Laclede Gas. There are also other management costs that occur
13 locally at the MGE organizational level that are not included in corporate allocations. These
14 would be included in Staff’s payroll and benefits annualization adjustment.

15 **CORPORATE ALLOCATIONS – INFLATION ADDER**

16 Q. MGE Witness Buck identifies the Company’s adjustment to corporate
17 allocations on page 2 of his rebuttal testimony. What is your opinion of MGE’s use of the
18 CPI to account for inflation?

19 A. As explained in my rebuttal testimony, the CPI has no correlation to the types
20 of services—Laclede Gas refers to these services as “shared services” —that MGE’s former
21 owners (Southern Union/ETE) or current owner – Laclede Gas will allocate to MGE. The
22 vast majority, if not all, of the expenses allocated to MGE will consist of labor (wages, salary,
23 and benefits), directors and officers insurance, and external audit fees. The CPI, which

Surrebuttal Testimony of
Keith Majors

1 measures the changes in price of a “market basket” of consumer goods and services, is a poor
2 measure of the changes in the types of corporate allocation expenses allocated to MGE.

3 The CPI measures the change in prices of actual purchased goods and services over a
4 period of time. These goods and services are a broad range from food and beverages to
5 tobacco and smoking products and haircuts. The CPI has no correlation to MGE’s corporate
6 allocations and the Commission should reject its use for that purpose.

7 Q. On Page 3, Witness Buck references salary surveys information provided to
8 Staff. Did Staff review any salary surveys?

9 A. Yes. Staff routinely reviews salary surveys in the course of a utility rate case
10 to determine how the utility establishes and supports its wage and salary rates. They were
11 reviewed on MGE premises on or about January 13, 2014. MGE provided Staff access to the
12 following salary surveys:

- 13 • 2008 American Gas Association Compensation Survey – Watson Wyatt
14 Data Services
- 15 • 2008 Energy Compensation Survey Report – Hay Group
- 16 • 2008 US MTCS for the Energy Sector Survey Report – Mercer
- 17 • 2008 Energy Services Report – Compensation Data Bank Executive
18 Database – Towers Perrin
- 19 • 2008 Energy Services Report – Compensation Data Bank Middle
20 Management and Professional Database – Towers Perrin

21 Q. Did Staff have difficulties obtaining information on compensation from MGE?

22 A. Yes. Staff was allowed access to the above surveys on January 6, 2014, nearly
23 **4 months** after the initial data request was submitted to MGE. The above provided surveys
24 were in the possession of MGE since the 2009 MGE Rate Case but were provided to Staff
25 very late in its audit.

1 Even though these salary surveys were provided late in the audit work, they were of
2 limited value because they related to 2008 time frame. The information was over five years
3 old and could not be used to compare to salaries for 2014.

4 Q. Did MGE provide any more current market salary and wage data?

5 A. MGE provided access to select portions of the 2011, 2012 and 2013
6 American Gas Association Compensation Survey on March 11, 2014, **6 months** after Staff's
7 initial data request, and after Staff's direct filing, Staff's true-up filing, and after the rebuttal
8 filing in this case.

9 Q. Does the information in the salary surveys support the use of the CPI to inflate
10 corporate allocations, as Witness Buck suggests on page 3 of his rebuttal testimony?

11 A. No. The information in the salary surveys is of a completely different nature
12 and used for different purposes than the CPI. Salary surveys compare wage, salary, benefit,
13 and incentive compensation information from a select group of companies, most commonly
14 for peer utilities. While the surveys demonstrate that salaries and wages generally increase
15 over time, there is no correlation with the information in the CPI to justify its use to inflate
16 MGE's corporate allocations. MGE is attempting to justify its use of a broad economic
17 indicator of inflation by comparing it to narrowly defined salary surveys applicable to only the
18 utility industry, the majority of which are from 2008 data. MGE's use of the CPI to inflate the
19 corporate allocations therefore should be rejected.

20 **CORPORATE ALLOCATIONS – SHARED SERVICES**

21 Q. Did MGE propose a new adjustment for corporate allocation in its
22 rebuttal testimony?

Surrebuttal Testimony of
Keith Majors

1 A. Yes. On pages 4-6 of Witness Buck's rebuttal testimony, MGE proposed a
2 new adjustment based on an estimate of \$800,000 of estimated services that are now being
3 provided by Laclede Group and Laclede Gas. This is a new adjustment that was not in the
4 Company's direct filing or any subsequent update supported by testimony. To date, MGE has
5 not filed an update to its original case, nor did MGE file a true-up case. MGE's direct filed
6 rate case did not include this adjustment, and because MGE has not updated its cost of service
7 through Staff's update period through September 30, 2013 or Staff' true-up period of
8 December 31, 2013, MGE has no case that supports this adjustment.

9 Similar to this new adjustment, MGE has also proposed a new incentive compensation
10 adjustment discussed later in this testimony. Recommending new adjustments that are
11 completely different in methodology in the rebuttal phase of testimony is contrary to the
12 normal rate case process and should be rejected by the Commission.

13 Q. Is Laclede Gas/Laclede Group currently charging MGE any allocated costs?

14 A. No. In the response to Data Request No. 229, MGE provided the
15 following response:

16 3. As Staff is aware, our accounting systems are not merged
17 but will be in April of 2014. Until such time, there are one-
18 time entries on MGE's books allocating approximately
19 \$466,000 a month from Laclede to MGE, which
20 approximate the Cost Allocation numbers supported in the
21 Company's direct filing.

22 MGE's "one-time entries" equate to an annual expense of \$5,592,000 (\$5.6 million). This is
23 approximately the amount of the stipulated cap of corporate allocations inflated by the CPI, as
24 recommended by MGE in its direct filing.

25 It is important to note that the actual amount currently being recorded on MGE's
26 books and records is not currently being allocated or billed by Laclede Gas or Laclede Group.

Surrebuttal Testimony of
Keith Majors

1 Laclede Gas does not currently have the necessary allocation procedures in place to make any
2 of the allocation for shared services it may be providing to MGE; as such these costs are not
3 “known and measurable.” As Witness Buck notes on page 5 of his rebuttal testimony,
4 Laclede Gas currently has no allocation methodology in place to account for the services
5 Laclede Gas and Laclede Group is providing MGE. While actual goods and services are
6 presumably being provided by Laclede Gas and Laclede Group, no cost allocation to MGE is
7 being made, therefore no intercompany billing or payment for those goods and services is
8 being currently being made.

9 Because there are no allocations being made, Staff has not had an opportunity
10 to review the actual allocation procedures that will be used. According to MGE, allocation
11 to MGE will not occur until sometime during or after the 2nd quarter of the 2014 fiscal year,
12 well outside of the scope of the true-up of this case that ended December 31, 2013. The
13 proposed \$800,000 amount requested by MGE in this case is not a “known and measurable”
14 ratemaking adjustment.

15 Q. If Laclede Gas does not have allocation procedures in place to allocate costs
16 for shared services to MGE, what expenses is being charged to MGE for corporate costs?

17 A. Currently, MGE is reflecting allocation of costs that approximate costs from
18 the previous owner, Southern Union. The \$5.6 million being accrued on MGE’s books is
19 based upon the stipulated cap of corporate allocations in the Acquisition Case increased by the
20 CPI. This number was based on the amount of corporate allocations from Southern Union
21 determined by Staff and MGE in the 2009 MGE Rate Case, Case No. GR-2009-0355
22 (“2009 Rate Case”). The \$5.08 million was Staff’s recommended level of corporate
23 allocations in that case, which was adjusted for incentive compensation and other expenses

Surrebuttal Testimony of
Keith Majors

1 Staff determined were not appropriate for rate recovery. MGE agreed with these adjustments
2 and reflected them in the accounting schedules attached to Witness Noack's Surrebuttal
3 testimony in the 2009 Rate Case.

4 In terms of actual expenses, MGE's accrual of \$5.6 million does not represent any
5 actual corporate allocations or billings to MGE and is based on Southern Union/ETE expenses
6 which no longer exist. These expenses are unrelated to the future corporate allocations from
7 Laclede Gas and Laclede Group to MGE.

8 Q. Can you explain the difference between the services provided by MGE's
9 local management and the services provided by its former corporate parents, Southern Union
10 and ETE?

11 A. MGE's local management was comprised of employees who oversaw the day
12 to day operations of providing natural gas service in the Company's service area. These
13 employees were located at MGE's headquarters in Kansas City and consisted of a Chief
14 Operating Officer, Vice President of Human Resources, and Vice President – Controller.
15 These were MGE employees and not part of the allocation of corporate costs from Southern
16 Union. Their costs were included on MGE's books as direct charged costs for administrative
17 and general ("A&G") costs and in prior rate cases were included in Staff's payroll and benefit
18 annualizations.

19 The corporate division of Southern Union/ETE provided MGE with services from
20 its finance, financial reporting, corporate governance, risk management, human resources,
21 legal, and environmental compliance departments, most of which were located in Texas. The
22 \$5.08 million of corporate allocations in the 2009 Rate Case was comprised of these expenses.

1 Q. Are MGE's local management personnel still functioning in management
2 capacity?

3 A. No. The Chief Operating Officer, Vice President of Human Resources, and
4 Vice President – Controller along with other personnel were released from MGE employment
5 the first day of the acquisition by Laclede Gas. These individuals are referred to as the
6 “Day 1” former employees.

7 Q. If no costs are being allocated from Laclede Gas or Laclede Group to MGE,
8 then is there any support for MGE's \$800,000 shared services adjustment?

9 A. No. The \$800,000 is an arbitrary amount that is unsupported by actual
10 expenses. It is an unauditable adjustment for which there is no basis.

11 Q. Is MGE's \$800,000 adjustment based on a “known and measurable” expense?

12 A. No. The “known and measurable” standard dictates that expenses included in
13 the cost of service are both known (a high degree of certainty that the expense will be incurred
14 by the utility), and measurable (a high degree of accuracy in measuring the expense). MGE's
15 proposed adjustment fails both of these standards. The \$800,000 amount requested by Laclede
16 Gas for shared services do not meet the standard of known and measurable costs.

17 **CORPORATE ALLOCATIONS – RETAINED SAVINGS FROM THE ACQUISITION**

18 Q. Can you provide an overview of the savings the Company can retain?

19 A. Yes. There are several categories of savings, both related to the acquisition of
20 MGE, and from the effect of positive regulatory lag. I will discuss each one:

- 21 1. The savings related to recent employee reductions, both the Day 1
22 employees and any other employees terminated through December 31,
23 2013;
- 24 2. Any other employee reductions after December 31, 2013;

Surrebuttal Testimony of
Keith Majors

- 1 3. The employee reductions between the 2009 Rate Case and the current rate
2 case;
- 3 4. The amount of corporate allocations currently in rates from the 2009 Rate
4 Case being paid by customers;
- 5 5. The difference between the greater corporate allocation to Laclede Gas
6 before the acquisition and the reduction after the acquisition;
- 7 6. The difference between the employee salary, wage, and benefit expense
8 built into rates and the reduction of that expense through ** _____
9 _____ **; and
- 10 7. Other savings related to the acquisition of MGE and the continued merger
11 of Laclede Gas and MGE operations.

12 Q. For Category 1 above, what savings has MGE realized from employee
13 reductions related to the acquisition through December 31, 2013?

14 A. Several former senior management employees, what MGE refers to as “Day 1”
15 employees, terminated their employment on or about the time of the acquisition on
16 September 1, 2013. These employees provided management at the MGE headquarters in
17 Kansas City; they were not Southern Union/ETE employees.

18 The terminated employees’ salaries, wages, and benefits total an annual expense of
19 approximately \$1.6 million. From the time of the acquisition, September 1, 2013, through the
20 effective date of new rates in this case, expected August 13, 2014, MGE will have retained
21 nearly a year of savings from the Day 1 employee reductions through regulatory lag. These
22 employee costs are currently being collected from existing rates. As such, while MGE is
23 collecting the salaries for released employees from its customers, the Company is not paying
24 for the services of these individuals. This represents a direct savings to the benefit of MGE.

Surrebuttal Testimony of
Keith Majors

1 MGE's new "shared services" adjustment not only ignores the \$1.6 million of savings
2 retained by MGE, but also asks its customers to pay an additional \$800,000 for services which
3 are neither being actually allocated to or actually being paid by MGE.

4 Q. What other savings will MGE retain from employee reductions through
5 December 31?

6 A. From July 2013 through September 30, 2013, MGE reduced its headcount by
7 an additional eight employees and from October 1 through December 31, MGE further
8 reduced its headcount by an additional five employees. From the time these employees ended
9 employment through the time the reductions are reflected in rates, MGE will retain the related
10 salaries, wages, and benefits. Below is a table summarizing the salaries, wages, and benefits
11 MGE will retain through regulatory lag through the effective date of rates in this case:

Employees	Salary & Wages	Benefits	Total Annual Savings
Day 1 Employees	1,029,557	567,286	1,596,843
Reductions July - September 30, 2013	456,170	251,349	707,519
Reductions October 1- December 31, 2013	308,032	169,726	477,757
Total Savings	\$ 1,793,759	\$ 988,361	\$ 2,782,120

13
14 Q. Did MGE reflect these savings in its filed rate case?

15 A. No. To date, MGE has filed only its direct case, filed on September 16, 2013,
16 which included payroll expense at July 20, 2013. MGE's payroll includes the Day 1
17 employees, as well as all other employee reductions through December 31, 2013.

18 MGE specifically did not recommend a true-up for the current rate case in the Direct
19 Testimony of Witness Noack:

1 **Q. IS MGE REQUESTING A “TRUE-UP” PROCESS?**

2
3 **A.** No. At this time, MGE believes that its recommended
4 update of costs, revenues and rate base through September 30,
5 2013 should be sufficient to establish a reasonable and
6 representative cost of service. I should note, however, that as this
7 proceeding unfolds there may be a need to revisit this issue
8 depending on the positions taken by other parties. There also may
9 be a need to consider certain additional changes in accounting
10 practices, orders or procedures or in tariff modifications to reflect
11 operational changes as the integration process proceeds.

12
13 [Noack Direct Testimony, Case No. GR-2014-0007, page 4]

14 Conversely, Staff filed both an updated case capturing increases and decreases in expenses
15 through September 30, 2013, and a true-up case capturing increases and decreases in expenses
16 through December 31, 2013. Staff reflected the actual MGE employee headcounts at both
17 cutoff dates, including the employee reductions.

18 MGE filed its case on September 16, 2013 but only recommended an update period of
19 September 30, 2013. This approach is completely contrary to what utilities typically request.
20 Most companies request an update several months past the actual filing date and several more
21 months for the true-up period. In this case, MGE departed from its usual position to reduce
22 regulatory lag as much as possible.

23 **Q.** What is regulatory lag?

24 **A.** Regulatory lag is the concept in ratemaking relating to the time it takes to
25 reflect in rates the actual impacts of utility operating events. It is necessary for the
26 Commission to have ample time to review the rate case material presented to support
27 recommendations by the parties in the regulatory process. It takes time to implement the
28 decisions of the Commission. Consequently, in order to use actual information to support
29 known and measurable precepts, the parties attempt to use information as close to the time

1 rates go into effect. It is critical to narrow the gap as much as possible between when actual
2 events occur and when those occurrences are recognized in rates.

3 In this case, because costs are declining, MGE has no interest in using the most current
4 costs to develop new rates. Thus, the reason why MGE recommended using the month in
5 which it filed its case as the cut-off-- September 30, 2013. This is inconsistent with how
6 MGE treated regulatory lag in the past.

7 Q. Has MGE in prior rate cases asked for a true-up early in the rate case process?

8 A. Yes. Witness Noack's testimony in the current rate case is completely contrary
9 and opposite to Witness Noack's testimony in MGE's rate cases in 2004, 2006, and 2009 rate
10 cases. MGE not only requested a true-up in direct testimony in each of those cases, but also
11 filed updated direct testimony and updated revenue requirement schedules.

12 Witness Noack's Updated Direct Testimony in Case No. GR-2009-0355 provided a
13 good description of why the true-up process is used to capture the most current expenses:

14 **Q. DOES MGE CONTINUE TO BELIEVE THAT A**
15 **TRUE-UP AUDIT IS NECESSARY AND APPROPRIATE?**

16
17 A. Yes.

18
19 **Q. WHY?**

20
21 A. MGE continues to believe that a true-up audit is necessary
22 an appropriate in this proceeding for several reasons. First, MGE
23 has budgeted approximately \$12,000,000, of capital investment
24 that it plans to place in service between June 30, 2009 and
25 September 30, 2009. This investment represents approximately
26 \$1,700,000 of additional annual revenue requirement.

27
28 Second, MGE plans to hire approximately 39 additional employees
29 during the summer of 2009. This includes 25 outside plant
30 personnel that would add approximately \$1,500,000 to the
31 Company's annual revenue requirement. MGE also plans to hire
32 at least 4 customer service representatives during the summer of
33 2009 to fill current vacancies in time to be trained for the

1 2009/2010 winter season. This would add approximately
2 \$240,000 to the annual MGE revenue requirement.
3

4 Lastly, to the extent the Commission uses a capital structure based
5 on the Company's actual debt and equity (without conceding the
6 appropriateness of such an approach), because MGE expects the
7 equity ratio to increase during the true-up period resulting in a
8 higher revenue requirement, MGE would want that structure to
9 reflect the Company's most current percentages. **Using the true-
10 up mechanism to recognize known and measurable changes
11 such as those listed above is the best way to mitigate regulatory
12 lag in this proceeding. Without a true-up, by the time rates go
13 into effect (February 28, 2010 based on the operation of law
14 date) MGE will already be experiencing a shortfall from the
15 authorized rate of return simply by not having the plant
16 increases and expense increases since April 2009 included in
17 rates.**
18

19 [Noack Updated Test Year Direct Testimony, Case No. GR-2009-
20 0355, pp 2-3, emphasis added]

21 Witness Noack's 2009 Rate Case testimony is similar to the testimony in MGE's 2004 and
22 2006 rate cases. MGE's testimony in these cases form a pattern of specifically requesting a
23 true-up when known and measurable expenses are increasing, but when expenses have the
24 chance to decrease to the benefit of customers, MGE would rather retain the savings to the
25 detriment of customers.

26 Q. What has been Laclede Gas' position been on the true-up process?

27 A. In Laclede Gas' most recent rate case, Case No. GR-2013-0171, Witness
28 Glenn W. Buck, who is also an MGE witness in the current rate case, opined on the need for a
29 true-up in that case:

30 Q. Is the Company [Laclede Gas] requesting a true-up in this
31 case?
32

33 A. **Yes. Laclede requests a true-up through a date no earlier
34 than July 31, 2013. It is essential that the most recently available
35 information be included in the calculation of rates.** Additionally,
36 there are several significant events that will occur between the

Surrebuttal Testimony of
Keith Majors

1 proposed update period of March 31, 2013 and July 31, 2013. These
2 include, but are not limited to, changes in labor rates paid under the
3 Company's union labor contracts, a possible change in the annual
4 assessment paid to the Commission, and, most importantly, the
5 placement in service of the new Customer Care and Billing system as
6 part of the EIMS project. However, the Company is willing to work
7 with the parties concerning an alternative update method that would
8 obviate the need for a complete true-up.

9
10 [Glenn W. Buck Direct Testimony, Case No. GR-2013-0171, page
11 11, emphasis and clarification added]

12 Witness Buck further explains at page 14 of his direct testimony in Case No. GR-2013-0171
13 that Laclede Gas had August 1, 2013 payroll increases which represented the need to have the
14 true-up at least through July 31, 2013 to allow for wage and salaries increases.

15 Q. For Category 2, does MGE plan to make additional employee reductions after
16 December 31, 2013?

17 A. Yes. Staff is aware of the expectation by MGE that it will have significant cost
18 reductions throughout 2014 and beyond, primarily as result of employee reductions and
19 consolidations from the acquisition. However, those cost savings have not been included in
20 this case by either MGE or Staff.

21 Q. Why was December 31, 2013 used as the true-up period in this case?

22 A. Staff was informed by the Company early in its audit process when it was
23 evaluating what true-up period to use that there would not be any significant costs savings the
24 first quarter of 2014. While Staff envisioned using March 31, 2014 as the true-up in the early
25 stages of the case, based on assurances by the Company that there were no significant changes
26 expected to occur until sometime later in the 2nd quarter of 2014, Staff decided on using
27 December 31, 2013 as the true-up. Staff used the December 31, 2013 cutoff, based on the
28 reliance of this information from the Company.

Surrebuttal Testimony of
Keith Majors

1 Q. Did Staff inquire if there were changes occurring after December 31, 2013?

2 A. Yes. After learning that significant cost reductions were going to occur on and
3 immediately after April 1, 2014, Staff submitted several data requests on March 11, 2014 for
4 the MGE positions added and eliminated through February 2014. MGE objected to Staff's
5 data requests 232, 233, and 234, but did refer Staff to the monthly reports related to staffing
6 that MGE provided pursuant to its obligations under the *Stipulation and Agreement* in GM-
7 2013-0254. The responses to these data requests are attached as Schedule KM-1.

8 According to these monthly reports provided by MGE pursuant to the Acquisition
9 Case, MGE has reduced its workforce by an additional ** ___ ** employees through
10 January 31, 2014, and an additional ** ___ ** employees through February 28, 2014. The
11 annual salaries, wages, and benefits related to these terminated employees are an additional
12 annual savings of ** _____ **.

13 Staff expects similar cost reductions in March and certainly there will be significant
14 reductions in April and likely the rest of 2014 as the consolidation of operations MGE into
15 Laclede Gas continues.

16 Q. Has Staff reflected these reductions in the cost of service?

17 A. No. Staff's true-up cutoff is December 31, 2014. To the extent cost increases
18 or reductions occur past this date there is no change in Staff's revenue requirement. In fact,
19 Staff included the ** _____ ** terminated employees' salaries, wages, and benefits in the cost
20 of service. The Company will retain these savings until the effective date of rates in the next
21 MGE division rate case. If the Company maintains its current pattern of rate case filings to
22 maintain the ability to have an ISRS surcharge, the Company will retain these savings, and
23 any other savings from employee reductions, **for nearly four years.**

Surrebuttal Testimony of
Keith Majors

1 Q. For Category 3, what salary, wages, and benefits savings did MGE realize
2 between the 2009 Rate Case and the current rate case?

3 A. Staff's true-up in the 2009 Rate Case captured MGE employee salary, wages,
4 and benefits through September 30, 2009. Staff's annualized level of these expenses included
5 700 employees, which was the exact number of employees at that cutoff period. Between the
6 September 30, 2009 cutoff and MGE's direct filed payroll based on July 2013, MGE reduced
7 its workforce by 44 employees. These reductions were before considering the Day 1
8 employees or the additional reductions through December 31, 2013. Using the average annual
9 wage rate and benefit gross up (55.1%), Staff calculated an annual savings of \$4.1 million for
10 the employee reductions from September 30, 2009 through July 2013. Based on the effective
11 date of new rates from this case (August 13, 2014), MGE will be able to retain the savings
12 from these reductions **nearly 4 years**, to the benefit of its shareholders.

13 Q. Can you summarize the savings MGE has realized and will retain in the future
14 from employee reductions?

15 A. The tables below summarize the annual savings from MGE's employee
16 reductions:

17

MGE Employee Savings by Cost Category			
Cost Category	Number of Employees	Employees	Total Annual Savings
1	6	Day 1 Employees	\$ 1,596,843
1	8	Reductions July - September 2013	707,519
1	5	Reductions October - December, 2013	477,757
2	** _ **	Reductions during January 2014	** _____ **
2	** _ **	Reductions during February 2014	** _____ **
3	44	Reductions September 2009 - July 2013	<u>4,131,955</u>
	** _ **	Total Savings	** \$ _____ **

18

Surrebuttal Testimony of
Keith Majors

1 Q. For Category 4, what savings will MGE retain from the amount of corporate
2 allocations currently in rates from the 2009 Rate Case being paid by customers?

3 A. The 2009 Rate Case included \$5.0 million (which is the source of the
4 stipulated cap) of corporate allocations, as adjusted by Staff, in the cost of service from
5 Southern Union, then owner of MGE. After the acquisition of MGE by Laclede Gas
6 September 1, 2013, the \$5.0 million in rates was no longer being paid to Southern Union/ETE
7 for its services to MGE. Because Laclede Gas and Laclede Group has no allocation
8 methodology in place, and therefore no billing and payment for goods and services to and
9 from MGE, and therefore no costs charged to MGE, the amount for corporate services in rates
10 will be retained by MGE until such time as an actual allocation is made. The amount in rates
11 going forward, as recommended by Staff, is the stipulated cap from the Acquisition Case. As
12 identified in Witness Buck's rebuttal testimony, the allocation process will "likely occur in the
13 3rd quarter of Fiscal 2014." Until that time, the amount of corporate allocations, both in
14 current rates resulting from the 2009 Rate Case and rates going forward from the current case
15 will be retained by MGE shareholders.

16 Q. For Category 5, what savings will MGE and Laclede Gas retain resulting from
17 the difference between the greater corporate allocation to Laclede Gas before the acquisition
18 and the same costs being allocated to MGE going forward?

19 A. Laclede Gas' most recent rate case, Case No. GR-2013-0171 included an
20 amount of corporate allocations in the cost of service. These allocations were premised upon
21 Laclede Gas being allocated the majority of the corporate allocations among Laclede Group's
22 divisions. The following table lists the allocation percentages for Laclede Group's divisions
23 *before* the acquisition of MGE:

Surrebuttal Testimony of
Keith Majors

1

The Laclede Group Subsidiaries	Pro Forma Allocation % without MGE
Laclede Development	0.09%
Laclede Energy Resources	6.72%
Energy Services (Dormant)	0.00%
Family Services - Life Insurance	0.01%
INV - Investment Holding Company	0.02%
Laclede Gas Company	92.61%
Propane Cavern (Dormant)	0.00%
Laclede Pipeline Company	0.24%
Missouri Gas Energy (MGE)	0.00%
Laclede Venture - CNG Fueling Stations	0.19%
LIR - Risk Management & Reinsurance	0.02%
OIL - Underground Oil Storage	0.10%
Total	100.00%

2

3

The following table lists the pro-forma allocation percentages for Laclede Group's divisions *after* the acquisition of MGE:

4

5

The Laclede Group Subsidiaries	Pro Forma Allocation % with MGE
Laclede Development	0.06%
Laclede Energy Resources	4.50%
Energy Services (Dormant)	0.00%
Family Services - Life Insurance	0.00%
INV - Investment Holding Company	0.02%
Laclede Gas Company	62.80%
Propane Cavern (Dormant)	0.00%
Laclede Pipeline Company	0.16%
Missouri Gas Energy (MGE)	32.24%
Laclede Venture - CNG Fueling Stations	0.13%
LIR - Risk Management & Reinsurance	0.01%
OIL - Underground Oil Storage	0.07%
Total	100.00%

6

Surrebuttal Testimony of
Keith Majors

1 The difference between Laclede Gas' pro-forma allocation before and after the MGE
2 acquisition is a reduction of 29.8%. Laclede Gas' most recent rate case resulted in an increase
3 of \$14.8 million, effective July 8, 2013, which included the higher level of corporate
4 allocations to Laclede Gas on a pre-acquisition basis. Laclede Gas ratepayers will be paying
5 an inflated level of corporate allocations considering the expected reduction in allocated costs
6 once MGE is actually allocated its share of these shared services. Laclede Gas will be able to
7 retain that excess until the effective date of rates in the next general rate case for the Laclede
8 Gas division, assuming an actual allocation and billing process to MGE can be established.

9 Using the pro-forma Laclede Gas and Laclede Group allocations to MGE, discussed in
10 Staff's Cost of Service Report, an estimate can be made of Laclede Gas retained savings.
11 Using the 29.8% savings difference from the tables above, and the 34.08% pro-forma
12 allocation of Laclede Gas internal payroll to MGE, the table below is an estimate of the
13 retained savings:

14

Laclede Gas Retained Savings	
Laclede Group Allocation Pool	\$ 10,482,630
Laclede Gas Pre/Post Merger % Difference	29.81%
Laclede Gas Savings from Laclede Group Allocations	3,124,356
Laclede Gas Allocation Pool (Labor)	\$ 9,532,122
Staff's Benefits Gross Up	55.10%
Laclede Gas Allocation Pool with Benefits	\$ 14,784,487
Laclede Gas Pre/Post Merger % Difference	34.08%
Laclede Gas Savings from Laclede Gas Payroll	5,038,553
Total Laclede Gas Retained Savings	8,162,909

15
16 The difference between Laclede Gas pre-merger and post-merger allocations creates a savings
17 of at least \$8.1 million of expense, which does not include amounts charged to capital.

Surrebuttal Testimony of
Keith Majors

1 Considering MGE’s new shared services adjustment, MGE Witness Buck is
2 advocating an even greater over collection of corporate allocations over and above what will
3 already be retained by MGE and Laclede Gas.

4 Q. Could this situation have been remedied by concurrent rate filings by the
5 Laclede Gas and MGE divisions?

6 A. Yes. Although Laclede Gas is under a rate moratorium agreed to in the
7 *Stipulation and Agreement* in Case No. GM-2013-0254 until October 1, 2015, MGE was not
8 obligated to file the current pending rate case. If a rate case were filed including both MGE
9 and Laclede Gas divisions and an appropriate allocation methodology was in place, each
10 division would receive its appropriate allocation which in turn would be paid by their
11 respective ratepayers.

12 In the current situation, Laclede Gas ratepayers are paying inflated corporate
13 allocations which the Company is currently collecting in rates, while MGE is requesting its
14 customers for an additional \$800,000 to pay for corporate allocations which are not even
15 being made.

16 Because of the difficulties in allocating corporate allocations between Laclede Gas and
17 MGE, it would have been preferable to examine both rate jurisdictions’ cost of service in a
18 joint rate filing.

19 Q. Can you give an example of a different utility that filed a rate case subsequent
20 to a merger or acquisition?

21 A. Yes. The 2008 acquisition of the former Aquila, Inc. (“Aquila”) properties by
22 Kansas City Power & Light Company’s (“KCPL”) parent Great Plains Energy, Inc had
23 similarities to the Laclede Gas – MGE acquisition. Both acquisitions were made by a

Surrebuttal Testimony of
Keith Majors

1 dominant entity as opposed to a “merger of equals”. Both involved a Missouri utility
2 acquiring a Missouri utility; although KCPL does have Kansas property, it is headquartered in
3 Missouri and the majority of its operations are in Missouri. Both acquisitions were followed
4 shortly by rate filings. For clarity, Aquila has now been renamed KCP& L – Greater Missouri
5 Operations, or GMO.

6 The KCPL rate case was filed September 5, 2008 after the July 14, 2008 close of the
7 Aquila acquisition. The MGE rate case was file in the same month of the acquisition—
8 September 16, 2013 filing and September 1, 2013 completion of the acquisition by
9 Laclede Gas.

10 But there are some key differences between the two acquisitions concerning the
11 treatment of corporate allocations and shared services between the acquiring and acquired
12 utility. In the case of the KCPL-Aquila acquisition, all former Aquila employees that
13 remained after the acquisition were immediately moved to KCPL. This necessitated an
14 allocation process to be in place Day 1 of the acquisition to appropriately allocate all costs not
15 only between KCPL and GMO, but also between GMO’s two rate jurisdictions – Missouri
16 Public Service – MPS and St. Joseph Light & Power – SJLP. Not only was this allocation
17 process in place the first day of the acquisition, the actual allocations formed the basis of
18 Staff’s payroll adjustment to the cost of service for all three rate jurisdictions. Both the
19 concurrent filing of the KCPL and GMO rate cases and the establishment of an appropriate
20 allocation mechanism ensured that each jurisdiction received the correct allocation of costs
21 creating no shortfall to the companies and no over collection from customers.

Surrebuttal Testimony of
Keith Majors

1 For a more thorough discussion of Staff’s adjustments in the referenced KCPL and
2 GMO rate cases, Case Nos. ER-2009-0089 and ER-2009-0090, see the Staff Cost of Service
3 report in the respective cases.

4 Q. Did KCPL request a true-up in the 2009 KCPL and GMO rate cases?

5 A. Yes. KCPL filed those rate cases in September 2008 and requested a true-up
6 through either March 31, 2009 or April 30, 2009 depending on when certain plant additions
7 were to be complete. In contrast, MGE requested a September 30, 2013 update date cutoff be
8 used for case which was filed September 16, 2013. The KCPL rate case had a true-up seven
9 months beyond the date of its rate request while MGE wanted to use the same month in which
10 it filed its rate case—a substantial difference.

11 Q. For Category 6, what savings will MGE retain based on the difference between
12 the employee salary, wage, and benefit expense built into rates and the reduction of that
13 expense through ** _____ **?

14 A. Staff Witness Lisa Kremer thoroughly discusses the ** _____
15 _____ ** in her surrebuttal testimony in this rate case. Any cost
16 reduction through ** _____ ** would be a cost reduction retained by
17 MGE until reflected in the cost of service in some future rate case. Staff has included the
18 salaries and wages of all MGE employees – including those who work in the ** _____ **
19 – in the cost of service as of December 31, 2013.

20 Q. For Category 7, what other savings related to the acquisition of MGE and the
21 continued merger of Laclede Gas and MGE operations will MGE retain?

22 A. Any cost savings that is realized because of the combination of Laclede Gas
23 and MGE operations is referred to as a “merger synergy.” While the majority of synergies are

Surrebuttal Testimony of
Keith Majors

1 obtained because of employee reductions, there are several categories of other non-labor
2 synergies that will occur. Some examples would be greater purchasing discounts from
3 suppliers, facilities consolidations, elimination of duplicate software licenses, and sharing of
4 subscriptions and corporate services.

5 Q. Can Staff quantify the amount of synergy savings from the acquisition?

6 A. From the limited information Staff has received, the actual non-labor synergy
7 savings achieved during September and October 2013 was ** _____ ** and the amount
8 projected for November and December 2013 was ** _____ **. On an annual level, this
9 amount would be approximately ** _____ ** [source: MGE response to Data Request
10 No. 50.1]. The entire amount of these synergies would be retained by MGE through the
11 effective date of rates in this case. Any synergies after Staff's December 31, 2013 cutoff will
12 be retained by MGE through the effective date of rates in MGE's **next** rate case. If the
13 Company maintains its current pattern of rate filings to maintain the ability to have an ISRS
14 surcharge, the Company will retain these savings, and any other savings from employee
15 reductions, **for nearly four years.**

16 Q. Please summarize your testimony concerning the issue of corporate allocations.

17 A. The Commission should adopt Staff's recommended level of corporate
18 allocations of the stipulated cap of \$5.08 million. MGE's adjustment to purportedly account
19 for inflation by using the CPI is an illogical use of this index and should be rejected. MGE's
20 adjustment to include an additional "adder" of \$800,000 of corporate allocations is not
21 known and measurable, and should likewise be rejected.

1 **INCENTIVE COMPENSATION**

2 Q. Please provide a brief summary of the difference between Staff and MGE
3 concerning incentive compensation.

4 A. In its direct filing, MGE included the test year unadjusted incentive
5 compensation expense of \$2,980,788. None of MGE's test year incentive compensation was
6 capitalized, unlike payroll and payroll related benefits. Staff has reflected a three-year
7 average of 2010-2012 actual payouts for safety and customer service metrics under the
8 Southern Union/ETE incentive compensation plans, addressed at Section VII. Income
9 Statement, C.2. Incentive Compensation and Bonuses, pp. 61-67 in Staff Report filed on
10 January 29, 2014. Staff recommends a \$351,343 gross expense, or \$298,607 after application
11 of Staff's O&M ratio of 84.99 percent.

12 MGE has also recommended a new adjustment in Witness Noack's rebuttal testimony
13 reducing MGE's request for incentive compensation expense. I will address both adjustments
14 in this testimony.

15 Q. How did Staff determine its adjustment for incentive compensation?

16 A. Staff calculated a three-year average of incentive compensation awards for
17 customer service and safety metrics based on actual payments for the plan years 2010, 2011,
18 and 2012, and did not include any financial-based metrics in its average. In addition, Staff
19 removed several management employees who are no longer employed by MGE from
20 the amounts used for Staff's average. After determining the normalized level of
21 incentive compensation, the total amount was reduced by the application of Staff's O&M
22 Expense Ratio.

Surrebuttal Testimony of
Keith Majors

The following table identifies the components of the incentive plan payouts for the years 2009 through 2012:

	Total Payout	Safety	Customer Service
2010 Incentive Compensation	1,462,153	141,041	141,041
Less: Removed Employees	284,766	25,908	25,908
2010 Net	\$1,177,388	\$115,132	\$115,132
2011 Incentive Compensation	1,317,086	125,456	125,456
Less: Removed Employees	262,807	20,762	20,762
2011 Net	\$1,054,279	\$104,694	\$104,694
2012 Incentive Compensation	2,489,281	389,298	389,298
Less: Removed Employees	645,413	82,110	82,110
2012 Net	1,843,868	307,189	307,189
2010-2012 3 Year Average	\$1,358,512	\$175,672	\$175,672

Below is the summary of Staff's recommended incentive compensation expense:

2010-2012 3 Year Average Safety	175,672
2010-2012 3 Year Average Customer Service	175,672
Staff Recommended Incentive Compensation – 3 year average of Safety and Customer Service	351,343
Staff's O&M Ratio	84.99%
Incentive Compensation to Expense	\$ 298,607

Q. What is the capital/expense ratio?

A. The expense ratio is used to identify the amount of payroll and payroll related costs, such as incentive compensation, that would be charged to expense. The amount charged to expenses is reflected in Staff's revenue requirement calculation. The remaining portion of these payroll costs are capitalized—allocated to construction projects and non-regulated operations.

Surrebuttal Testimony of
Keith Majors

1 Q. On page 17 of Witness Noack's rebuttal testimony, he states that Laclede Gas
2 is offering the incentive compensation plan to MGE union employees for the 2013-14
3 plan year. Are MGE employees currently covered under any specific incentive
4 compensation plan?

5 A. No. Although MGE has asserted in both meetings with Staff and in written
6 responses to data requests that MGE will be included in Laclede's incentive compensation
7 plans, MGE has not provided Staff any actual plan documents that have been provided to
8 MGE employees, metrics, goals, or any other document that would identify the bonus payout
9 pool or the projected payout to the eligible employees. At this time, Staff has not been
10 provided any goals, guidelines, or metrics that an incentive payment would be based on. Staff
11 has received documentation related to Laclede's FY2013 (October 2012-September 2013)
12 incentive plan, but this was on a pre-MGE acquisition basis.

13 Staff has been informed that MGE is currently in negotiations with its union for a new
14 contract. Currently MGE's union is not included in any incentive compensation plan.
15 Whatever outcome of those negotiations, including any new incentive compensation plan,
16 would be an out-of-period event that is not known and measurable.

17 There are expected employee reductions that have already occurred beginning in
18 January 2014, therefore the work force that the incentive compensation is purported to be
19 applied to will be declining through the year. It is not possible to know what level of
20 incentive compensation will be paid out in 2014 due to the uncertainty of employee levels and
21 uncertainty surrounding the plan itself.

22 Q. How do short-term incentive compensation plans typically work?

Surrebuttal Testimony of
Keith Majors

1 A. For a given plan year, management determines the goals and objectives for the
2 incentive compensation plan and communicates them to the general body of employees at the
3 start of the plan year. These goals are typically communicated to employees in writing early
4 in the plan year to provide employees time to achieve the goals and for management to
5 determine and assess performance. In the case of MGE, five months will have passed from
6 the beginning of the plan year which started October 1, 2013. Staff has no information from
7 MGE concerning goals and objectives for the FY 2014 incentive compensation plan for MGE
8 employees. Since it appears MGE has not determined goals for the FY 2014 plan and has not
9 communicated them to the eligible employees, this is contrary to the goal of having an annual
10 incentive plan as the fiscal year is nearly half over.

11 Q. Why is it important to have objectives and goals in writing for an
12 incentive plan?

13 A. Employees who are being counted on to perform at a level that would generate
14 cost savings, provide exceptional customer service at safe and reliable standards can provide
15 such through incentive mechanism. In fact, it is on this basis in which incentive plans were
16 developed. If employees are to be held to performance standards they must be made aware of
17 the expectations. Letting employees know what is expected of them as early in the plan year
18 as possible is a key element in providing safe, reliable utility service at lowest costs.

19 Q. On page 17, Witness Noack makes the following statement: "...As
20 acknowledged by Staff, MGE management employees will be included in Laclede Gas'
21 incentive compensation plan, which covers the period October 1, 2013 – September 30,
22 2014." What evidence does Staff have that any MGE employees will be included in Laclede
23 Gas' incentive compensation plan?

Surrebuttal Testimony of
Keith Majors

1 A. Other than Laclede Gas employees' assertions, Staff has no documentation, no
2 goals, no metrics, and no projected payouts that could be used to determine an actual payout,
3 or even a projected payout, for MGE employees. According the response to Data Request
4 No. 230.4, MGE employees will receive incentive compensation earned in fiscal year 2014
5 shortly after the beginning of October following FY2014, which would be October 2014.
6 This is the first date an actual incentive compensation payment under the Laclede Gas
7 incentive plan would be paid to MGE employees. This date is far beyond Staff's
8 December 31, 2013 true-up date and the August 13, 2014 Operation of Law date in the current
9 case. Any projected payment MGE recommends would be an out-of-period adjustment and
10 not "known and measurable."

11 Q. What is the "known and measurable" standard?

12 A. The "known and measurable" standard dictates that expenses included in the
13 cost of service are both known (a high degree of certainty that the expense will be incurred by
14 the utility), and measurable (a high degree of accuracy in measuring the expense). Any
15 projected payments to MGE employees that are to be paid October 2014 will not be known
16 until the actual results of the FY2014 plan year were calculated. It would be inappropriate to
17 include any incentive compensation based on these projected payments in the cost of service
18 and on a plan that has not been communicated to employees and to a work force that is
19 anticipated to be significantly reduced.

20 Q. On page 16 of his rebuttal testimony, Witness Noack calculates Staff's
21 recommended incentive compensation as 0.7 percent of payroll. Is this figure in line with the
22 amounts Staff and MGE have included in MGE's cost of service in the 2009 Rate Case?

1 A. Yes. In the 2009 Rate Case, Witness Noack recommended to the Commission
2 that MGE not recover financially based MGE incentive compensation through the cost of
3 service which is consistent with the approach taken by Staff in this case. Witness Noack's
4 Direct testimony in the 2009 Rate Case addressed MGE's incentive compensation adjustment:

5 **Q. PLEASE EXPLAIN THE PAYROLL RELATED**
6 **ADJUSTMENTS.**

7
8 A. ...A separate adjustment has been proposed on Schedule
9 H-18, which eliminates financially based MGE incentive
10 compensation and bonuses included in the test year...

11
12 [Noack Direct Testimony, Case No. GR-2009-0355, page 10]

13 MGE provided workpapers in its filed cost of service model in that case. MGE's incentive
14 compensation adjustment H-18 was included in the filed cost of service model and was
15 premised upon the test year ending December 31, 2008 incentive compensation.

16 MGE's Adjustment H-18 in GR-2009-0355 is summarized below:

17

Description	Incentive Compensation	Holiday Bonuses	Work Performance Bonuses	Total
2008 Incentive and Bonus Payments	\$1,275,200	\$51,215	\$8,550	\$1,334,965
Non Financial Based Incentives	366,060	0	8,550	\$374,610
Adjustment	(\$909,140)	(\$51,215)	\$0	(\$960,355)

18
19 MGE's adjustment removed all financial-based incentives, as well as holiday bonuses. Staff
20 reflected MGE's adjustment in the cost of service.

Surrebuttal Testimony of
Keith Majors

1 As a percentage of payroll, both MGE's 2009 Rate Case incentive compensation
2 adjustment and Staff's current rate case incentive compensation adjustment are both less than
3 one percent of payroll:

Case	Annualized Payroll	Annualized Incentive Compensation	Incentive as % of Payroll
2009 Rate Case	\$42,422,661	\$374,610	0.88%
2014 Rate Case	\$44,402,461	\$351,343	0.79%

5
6 Q. What is the difference between MGE's 2009 Rate Case adjustment and Staff's
7 adjustment in this rate case?

8 A. The only difference between the two adjustments is that Staff in this case used
9 a three-year average of actual incentive compensation payments, and MGE used the test year
10 payments.

11 Q. Did MGE give a reason why it did not adjust incentive compensation expense
12 in the current case similar to what it did in the 2009 Rate Case?

13 A. No. If neither Staff nor MGE adjusted incentive compensation expense, the
14 resulting amount remaining in the test year would be the higher than any plan payout during
15 the past five years. It would be to MGE's advantage not to adjust incentive compensation
16 expense because it results in higher costs and increases revenue requirement, which means the
17 revenue collected for the incentive compensation will be retained as earnings if the payments
18 are not actually made. There are several reasons why the amount of incentive compensation in
19 the test year ending April 30, 2013 is abnormally high:

- 20 1. The test year included expenses for both the 2012 Calendar Plan year
21 and the 2013 Calendar Plan year;

Surrebuttal Testimony of
Keith Majors

1 2. The test year amount booked was 100 percent of the amount incurred,
2 there was no incentive compensation charged to capital accounts (capitalized);
3 and

4 3. The test year amount included incentive compensation for terminated
5 “Day 1” employees that will no longer be paid.

6 Q. How does the amount MGE has recommended in the cost of service compare
7 with previous levels of incentive compensation?

8 A. The amount MGE requests is the higher than any of the five previous calendar
9 plan year actual payouts. Below is a table that details the last five plan year payouts, as well
10 as MGE’s recommended test year ending April 30, 2013 incentive compensation:

11

Plan Year	Actual Payout
2009 Plan Year Payout	\$ 1,022,803
2010 Plan Year Payout	\$ 1,462,153
2011 Plan Year Payout	\$ 1,317,086
2012 Plan Year Payout	\$ 2,489,282
2013 Plan Year Payout - Partial Year	\$ 1,547,948
MGE’s Test Year ending April 30, 2013	\$ 2,980,788

12
13 The amount of the actual 2013 plan year payout was based on January 1, 2013 through
14 August 31, 2013 – the period of time MGE was owned by Southern Union/ETE. The test year
15 ending April 30, 2013 was abnormally high, and did not equal any plan year because the test
16 year spans both the 2012 and 2013 plan years. MGE did not even adjust the test year expense
17 to account for this abnormality, leaving the inflated expense in the test year cost of service to
18 its benefit.

19 Q. How is the amount booked to the test year inflated by MGE not charging any
20 incentive compensation to capital accounts?

Surrebuttal Testimony of
Keith Majors

1 A. MGE’s policy is to charge 100 percent of incentive compensation to expense.
2 The amount expensed in the test year is the gross incentive compensation costs, with no
3 amount charged to construction. Staff routinely recommends capitalizing employee benefits,
4 including a portion of incentive compensation, discussed earlier in this testimony. In the
5 current rate case, both Staff and MGE recommended the capitalization of a portion of the
6 following expenses:

7 Payroll – Salaries and Wages
8 Medical, Dental, and Vision Benefits
9 Payroll Taxes – FICA, Federal & State Unemployment Taxes
10 Payroll Related Insurance – Life, Long-Term Disability
11 Deferred Compensation – 401k Company Match
12 Pension Expense and Tracker Amortization

13 A portion of payroll and benefits expense is capitalized because throughout the year a
14 substantial portion of MGE’s directly charged labor expense is related to construction
15 activities. Because the direct labor is charged to construction activities, a commensurate
16 portion of benefits, payroll taxes, and incentive compensation should also be capitalized.

17 Staff’s recommended incentive compensation expense is based on MGE’s historical
18 payouts from the short-term incentive compensation plan. The awards were cash-based and
19 were paid to eligible non-union employees. Staff sees no reason why a portion of incentive
20 compensation should not be capitalized just like any other payroll related costs.
21 Understandably, MGE did not adjust incentive compensation, as the expense was inflated and
22 contributed to a higher overall revenue requirement.

23 Q. Does the test year incentive compensation expense include amounts paid to
24 employees who are no longer at MGE?

25 A. Yes. MGE’s recommended level of incentive compensation includes both
26 amounts related to the “Day 1” local MGE senior management employees and amounts

1 related to any other employee reductions MGE has experienced. Staff's recommended level
2 does not include the amounts awarded to the Day 1 employees, and the effect of fluctuating
3 employee levels is mitigated by Staff's recommended 2010-2012 three-year average.

4 MGE has reduced its workforce by over 10 percent since the 2009 Rate Case. The
5 table below details the employee reductions by time period and the related annual savings
6 with benefits:

7

MGE Employee Reductions		
Number of Employees	Time Period	Total Annual Savings
44	Reductions September 2009 - July 2013	\$4,131,955
8	Reductions July - September 2013	707,519
6	Day 1 Employees	1,596,843
5	Reductions October - December, 2013	477,757
** _ **	Reductions during January 2014	** _____ **
** _ **	Reductions during February 2014	** _____ **
** _ **	Total Reductions	** _____ **

8
9 MGE's test year incentive compensation includes expense related to the vast majority of these
10 terminated employees. The incentive compensation expenses related to these terminations
11 will no longer be incurred by MGE, and the incentive compensation expenses booked to the
12 test year are therefore inflated. Yet, the Company used this inflated test year amount as basis
13 for its request in this case.

14 Q. Witness Noack discusses Laclede Gas' incentive plan on page 18 of
15 his rebuttal testimony. Did MGE provide any documentation related to the Laclede Gas
16 incentive plan?

Surrebuttal Testimony of
Keith Majors

1 A. Yes. MGE provided the actual payouts for the FY2013 plan year and some
2 documentation on the calculation of the incentive. The Laclede Gas incentive is based on
3 various factors for union, non-union management, and director level management.

4 Q. Was any of the Laclede Gas incentive compensation paid based on financial
5 goals or metrics?

6 A. Yes. For the union and non-union management incentive, 20 percent of the
7 incentive was based on Laclede Group Earnings per Share (EPS) and 30 percent on Laclede
8 Gas operating income. Staff did not receive data on any payouts for the director level Laclede
9 Gas management, but, for this analysis, there should be no director level management at the
10 MGE level because MGE has no director level management of its own.

11 Q. On pages 19-23 of his rebuttal testimony, Witness Noack provides several
12 reasons why the Commission should allow incentive compensation based on financial metrics
13 in the cost of service. How has the Commission previously ruled on financial based incentive
14 compensation?

15 A. As I explained in my rebuttal testimony, the Commission has a long history of
16 disallowing incentive compensation based on financial metrics from the cost of service.
17 There have been several recent rate cases, including MGE rate cases, that the Commission has
18 disallowed financial-based incentive compensation:

19 Missouri Gas Energy – GR-96-285

20 Missouri Gas Energy – GR-2004-0209

21 Kansas City Power & Light – ER-2006-0314

22 Kansas City Power & Light – ER-2007-0291

Surrebuttal Testimony of
Keith Majors

1 For brevity, I have referenced the pertinent section of the Report and Order in each of these
2 cases in my rebuttal testimony and did not reference them in this testimony.

3 In prior cases, the Commission has allowed a portion of incentive compensation that
4 was not based on financial metrics, but rather was based on customer service, safety, or other
5 metrics that can be shown to directly benefit the customers.

6 Q. On page 19 of his rebuttal testimony, Witness Noack supports an incentive
7 plan that aligns the interests of customers and shareholders. Is Staff opposed to such an
8 incentive plan?

9 A. No. Staff does not take issue with the design of MGE or Laclede Gas'
10 incentive plan. Staff's concern lies with ensuring that the primary beneficiaries of the benefits
11 of the incentive plan appropriately pay for the costs of the incentive plan. For example,
12 Staff's adjustments in the 2009 Rate Case, and in the four most recent KCPL rate cases, focus
13 on assigning the costs to the stakeholder group that receives the benefit. In this case, Staff
14 endorses customers paying for metrics based on customer service and safety, and shareholders
15 paying for metrics based on financial performance, the benefits of which shareholders reap in
16 the form of increased earnings. This represents an appropriate sharing mechanism where
17 stakeholders pay for the benefits they receive.

18 Based on Staff's recommended adjustments, the Commission has endorsed this
19 sharing of costs between shareholder and ratepayer. In the 2006 and 2007 KCPL rate case
20 Report and Orders specifically, Staff removed amounts awarded for financial metrics and
21 appropriately allocated customer focused awards to customers through the cost of service.
22 Witness Noack quotes at page 19 of his rebuttal testimony, from the Commission's 2006
23 Report and Order in Case No. ER-2006-0314, "if the method KCPL chooses to compensate

Surrebuttal Testimony of
Keith Majors

1 employees shows no tangible benefit to Missouri ratepayers, then those costs should be borne
2 by shareholders, and not included in the cost of service.” What Staff did in the 2014 MGE
3 case is consistent with what it did in the 2006 KCPL rate case.

4 MGE’s recommendation recognizes that shareholders and ratepayers should share in
5 the benefits of an incentive program, but allocates all the costs of those benefits to the
6 ratepayer. This is a one-sided approach and should be rejected by the Commission.

7 Q. On page 20, Witness Noack identifies reduced O&M expense per customer as
8 a metric of the Laclede Gas incentive program. Would this be an appropriate metric for an
9 incentive plan?

10 A. It could be, if it is not at the expense of quality of service. In this case, because
11 MGE will purportedly be implementing the Laclede Gas incentive plan on a prospective basis,
12 ratepayers are paying “inflated” O&M expenses that the incentive compensation program is
13 designed to reduce. In this case, MGE is requesting an incentive expense that has never been
14 paid to employees, and yet MGE is requesting in rates higher expense which the plan is
15 designed to reduce. In the meantime, if the Commission endorses MGE’s position, customers
16 would pay for both the incentive plan and inflated costs, costs that when reduced the
17 shareholders immediately benefit.

18 Q. When costs are reduced do customers always benefit?

19 A. No. Unlike shareholders, who directly and immediately benefit from any cost
20 reductions, customers have to wait for cost savings until rates are changed. If there are cost
21 decreases during a time when rates are not changed frequently, customers may never benefit
22 from these decreases. For example, if the Company experiences declines in its payroll costs
23 from work force reductions, the Company’s costs will immediately go down with the

Surrebuttal Testimony of
Keith Majors

1 shareholders directly benefiting. The customers will not see any of those savings, if at all,
2 until rates change to reflect costs for those reductions of the payroll costs. If the Company
3 goes through a period of time without filing for a rate increase, the payroll cost savings will
4 go directly to shareholders during the entire period before rates are changed. At the time of
5 filing next rate case, if the Company's costs for payroll increase, the customers will never
6 have opportunity to benefit from the employee reductions.

7 Q. On page 22, Witness Noack states that "customers should not be asked to pay
8 for an incentive program that benefits only shareholders and provides no tangible benefit to
9 the customers themselves." Is this how MGE or Laclede Gas' incentive programs are
10 designed?

11 A. No. Both Laclede Gas' current and MGE's former incentive program used a
12 balanced approach, providing customer-focused and shareholder-focused goals to its
13 employees. My understanding of Witness Noack's testimony is that if there is even one
14 portion of the incentive plan that benefits customers, then customers should pay for the entire
15 incentive, regardless of the portion that directly benefits them. Essentially, this is an "all or
16 nothing" approach. This could result in customers paying for an unbalanced incentive, for
17 example 95 percent financial driven and 5 percent customer driven. MGE would have
18 customers pay for the entire incentive, while they would not directly benefit from the vast
19 majority of the goals of that plan. Shareholders, on the contrary, would be getting a "free
20 ride," because they would not be paying for any of the costs of the benefits they would reap.
21 Again, this is a one-sided, unbalanced approach that is contrary to the common-sense
22 approach that Staff advocates and that the Commission has previously approved.

Surrebuttal Testimony of
Keith Majors

1 Q. Did Laclede Gas request recovery of all incentive compensation in the last
2 prior Laclede Gas rate case?

3 A. No, Laclede removed some of the incentive compensation from consideration
4 in rates. Laclede Gas Witness David M. Seevers addressed the recovery of Laclede Gas'
5 incentive compensation in his direct testimony in Case No. GR-2013-0171:

6 Q. Has the Company [Laclede Gas] sought to recover all of
7 its incentive pay in rates?
8

9 A. No. Laclede does seek recovery of all of the costs of the
10 LGIP and AIP in rates. As indicated earlier in my testimony,
11 incentive payments under these programs are a common and
12 normal part of compensation, an expense that the Company
13 should be able to recover. With respect to the EIP, however,
14 while the Company believes that this program also provides
15 significant value to its customers, the non-capitalized portion of
16 these costs were excluded in order to make sure that
17 shareholders were also contributing to the cost of incentive pay.
18 In other words, the Company is seeking to recover only the
19 portion of EIP incentive pay that is required to be capitalized
20 under accounting rules. However, the considerable benefits
21 provided to customers by these plans would justify a much
22 higher allowance in rates of the costs associated with these
23 plans.
24

25 [David M. Seevers Direct Testimony, Case No. GR-2013-0171]

26 Witness Seevers' testimony reveals that Laclede Gas' approach to incentive compensation
27 differs from MGE's in the current case. Laclede Gas endorses the shareholders contributing
28 to the cost of incentive compensation; based on MGE's direct case, MGE does not. Laclede
29 Gas also capitalizes incentive compensation; it has been MGE's policy to not capitalize any of
30 these expenses.

31 Q. What are the respective portions that Staff advocates should be paid by
32 customers?

1 A. Staff recommends a three-year average of actual incentive compensation based
2 on customer service and safety metrics. The total three-year average of incentive
3 compensation, less the amounts paid to the former MGE management Day 1 employees, is
4 \$1,358,512. Of that amount, Staff recommends \$351,344 should be recovered from customers
5 in the cost of service, 25.9 percent of the three-year average. Based on the design of MGE's
6 former incentive plan, and the prospective Laclede Gas incentive plan, this represents an
7 appropriate sharing of the incentive costs between the shareholder and the ratepayer.

8 **INCENTIVE COMPENSATION – MGE'S NEW REBUTTAL ADJUSTMENT**

9 Q. Did MGE propose a new adjustment for incentive compensation in its rebuttal
10 testimony?

11 A. Yes. On pages 22-23 of Witness Noack's rebuttal testimony, MGE proposed a
12 new adjustment based on an estimate of \$1.522 million of incentive compensation. This is a
13 new adjustment that was not in the Company's direct filing or any subsequent update
14 supported by testimony. To date, MGE has not filed an update to its original case, nor did
15 MGE file a true-up case. MGE's direct filed rate case did not include this adjustment, and
16 because MGE has not updated its cost of service through Staff's update period through
17 September 30, 2013 or Staff' true-up period of December 31, 2013, MGE has no case that
18 supports this adjustment.

19 Similar to this new adjustment, MGE has also proposed a new corporate allocation
20 adjustment discussed elsewhere in this testimony. Recommending new adjustments that are
21 completely different in methodology in the rebuttal phase of testimony is contrary to the
22 normal rate case process and should be rejected by the Commission.

Surrebuttal Testimony of
Keith Majors

1 Q. Is MGE's \$1.5 million adjustment based on a "known and measurable"
2 expense?

3 A. No. MGE's new adjustment amount for incentive compensation does not meet
4 the standard of known and measurable costs. Staff only has the historical MGE incentive
5 compensation expense on which to base its adjustment. Any adjustment based on amounts
6 which are yet to be paid would be speculative and not known and measurable. MGE's
7 proposal goes months beyond the Operation of Law date in this case.

8 Q. MGE's new adjustment is based on Laclede Gas' incentive compensation
9 expense. Is this an appropriate comparison?

10 A. No. Staff has no evidence that the metrics for Laclede Gas' incentive program
11 will be similar to the program for MGE employees, and Staff only has anecdotal evidence that
12 MGE employees will be included in Laclede Gas' incentive program. Staff has requested but
13 not received projected payouts or any goals given to MGE employees. Witness Noack's new
14 adjustment is speculative and should be given no weight in determining incentive
15 compensation that should be paid by ratepayers in the cost of service.

16 **PENSIONS**

17 Q. Has Staff included in its revenue requirement recommendation an amount for
18 pension expense?

19 A. Yes. This topic has been addressed at Section VI. Rate Base, E. Pension
20 Tracker Asset/ Liability pp. 42-43, and Section VII. Income Statement, C.3. Pension Expense
21 pp. 67-74 in the Staff Report filed on January 29, 2014. There are two distinct expenses
22 related to pensions in the cost of service: 1) an expense related to prior pension tracker
23 mechanisms as described below; and 2) an allowance for ongoing pension expense, which

Surrebuttal Testimony of
Keith Majors

1 will be included in an ongoing pension tracker mechanism. Staff has reflected an amount for
2 pensions consistent with prior agreements reached in previous MGE rate cases outlined in the
3 *Stipulation and Agreement* (“2009 Stipulation”) in the 2009 Rate Case that addressed the
4 three pension amortizations relating to Case Nos. GR-2004-0209 (“2004 Rate Case”),
5 GR-2006-0422 (“2006 Rate Case”), and GR-2009-0355.

6 Also, Staff has reflected an amount in the revenue requirement calculation for Other
7 Post-Employment Benefits (OPEBs), commonly referred to as FAS 106 expense amounts.
8 This was addressed in the Staff Report at Section VII. Income Statement, C.4. Other Post-
9 Employment Benefits. pp. 74-78. The amount for OPEB’s is separate and distinct from
10 pension expense.

11 Q. Does MGE agree with how Staff calculated the pension expense in this case?

12 A. No. Company witness Michael R. Noack addresses MGE’s objection to Staff’s
13 pension calculation at pp. 23-24 of his rebuttal testimony. MGE is opposed to the calculation
14 made by Staff to reflect an over collection of pension amortization for prepaid pension assets
15 determined in the Company’s last rate case, Case No. GR-2009-0355. In that case, Staff
16 included amortizations for recovery of the prepaid pension assets determined in MGE’s 2004
17 Rate Case, the 2006 Rate Case, and the 2009 Rate Case.

18 Staff computed the pension expense and resulting prepaid pension asset/liability
19 amortization in this rate case—the 2014 Rate Case—using the total collected amortization
20 amounts for prepaid pension assets determined in the 2009 Rate Case that fully amortized
21 these assets. MGE opposes any consideration of the over collected amortization amounts
22 collected from customers during the time existing rates have been in effect. MGE instead
23 believes amounts collected in rates for expired amortizations should not be used to offset any

Surrebuttal Testimony of
Keith Majors

1 remaining outstanding pension assets. MGE believes these over collected pension
2 amortizations belong to the Company for whatever purposes it deems appropriate. Staff could
3 not disagree more with MGE's position on this point.

4 Q. What is a "tracker mechanism", as that term applies to ratemaking
5 methodology?

6 A. For ratemaking purposes, a tracker mechanism is an ongoing comparison of the
7 amount of an expense actually incurred by a utility to the amount of the same expense
8 reflected in the utility's rates. While tracker mechanisms are generally not appropriate for use
9 in setting rates, trackers for pension expenses are a unique exception because of the possibly
10 significant cash flow implications to utilities if their pension funding requirements are
11 materially different from their pension expense recovery levels in rates. Tracker mechanisms
12 provide rate recovery for the exact amount of an expense and are specifically designed to
13 consider increases and decreases to specific costs; in this instance, pensions. Ongoing tracker
14 mechanisms capture both under and over recoveries of an expense for reimbursement from or
15 return to ratepayers. The overall goal of a tracker mechanism, when properly exercised, is to
16 provide the utility with dollar-for-dollar recovery of reasonable and prudently incurred
17 expenses in the category covered, no more and no less.

18 Q. What are "vintages," as that term applies to tracker methodology?

19 A. A tracker captures the relationship between cash expenditures paid by a utility
20 and specific recovery of those expenditures in rates during a specific time period. From rate
21 case to subsequent rate case, under-recovery or over-recovery is captured into a regulatory
22 asset or regulatory liability, respectively, depending on what was included specifically in rates
23 for the expenditure and what the utility incurred for that expenditure. The specific time

Surrebuttal Testimony of
Keith Majors

1 periods are determined by cutoff periods in rate cases, and effective dates of new rates in
2 rate cases. These assets or liabilities are amortized to allow sufficient recovery in rates to
3 recover the pension costs and are referred to as “vintages,” “layers,” or “tiers.” Each vintage
4 is specially identified to ensure that each of the pension layers related to each rate case is
5 fully recovered.

6 Q. What is the difference between MGE’s pension tracker and Accounting
7 Authority Orders (AAOs)?

8 A. In most cases, an AAO represents a unique, infrequent, and extraordinary
9 expense incurred by a utility for which that utility requests deferral treatment of those costs
10 into a regulatory asset for possible future rate recovery. Utilities typically request the
11 Commission to approve AAOs outside the context of a rate case. Examples of expenses the
12 Commission has approved for AAO treatment include severe ice storms, catastrophic weather
13 events, changes in Commission rules that require utilities to incur additional costs such as for
14 environmental costs, and one-time costs for conversion of generating assets. Trackers, on the
15 other hand, are created in the context of a rate case and are rarely used.

16 While pension expenses are most definitely unique, they are not necessarily infrequent
17 or extraordinary. Historically, cash expenditures to the pension trusts and pension expense
18 can and have varied significantly from year to year. Market conditions, actual returns, and
19 cash expenditures are some of the variables that created the need for a pension tracker
20 mechanism first established for MGE in the 2004 Rate Case.

21 Q. Are tracker mechanisms appropriate for broad categories of expenses?

22 A. No. Pension expenses have unique attributes that reduce the amount of direct
23 control utility management has over these expenses. While management has some control of

Surrebuttal Testimony of
Keith Majors

1 the expenses, such as the asset mix of the pension trusts and negotiation of future benefits, the
2 investments in the pension trusts are subject to market forces, over which management has
3 little to no control.

4 Q. How did the current over collection situation for the pension amortizations
5 occur?

6 A. During the period rates which were determined in the 2009 Rate Case have
7 been in effect (from February 28, 2010—the effective date of rates, through the present time),
8 MGE began collecting a monthly amortization for the three prepaid pension assets. The
9 amortizations for the first two prepaid pension assets—referred to as Vintages 1 and 2—were
10 fully recovered in September 2011 and March 2012, respectively, yet rates did not change.
11 That is, once an asset’s amortization is included in the cost of service, the balance of that asset
12 is reduced ratably over the time of the amortization, and the Company continues to collect the
13 amortization even after the asset has been reduced to zero (fully recovered) until the next rate
14 case. As a result, MGE continued to collect from customers every month the same amount for
15 each of these amortizations. The third prepaid pension asset—Vintage 3 from the 2009 Rate
16 Case—continued its amortization beyond the end of the amortizations for Vintages 1 and 2.
17 Since the expired amortizations of Vintages 1 and 2 continued to be collected in rates, an over
18 collection occurred that should have been used by MGE to pay down the outstanding balance
19 of Vintage 3. However, MGE did not apply those over collected amortizations to the
20 Vintage 3 pension asset. In this rate proceeding, Staff determined the amount of the over
21 collections and applied that amount to the remaining pension amortizations pursuant to the
22 2009 Stipulation. During the period of the current rates, MGE fully collected from customers
23 all the pension amortization amounts. In fact, not only did MGE fully recover the prepaid

Surrebuttal Testimony of
Keith Majors

1 pension assets for each of the past three rate cases (the 2004, the 2006 and the 2009 rate
2 cases), the amortizations continue to be collected in rates and will do so until rates are
3 changed in the current rate case (in which rates are expected to change no later than
4 August 13, 2014). Thus, the over collection of the prepaid pension assets will continue until
5 the Commission approves new rates.

6 Q. How does MGE characterize Staff's position for the over collected
7 amortization amounts?

8 A. Witness Noack states at page 24 of his rebuttal testimony that MGE disagrees
9 with using any aspect of the over collected amortizations from customers in the pension
10 calculation in this case. Witness Noack states:

11 Q. What do you disagree with?

12
13 A. I do not agree with the Staff's attempt to create a
14 regulatory liability and apply negative amortization balances to
15 the 2004 and 2006 pension amortizations. The way these
16 amortizations were treated under the Stipulation and Agreement
17 approved by Commission in MGE's previous rate case, Case
18 No. GR-2009-0355, did not provide for negative amortizations
19 of their balances. Rather the balances were to be amortized to
20 zero, which they were. Staff's attempt to amortize those
21 balances past zero is a violation of the agreement approved by
22 the Commission in Case No. GR-2009-0355.

23
24 [Noack Rebuttal Testimony, Case No. GR-2014-0007, page 24]

25 According to Witness Noack, MGE believes it is improper to use any of the amortization
26 amounts that were specifically included in rates for a given "vintage" approved in the last rate
27 case for pension related costs to be used for the collection of any of the remaining outstanding
28 prepaid pension asset balances. Once an asset was fully recovered, MGE continued and still
29 continues to collect the monthly amortizations from customers because rates for natural gas
30 service did not change. MGE believes these monies—what Staff refers to as over collection

1 of pension amortizations—belonged to the Company instead of being used to “pay-down” the
2 remaining prepaid pension asset balance, Vintage 3.

3 Q. Does Staff agree with MGE’s interpretation of the 2009 Stipulation approved
4 by the Commission in the 2009 Rate Case regarding the prepaid pension asset amortizations?

5 A. No. The agreement reached with MGE in the last case was very clear
6 regarding how the pension costs were to be recovered in rates. This agreement required that
7 all amortizations of the prepaid pension assets be recovered through customer rates until those
8 amortizations were “eliminated” – that is, fully recovered. At page 10 of the 2009 Stipulation
9 (Paragraph 21), it was agreed to allow full recovery until the amortization of the balances was
10 complete: “Recovery in rates of the prepaid pension asset amortizations listed above shall
11 continue in subsequent rate cases as necessary until the asset balances are eliminated.” In the
12 2009 Stipulation there were three identified prepaid pension assets recognized as follows:

13 **Pensions (FAS87) and Other Post-Employment Benefits**
14 **(FAS106)**
15

16 20. The Parties agree that the rates established in this
17 case for Missouri Gas Energy, a division of Southern Union
18 Company (“Company”) for pension expense include an
19 allowance of \$10,000,000. Additionally, **the rates established**
20 **in this case include recovery of the amortization of prepaid**
21 **pension assets established in prior cases** and the amortization
22 of the prepaid pension asset established in this case as follows:
23

- 24 a. \$1,139,310 – GR-2004-0209;
25
26 b. \$803,300 – GR-2006-0422;
27
28 c. \$2,828,673 – GR-2009-0355
29

30 (All amounts above, including the \$10,000,000, are
31 stated prior to application of transfer rate.)
32

1 **21. Recovery in rates of the prepaid pension asset**
2 **amortizations listed above shall continue in subsequent rate**
3 **cases as necessary until the asset balances are eliminated.**
4

5 [*Stipulation and Agreement*, Case No. GR-2009-0355,
6 paragraph 20 & 21, pp. 9-10; emphasis added]

7 From the language in the 2009 Stipulation, the amortizations “shall continue” until all the
8 balances of the prepaid pension asset amortization were “eliminated” (fully recovered). It
9 cannot be clearer that the amortizations would continue until all of the balances were
10 “eliminated.”

11 Q. Does Staff believe the amortization amounts agreed to in the 2009 Rate Case
12 were for the purpose of only allowing recovery of pension costs?

13 A. Yes. Staff agreed to include amounts in rates to recover the pension costs
14 through an amortization for each of the three vintages. The recovery of pension costs,
15 specifically the prepaid pension assets, was determined by identifying the amounts included in
16 previous rate cases and comparing those to the remaining amortization balances. It was
17 determined those amortizations were enough to cover the amounts funded for pensions.
18 These amortizations for the prepaid pension assets, and any corresponding liabilities to the
19 extent they existed, were “earmarked” for the recovery of pension costs and only for pension
20 costs. This mechanism for recovering pension costs is referred to as a “pension tracker.”
21 Within a tracker mechanism, the amounts reflected in rates for pensions are not to be used for
22 any other purposes.

23 Q. How long has Staff used the pension tracking approach for rate purposes?

24 A. Staff has used pension tracking mechanisms for over ten years and for MGE
25 since the 2004 Rate Case. This rate mechanism was developed because of the difficulty of
26 predicting with accuracy the amount of pension costs that should be included in rates. Using

Surrebuttal Testimony of
Keith Majors

1 information to evaluate pension costs on a normalized basis in rates could result in an over or
2 under collection. To address this problem, Staff entered into agreements with most of the
3 major utilities in the state on some form of a pension tracker. This mechanism allowed
4 recovery in rates of the exact amount pension costs, tracking the amounts included in rates to
5 determine any over or under recoveries. In each rate case, a review of the over or under
6 recoveries would be performed to see if the recovery mechanisms were working and if
7 modifications needed to be made. A tracking device considers both cost increases as well as
8 cost decreases. In the example of pension costs, Staff would consider the funding
9 recommendations made by the utility company's actuary. The funding requirement for
10 pensions would be included in the rate recommendation made by Staff, taking into account
11 any amount of actual funding that was under or over the levels included in rates. If an amount
12 for pensions was actually funded at a higher level by the utility than what was included in
13 rates then that would result in a prepaid pension asset—reflected as a positive investment to
14 rate base and resulting in a positive amortization to expense. If the amount for pensions was
15 funded by the company at a lower level than was included in rates then this would result in a
16 prepaid pension liability—reflected as a negative offset amount reducing rate base and
17 resulting in a negative amortization to expense.

18 The amortizations would either be positive for pension assets— as was the case with
19 each of the three amortizations in MGE's 2004, 2006 and 2009 rate cases—or negative for
20 pension liabilities—which is what happened in the current case. The current amount collected
21 in rates has been greater than what was required to fund the pension costs, so the difference
22 has resulted in a prepaid pension liability that was reflected in the true-up case ending
23 December 31, 2013, filed on February 14, 2014, as part of Staff's supplemental direct filing.

Surrebuttal Testimony of
Keith Majors

1 Q. Please explain how Staff calculated its proposed amortization of prepaid
2 pension assets in this case.

3 A. Staff identified all the amounts collected in rates since the 2009 Rate Case.
4 There were three amortizations addressed in the 2009 rate case: Amortization 1 related to the
5 2004 Rate Case; Amortization 2 related to the 2006 Rate Case; and Amortization 3 related to
6 the 2009 Rate Case. The following table identifies each amortization amount and the initial
7 period covered for the amortizations:

8

MGE Rate Cases	Total Prepaid Pension Asset	Annual Amortization	Monthly Amortization	Amortization Period	Start of Amortization	End of Amortization
GR-2004-0209	\$7,975,181	\$1,139,310	\$94,943	7 years	October 2004	September 2011- fully recovered
GR-2006-0422	\$4,016,500	\$803,300	\$66,942	5 years	April 2007	March 2012- fully recovered
GR-2009-0355	\$14,143,364	\$2,828,673	\$235,723	5 years	March 2010	February 2015- fully recovered October 2013

9
10 In each rate case, the amortization amounts were determined to allow MGE full recovery in
11 rates. In the 2009 Rate Case, the amortization amounts were specifically identified at page 10
12 of the 2009 Stipulation agreed to by MGE and Staff and approved by the Commission.

13 Q. Witness Noack states at page 24, “Staff’s attempt to amortize those
14 balances past zero is a violation of the agreement approved by the Commission in Case No.
15 GR-2009-0355.” Do you believe MGE is correct in its view that the calculation made by
16 Staff regarding pensions is a “violation” of the 2009 Stipulation?

17 A. No. The agreement referred to by Witness Noack is the 2009 Stipulation. The
18 language in this agreement is quite clear—“recovery in rates of the prepaid pension asset

1 **amortizations** listed above **shall continue in subsequent rate cases as necessary until the**
2 **asset balances are eliminated**” (emphasis added). I do not believe this could be any more
3 plain—the recovery in rates “shall continue...until the asset balances are eliminated.” The
4 key phrase in this agreement is “balances are eliminated” – plural meaning all balances are
5 eliminated.

6 Staff witness Mark L. Oligschlaeger will also be addressing Staff’s view of the 2009
7 Stipulation in his surrebuttal testimony in this case.

8 Q. Would Staff have agreed to use pension trackers where the amortizations ended
9 and the utility company was allowed to keep the collected monies for itself?

10 A. No. The only condition under which Staff agreed to use the pension tracker
11 mechanism for MGE and other utilities was to allow dollar for dollar rate recovery of the
12 pension costs. This pension cost recovery mechanism exists solely for the purpose of
13 allowing companies like MGE to collect prudent and reasonable pension costs—no more, no
14 less. Staff would not have agreed to use this rate mechanism, nor continued its use,
15 if companies were able to use the amounts collected specifically for pension costs for
16 some other purposes. This is especially the case if utilities saw this as an opportunity to
17 enhance earnings through over collection of the amortizations simply by the timing of their
18 rate case filings.

19 The pension tracking mechanism was a ratemaking device that allowed for the
20 collection of prudent and reasonable pension costs on a dollar for dollar basis. It was
21 understood – or should have been understood—that any amounts collected under this tracker
22 mechanism would be used for pension costs. The pension tracking device allowed for the rate
23 recovery of the prepaid pension assets (positive) and liabilities (negative) with the expectation

Surrebuttal Testimony of
Keith Majors

1 that any amounts collected beyond the amortization amounts would be “tracked” for future
2 pension costs.

3 Certainly, the language in the 2009 Stipulation where the prepaid pension asset
4 amortizations “shall continue” until all the asset balances are “eliminated” was intended to
5 mean using all collected amortizations to pay-down any outstanding balances of
6 amortizations. As long as any of the prepaid pension assets contained an outstanding balance,
7 the amortization amounts collected in rates were to be used to reflect recovery of those
8 amortizations amounts. To do otherwise would allow MGE to reap windfalls through certain
9 over collections of pension amortizations in rates.

10 Q. Why do you believe MGE would get a windfall of over collections of pension
11 amortizations?

12 A. MGE, like any other utility, plans its rate cases when it believes a shortfall in
13 earnings exists, or is likely to exist in the near term. Whether they should or not, utilities
14 simply do not file for rate reductions. Companies like MGE analyze their operations and
15 project when they need to file for rate relief. It may be because of under earnings or because
16 of some regulatory requirement (such as when it requests recovery of its infrastructure system
17 replacement surcharge (ISRS) which has a finite period in which companies must file for
18 permanent rate relief). The timing of rate cases is largely driven by utilities and events that
19 cause a decline in earnings, not necessarily when pension amortizations expire. In fact, if a
20 company can refrain from asking for rate relief, it has a longer time to retain (keep) any
21 reduction in costs, assuming rates do not change. Because this is fundamental to ratemaking
22 theory, the pension trackers were intended to track all amortizations— positive and
23 negative—throughout the entire amortization period. Because rates do not change at the

Surrebuttal Testimony of
Keith Majors

1 expiration of the amortizations, as these amortizations become fully recovered—no
2 amortization amount remains to be collected from customers—they should be tracked as
3 negative amounts to be used in future pension cost calculations. To do otherwise results in
4 an unreasonable “profit” to the utility from a regulatory device that is intended to be
5 “earnings neutral.”

6 Under MGE’s view of the language of the 2009 Stipulation for the pension costs as
7 presented by Mr. Noack, it would be a virtual certainty that the Company would receive an
8 over collection of the amortization in rates for any expired pension amortization, since there
9 would not be a corresponding reduction in rates for the expired amortizations. There would
10 always be outstanding amortizations to include from rate case to rate case with individual
11 amortizations ending when fully recovered, but the Company would continue to collect those
12 expired amortizations in rates until the effective date of rates in the next rate case. That
13 simply is not what Staff contemplated when it started using the pension tracker mechanism.
14 Staff had no sense that MGE or any other company would use the fully recovered expiring
15 pension amortization to its advantage to “game” these over collections.

16 To the contrary, any amount of over collected monies from rates for the pension costs
17 were to be used for the recovery of the prepaid pension assets—not for some other purposes
18 such as the enhancement of MGE’s earnings. These over collected amortizations were to be
19 tracked to use for future pension costs (i.e., an advance payment of pension costs).

20 Q. Has MGE fully recovered all the prepaid pension amortizations established in
21 the 2009 Rate Case?

Surrebuttal Testimony of
Keith Majors

1 A. Yes. As of mid-November 2013 all three of the amortizations have been fully
2 recovered from customers—or as referred to in the 2009 Stipulation—the amortization
3 balances have been completely “eliminated.”

4 Q. Is MGE opposed to “tracking” any over collected pension amortizations?

5 A. According to Mr. Noack’s rebuttal testimony on page 24, the answer is yes,
6 although MGE is “willing to work with Staff and others to structure pension amortizations in
7 a different manner in this case on a going forward basis.” While MGE has made this
8 statement, to date, there has been no specific proposal offered by MGE in testimony to
9 account for the over collections of pension amortizations.

10 Even though the over collected amortizations paid in rates by customers for natural gas
11 service has allowed the Company to fully recover all the remaining outstanding prepaid
12 pension assets determined from the 2009 Rate Case, MGE is still seeking the further
13 collection of the amortization of what is referred to as Vintage 3 amortization. Using the
14 amortizations of the expired Vintage 1 (fully recovered September 2011) and Vintage 2 (fully
15 recovered March 2012), MGE received full recovery of Vintage 3 amortization at some point
16 in November 2013. In the 2009 Rate Case, the Vintage 3 amortization began February 28,
17 2010 (when rates went into effect for the 2009 Rate Case) and was calculated based on a five-
18 year amortization period which would be complete in February 2015. But because of the over
19 collection of the pension amortizations from Vintages 1 and 2, Vintage 3 was fully recovered
20 in November 2013—a year and half prior to February 2015. Yet despite this full recovery of
21 Vintage 3, MGE still wants customers to supply pension amortizations for this vintage over
22 and above the amount necessary for full recovery.

23 Q. What amounts are being collected in rates for the prepaid pension assets?

Surrebuttal Testimony of
Keith Majors

1 A. Established in the 2009 rate case, Staff included the following amounts for the
2 various vintages:

3

Vintages (or Tiers)	Monthly Amortization	Annual Amortization
Vintage 1	\$94,943	\$1,139,312
Vintage 2	\$66,942	\$803,300
Vintage 3	<u>\$235,723</u>	<u>\$2,828,673</u>
Total	\$397,608 monthly collection	\$4,771,285 annual collection

4
5 As of December 31, 2013, the end of the true-up in this case, customers had supplied
6 \$669,108 more than the total amortizations, by way of the over collection of Vintage 1 and
7 Vintage 2 offsetting the outstanding balance of Vintage 3. The table below shows the
8 calculation taking the over collections of Vintages 1 and 2 at December 31, 2013, offsetting
9 the balance of Vintage 3:

10

Balance of Vintage 3 at December 31, 2013	3,300,118
Over collection of Vintage 1 (October 2011 - December 2013)	(2,563,451)
Over collection of Vintage 2 (April 2012 - December 2013)	(1,405,775)
Net Over collection at December 31, 2013	\$ (669,108)

11
12 Assuming rates in this rate case go into effect August 13, 2014 (MGE filed its rate case
13 September 16, 2013), there would be seven and one-half months of additional over collected
14 amortizations from January 1, 2014 to August 13, or a total of \$2,982,060. The over
15 collection from mid-November 2013 through August 2014 is \$3,651,168 [\$669,108 plus
16 \$2,982,060]. These pension amortization amounts are summarized as follows:

1

	Months of Over Collection	Monthly Amortization	Amount of Over Collection Pension Amortization
Over collection from mid-November 2013 to December 31, 2013	1 ½ months	\$397,608 monthly collection for Tiers 1, 2 & 3	\$669,108
Over collection from January through mid-August 2014	7 ½ months	\$397,608 monthly collection for Tiers 1, 2 & 3	<u>\$2,982,060</u>
Total	9 months		\$3,651,168

2

3

Q. If MGE's position on pension amortizations is adopted, would this result in further over collections from customers?

4

5

A. Yes. In addition to the \$3.6 million over collection of the pension amortizations identified above through the effective date of rates, there will be further over collections if MGE's recommendation is approved by the Commission. MGE proposes to continue the amortization for Vintage 3, which has a monthly amortization of \$235,723. Even though the amortizations from the fully amortized Vintage 1 (fully amortized September 2011) and Vintage 2 (fully amortized March 2012) completed the recovery of Vintage 3 in mid-November 2013, MGE wants to continue the amortization of Vintage 3 in this case. Vintage 3 results in a \$2.8 million annual amortization amount collected from MGE customers. Because MGE cannot file for a rate case any earlier than October 1, 2015 based on the agreement reached in the MGE acquisition case (*Stipulation and Agreement*, Case No. GM-2013-0254, Section II, Paragraph 1, Rate Moratorium, page 7), the Vintage 3 amortization will continue to be collected in rates until at least September 1, 2016 (11 months after October 1, 2015). If the monthly amortization of \$235,723 is allowed to continue to be

17

Surrebuttal Testimony of
Keith Majors

1 collected in rates until September 1, 2016, this would result in further over collection of
2 pension amortizations from the 2009 Rate Case of \$5.7 million (\$5,657,352 equals \$235,723
3 multiplied 24 months from August 2014 until August 2016) in addition to the over collections
4 through August 2014:

	Months of Over Collection	Monthly Amortization	Amount of Over Collection Pension Amortization
Over collection from mid-November 2013 to August 2014 (effective date of rates GR-2014-0007)	9 months	\$397,608 monthly collection for Vintages 1, 2 & 3	\$3,651,168
Over collection from August 2014 to August 2016- 24 months	24 months	\$235,723 monthly collection for Vintage 3	\$5,657,352
Total	33 months		\$9,308,520

6
7 Thus, if MGE's position prevails on this issue, it will reap a tremendous windfall resulting
8 from over collection of amortizations that were fully recovered as of November 2013 through
9 the effective date of MGE's next rate case of September 1, 2016 of at least \$9.3 million.

10 Q. Is MGE required to file for a rate increase on October 1, 2015?

11 A. No. MGE can file no earlier than October 1, 2015 but can delay this filing
12 until required to do so for future ISRS cases. Generally speaking, utilities using the ISRS
13 mechanism cannot collect the ISRS for more than three years unless the utility has filed or is
14 the subject of a new general rate proceeding (reference 4 CSR 240-3.265 Paragraph 6). In the
15 rate case process, all other components of the revenue requirement calculation can be
16 considered. Assuming MGE decides to wait to file for a rate increase later than October 1,
17 2015, customers would continue to pay \$235,723 each and every month until rates are

Surrebuttal Testimony of
Keith Majors

1 changed unless the Commission rejects MGE's proposal. The annual amortization for
2 Vintage 3 is \$2.8 million.

3 For example, if MGE files its next rate case May 2017 instead of October 1, 2015,
4 rates would not change until April 2018— over three years past the original February 2015
5 calculation date for the Vintage 3 amortization (even though Vintage 3 was fully recovered as
6 of November 2013). The total over collection for the pension amortization would be in excess
7 of \$14.3 million, summarized as follows:

8

	Months of Over Collection	Monthly Amortization	Amount of Over Collection Pension Amortization
Over collection from mid-November 2013 to mid-August 2014 (effective date of rates GR-2014-0007)	9 months	\$397,608 monthly collection for Vintages 1, 2 & 3	\$3,651,168
Over collection from mid-August 2014 to mid-April 2018	44 months	\$235,723 monthly collection for Tier 3	<u>\$10,371,812</u>
Total	53 months		\$14,022,980

9

10 Q. Why was the May 2017 date used in the above example?

11 A. While Laclede Gas, owner of MGE, agreed to file its next rate case no sooner
12 than October 1, 2015 in the acquisition case, it could file later than this date. Laclede Gas also
13 agreed that its next rate case must also include a requested rate change for MGE. Laclede Gas
14 has filed an ISRS application January 17, 2014 which is projected to be completed May 17,
15 2014—120 days from the date filed which is the maximum length of time for the Commission
16 to review the ISRS filing. If the ISRS case is completed May 2014 then Laclede Gas would
17 be effectively required to file its next case, and that of MGE, no later than 3 years from that
18 point, or May 2017. Under this scenario, rates would not change until April 2018—11

1 months after the May 2017 rate filing. Unless the Commission rejects MGE’s proposal to
2 continue the Vintage 3 amortization, it would receive a substantial windfall from rates
3 collected for this pension amortization until rates change in the Company’s next rate case.
4 This windfall would occur each month from the point when the amortization was fully
5 recovered—mid-November 2013 to mid-April 2018—a period of 53 months. It is estimated
6 this over collection would result in an additional \$14 million collected in rates by MGE for
7 the prepaid pension amortization. MGE’s position would be to keep this entire amount as a
8 windfall profit to its bottom line.

9 Q. Did MGE understand that the treatment of pension expense authorized for it in
10 prior rate cases constituted use of a “tracker”?

11 A. Yes. Attached as Schedule KM-2 is the 2009 rebuttal testimony of MGE
12 Witness John A. Davis, who at that time was the Vice President and Controller of MGE.
13 Witness Davis makes the following statements concerning OPEBs (which are tracked
14 similarly to pensions), and the pension tracker mechanism:

15 **Q. WOULD A TRACKER MECHANISM, AS**
16 **PROPOSED IN THE STAFF’S TESTIMONY, BE A**
17 **MORE APPROPRIATE METHOD FOR RECOVERY OF**
18 **SFAS106 EXPENSES?**

19
20 A. Yes, a tracker mechanism that is based upon an agreed
21 to level of recovery in rates and an agreed to level of expense
22 for the Company would be the most appropriate was to ensure
23 amounts recovered through rates are reconciled back to the
24 amounts expensed per the books. The Company uses similarly
25 structured tracker mechanisms for its gas cost filings.

26
27 **PENSION EXPENSE**

28
29 **Q. HOW DOES MGE CURRENTLY TRACK**
30 **PENSION EXPENSES FOR PURPOSES OF RATE**
31 **RECOVERY?**
32

1 **A. The Company currently uses a “pension tracker”**
2 **that was established by stipulation in a prior rate case, GR-**
3 **2004-0209.**

4
5 [John A. Davis Rebuttal Testimony, Case No. GR-2009-0355,
6 pp 4-5, emphasis added]

7 Q. Witness Davis compares MGE’s pension tracker mechanism to the tracker
8 mechanism MGE has for its gas cost filings. What tracker mechanism does MGE have for its
9 gas cost filings?

10 A. MGE has in place a Purchased Gas Adjustment / Actual Cost Adjustment
11 (PGA/ACA) mechanism in place to recover its cost of purchased natural gas. This
12 mechanism involves periodic filings by the utility to set the amount of the gas costs on its
13 customer’s bills, along with later adjustments to true-up these amounts to reflect its actual
14 costs. Generally speaking, the PGA/ACA mechanism is designed for the Company to recover
15 its cost of purchased gas, subject to prudence reviews. The PGA/ACA mechanism **does not**
16 allow the Company to unduly gain from over collections of expenses from its customers.
17 Witness Davis drew an appropriate comparison of the pension tracker mechanism to the
18 existing PGA/ACA mechanism, which suggested that MGE understood exactly how the
19 mechanism worked. MGE’s pension tracker mechanism, similar to the PGA/ACA, should not
20 be used to gain windfalls from its customers.

21 **ON-GOING LEVELS OF PENSION COSTS FOR CASE NO. GR-2014-0007**

22 Q. What amount did Staff include for on-going pension costs in its revenue
23 requirement recommendation?

24 A. Staff included an updated amount of \$9.9 million for the on-going expense
25 level for pensions in this case. This \$9.9 million amount will be compared to what was

Surrebuttal Testimony of
Keith Majors

1 actually funded by MGE beginning with the effective date of rates in this case. Whether the
2 pension funding by the Company is higher or lower than this \$9.9 million amount will
3 determine if there is a prepaid pension asset or liability that would result in future
4 amortizations—positive if a pension asset or negative if a pension liability.

5 Staff included a negative \$5,483,060 amount -- (\$5.5 million) -- identified as a prepaid
6 pension liability related to the pension tracker authorized in the 2009 rate case for MGE's
7 ongoing pension expenses. This negative \$5.5 million amount is the basis for the start of a
8 negative amortization over 5 years resulting from the amount included as pension expense of
9 \$10 million from the 2009 Rate Case. This \$10 million was identified in the 2009 Stipulation
10 at page 9, paragraph 20. Staff compared the \$10 million amount of pension expense from the
11 2009 Rate Case to the actual funding levels made by MGE during the period since the 2009
12 rates were put in effect. This comparison identified that the amount of actual funding for
13 pensions was less than the \$10 million level included in rates. The negative (\$5.5 million)
14 difference from amount of actual funding to the \$10 million amount included in rates
15 collected from MGE customers is the basis for prepaid pension liability which then results in
16 the negative amortization over 5 years.

17 Q. Is there a dispute between MGE and Staff relating to the 2014 rate case
18 pension expense amount?

19 A. No. Staff does not believe there is any disagreement regarding the \$9.9 million
20 amount for the on-going pension future amount.

21 Q. Is there a dispute between MGE and Staff relating to the prepaid pension
22 liability of \$5.5 million determined in the 2014 rate case?

Surrebuttal Testimony of
Keith Majors

1 A. No. Staff does not believe there is any disagreement regarding the \$10 million
2 amount from the 2009 Rate Case, currently being collected in rates, that causes a negative
3 amortization for the prepaid pension liability of \$5.5 million.

4 Q. Witness Noack indicates a willingness to work with Staff to identify a different
5 approach to pension amortizations on a going forward basis. Does Staff agree to work with
6 MGE to come up with a different method for pension costs?

7 A. Yes. However, an important element from Staff's perspective would be to find
8 a solution to the over collected amounts of the amortizations. It is difficult to come up with a
9 solution to this problem when the Company and Staff have such fundamental differences on
10 what happened with the three prepaid pension amortizations. MGE has indicated that it "...is
11 not willing to change the prior agreement retroactively..." (page 24 of Noack rebuttal). Staff
12 has a completely different view of the language regarding the pension amortizations from the
13 2009 Stipulation as discussed above.

14 Witness Noack does indicate at page 24 of his rebuttal that MGE is willing to consider
15 changes to the pension amortizations that will alter the amortization of the 2009 rate case
16 amount. Mr. Noack states the following:

17 ...Rather than continue to have separate amortization balances
18 from each rate case, MGE is willing to roll the unamortized
19 prepaid pension balance from the 2009 rate case, at the time
20 rates go into effect, in with the current balance that has
21 accumulated since the 2009 rate case through the true-up period
22 of 12/31/13. MGE understands and accepts that the netting of
23 these two balances will result in regulatory liability which will
24 have a negative amortization balance.

25 [Noack Rebuttal Testimony, GR-2014-0007, page 24]
26

27 Staff does not believe this goes far enough. MGE will not accept the fact that an over
28 collection of the pension amortization started in September 2011 for Vintage 1 and March

1 2012 for Vintage 2 and that the over collection should be used to reduce the outstanding
2 balance of Vintage 3. Under the Company's approach, the amortization of Vintage 3 would
3 continue. I have addressed this earlier in my surrebuttal testimony. A substantial amount of
4 over collection will occur unless the Vintage 3 amortization is stopped in this rate case. MGE
5 is not proposing to do this. Consequently, Staff cannot reach an agreement with the Company
6 unless it is willing to consider the over collected amounts resulting from the pension
7 amortizations.

8 **RECOMMENDATIONS FOR PENSION COSTS**

9 Q. What are Staff's recommendations regarding pension costs?

10 A. Staff recommends the Commission adopt the following findings and
11 recommendations for pension costs:

- 12 • All regulatory assets (Vintage 1, 2, and 3) established in
13 the 2009 Stipulation were fully recovered from
14 customers as of November 2013;
- 15 • The pension tracker from the cutoff of the 2009 Rate
16 Case through December 31, 2013 (Vintage 4) is
17 established as a regulatory liability of \$(5,483,060).
18 This amount will be returned to customers over 5 years
19 beginning with the effective date of rates in this case;
- 20 • The amount of the excess over collections of Vintages 1,
21 2, and 3 at December 31, 2013 is established as a
22 regulatory liability of \$(669,108). This amount will be
23 returned to customers over 5 years beginning with the
24 effective date of rates in this case;
- 25 • The amortizations of Vintages 1, 2, and 3, which are
26 currently being collected in rates, will be tracked from
27 January 1, 2014 through the effective date of rates in this
28 case. The monthly amortizations of Vintages 1, 2, and 3
29 are as follows:

Surrebuttal Testimony of
Keith Majors

Vintage 1	\$94,943
Vintage 2	\$66,942
Vintage 3	\$235,723
Total Monthly Amortization	\$397,608

1
2 These amounts will be tracked as a regulatory liability
3 for return to customers in a future MGE rate case.

- 4
- 5 • MGE must track the amount currently in rates,
6 (\$10,000,000 from the 2009 Rate Case), compared to the
7 actual pension contributions from January 1, 2014
8 through the effective date of rates in this rate case. This
9 amount may be a regulatory asset or liability and will be
10 tracked for reimbursement from or return to customers
11 in a future MGE rate case.
 - 12 • \$9,920,720 (\$9.9 million) will be established for on-
13 going pension expense in this 2014 rate case. Beginning
14 with the effective date of rates, this amount will be
15 compared to the actual contributions to the pension
16 trusts. If the contributions are less than the amount in
17 rates, a regulatory liability will be created for the
18 difference, for future return to customers. If the
19 contributions are more than the amount in rates, a
20 regulatory asset will be created for the difference, for
future recovery from customers.

21 Q. Does conclude your surrebuttal testimony?

22 A. Yes, it does.

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of Missouri Gas Energy, Inc.'s)
Filing of Revised Tariffs to Increase its Annual) Case No. GR-2014-0007
Revenues for Natural Gas)

AFFIDAVIT OF KEITH MAJORS

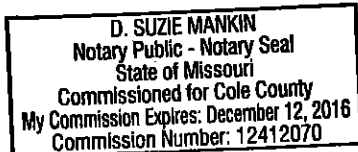
STATE OF MISSOURI)
)
COUNTY OF COLE) ss.

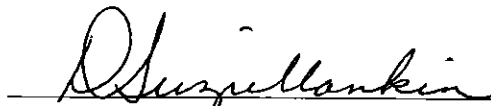
Keith Majors, of lawful age, on his oath states: that he has participated in the preparation of the foregoing Surrebuttal Testimony in question and answer form, consisting of 64 pages to be presented in the above case; that the answers in the foregoing Surrebuttal Testimony were given by him; that he 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.



Keith Majors

Subscribed and sworn to before me this 3rd day of April, 2014.





Notary Public

Missouri Public Service Commission

Respond Data Request

Data Request No.	0232
Company Name	Missouri Gas Energy (Laclede)-Investor(Gas)
Case/Tracking No.	GR-2014-0007
Date Requested	3/11/2014
Issue	Expense - Payroll
Requested From	Michael R Noack
Requested By	John Borgmeyer
Brief Description	MGE job positions added and eliminated
Description	1. Identify each and every job position added and eliminated for Missouri Gas Energy for the period a) January 1, 2014 through February 28, 2014 b) planned/ expected to be added and eliminated March 1, 2014 through April 30, 2014. Provide by job position, individual name and existing salary/ wage rates for each position added and eliminated. 2. Identify each and every employee who has received a promotion and demotion for Missouri Gas Energy for the period a) January 1, 2014 through February 28, 2014 b) planned/ expected promotion and demotion from March 1, 2014 through April 30, 2014. Provide job position for each promotion and previous job position, individual name and existing salary / wage rates. Provide job position for each demotion and previous job position, individual name and existing salary / wage rates. DR requested by Keith Majors (Keith.Majors@psc.mo.gov).
Response	With respect to OPC Data Request 232, MGE objects to this data request as it seeks the discovery of information which is irrelevant, immaterial and inadmissible in GR-2014-0007, and which discovery is not reasonably calculated to lead to the production of relevant and admissible evidence in GR-2014-0007.. Without waiving its objections to this data request, MGE refers Staff to the monthly reports related to staffing that it has provided pursuant to its obligations under GM-2013-0254.
Objections	NA

The attached information provided to **Missouri Public Service Commission** Staff in response to the above data information request is accurate and complete, and contains no material misrepresentations or omissions, based upon present facts of which the undersigned has knowledge, information or belief. The undersigned agrees to immediately inform the **Missouri Public Service Commission** if, during the pendency of Case No. **GR-2014-0007** before the Commission, any matters are discovered which would materially affect the accuracy or completeness of the attached information. If these data are voluminous, please (1) identify the relevant documents and their location (2) make arrangements with requestor to have documents available for inspection in the **Missouri Gas Energy (Laclede)-Investor(Gas)** office, or other location mutually agreeable. Where identification of a document is requested, briefly describe the document (e.g. book, letter, memorandum, report) and state the following information as applicable for the particular document: name, title number, author, date of publication and publisher, addresses, date written, and the name and address of the person(s) having possession of the document. As used in this data request the term "document(s)" includes publication of any format, workpapers, letters, memoranda, notes, reports, analyses, computer analyses, test results, studies or data, recordings, transcriptions and printed, typed or written materials of every kind in your possession, custody or control or

within your knowledge. The pronoun "you" or "your" refers to **Missouri Gas Energy (Laclede)-Investor(Gas)** and its employees, contractors, agents or others employed by or acting in its behalf.

Security : Public
Rationale : NA

Missouri Public Service Commission

Respond Data Request

Data Request No.	0233
Company Name	Missouri Gas Energy (Laclede)-Investor(Gas)
Case/Tracking No.	GR-2014-0007
Date Requested	3/11/2014
Issue	Expense - Payroll
Requested From	Michael R Noack
Requested By	John Borgmeyer
Brief Description	Laclede Gas job positions added and eliminated
Description	Identify each and every job position eliminated and added for Laclede Gas Company and The Laclede Group for the period from March 31, 2013-- the end of the update period in Laclede Gas' last rate case, Case No. GR-2013-0171-- to February 28, 2014 and planned to be eliminated and added from March 1 through April 30, 2014. List by individual, job position and salary / wage rates and date of employment. DR requested by Keith Majors@psc.mo.gov
Response	With respect to OPC Data Request 233, MGE objects to this data request as it seeks the discovery of information which is irrelevant, immaterial and inadmissible in GR-2014-0007, and which discovery is not reasonably calculated to lead to the production of relevant and admissible evidence in GR-2014-0007. Without waiving its objections to this data request, MGE refers Staff to the monthly reports related to staffing that it has provided pursuant to its obligations under GM-2013-0254.
Objections	NA

The attached information provided to **Missouri Public Service Commission** Staff in response to the above data information request is accurate and complete, and contains no material misrepresentations or omissions, based upon present facts of which the undersigned has knowledge, information or belief. The undersigned agrees to immediately inform the **Missouri Public Service Commission** if, during the pendency of Case No. **GR-2014-0007** before the Commission, any matters are discovered which would materially affect the accuracy or completeness of the attached information. If these data are voluminous, please (1) identify the relevant documents and their location (2) make arrangements with requestor to have documents available for inspection in the **Missouri Gas Energy (Laclede)-Investor(Gas)** office, or other location mutually agreeable. Where identification of a document is requested, briefly describe the document (e.g. book, letter, memorandum, report) and state the following information as applicable for the particular document: name, title number, author, date of publication and publisher, addresses, date written, and the name and address of the person(s) having possession of the document. As used in this data request the term "document(s)" includes publication of any format, workpapers, letters, memoranda, notes, reports, analyses, computer analyses, test results, studies or data, recordings, transcriptions and printed, typed or written materials of every kind in your possession, custody or control or within your knowledge. The pronoun "you" or "your" refers to **Missouri Gas Energy (Laclede)-Investor(Gas)** and its employees, contractors, agents or others employed by or acting in its behalf.

Security :	Public
Rationale :	NA

Missouri Public Service Commission

Respond Data Request

Data Request No.	0234
Company Name	Missouri Gas Energy (Laclede)-Investor(Gas)
Case/Tracking No.	GR-2014-0007
Date Requested	3/11/2014
Issue	Expense - Payroll
Requested From	Michael R Noack
Requested By	John Borgmeyer
Brief Description	MGE and Laclede Gas terminations
Description	1. Identify all individuals who have been given notice of termination/ separation from Missouri Gas Energy division to be effective during the period January 1, 2014 through December 31, 2014 providing when this termination / separation took place/ is to take place. Identify by job position, individual name and existing salary/ wage rates. 2. Identify all individuals who have been given notice of termination/ separation from Laclede Gas Company to be effective during the period January 1, 2014 through December 31, 2014 providing when this termination / separation took place/ is to take place. Identify by job position, individual name and existing salary/ wage rates. DR requested by Keith Majors (Keith.Majors@psc.mo.gov).
Response	With respect to OPC Data Request 234, MGE objects to this data request as it seeks the discovery of information which is irrelevant, immaterial and inadmissible in GR-2014-0007, and which discovery is not reasonably calculated to lead to the production of relevant and admissible evidence in GR-2014-0007. Without waiving its objections to this data request, MGE refers Staff to the monthly reports related to staffing that it has provided pursuant to its obligations under GM-2013-0254.
Objections	NA

The attached information provided to **Missouri Public Service Commission** Staff in response to the above data information request is accurate and complete, and contains no material misrepresentations or omissions, based upon present facts of which the undersigned has knowledge, information or belief. The undersigned agrees to immediately inform the **Missouri Public Service Commission** if, during the pendency of Case No. **GR-2014-0007** before the Commission, any matters are discovered which would materially affect the accuracy or completeness of the attached information. If these data are voluminous, please (1) identify the relevant documents and their location (2) make arrangements with requestor to have documents available for inspection in the **Missouri Gas Energy (Laclede)-Investor(Gas)** office, or other location mutually agreeable. Where identification of a document is requested, briefly describe the document (e.g. book, letter, memorandum, report) and state the following information as applicable for the particular document: name, title number, author, date of publication and publisher, addresses, date written, and the name and address of the person(s) having possession of the document. As used in this data request the term "document(s)" includes publication of any format, workpapers, letters, memoranda, notes, reports, analyses, computer analyses, test results, studies or data, recordings, transcriptions and printed, typed or written materials of every kind in your possession, custody or control or within your knowledge. The pronoun "you" or "your" refers to **Missouri Gas Energy (Laclede)-Investor(Gas)** and its employees, contractors, agents or others employed by

or acting in its behalf.

Security : Public
Rationale : NA

Exhibit No.: _____
Issues: SFAS 106
Pension Tracker
Mechanism
Witness: John A. Davis
Sponsoring Party: Missouri Gas Energy
Case No.: GR-2009-0355
Date Testimony Prepared: September 28, 2009

MISSOURI PUBLIC SERVICE COMMISSION

MISSOURI GAS ENERGY

CASE NO. GR-2009-0355

REBUTTAL TESTIMONY OF

JOHN A. DAVIS

Jefferson City, Missouri

September 2009

REBUTTAL TESTIMONY OF

JOHN A. DAVIS

CASE NO. GR-2009-0355

SEPTEMBER 2009

INDEX TO TESTIMONY

	Page <u>Number</u>
1. SFAS 106/OPEBS ISSUE.....	2
2. PENSION EXPENSE.....	4

REBUTTAL TESTIMONY OF

JOHN A. DAVIS

CASE NO. GR-2009-0355

September 2009

1 **Q. WOULD YOU PLEASE STATE YOUR NAME AND BUSINESS ADDRESS?**

2 A. My name is John A. Davis, and my business address is 3420 Broadway, Kansas City,
3 Missouri 64111.

4

5 **Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?**

6 A. I am the Vice President, Controller of Missouri Gas Energy (“MGE” or “Company”), a
7 division of Southern Union Company.

8

9 **Q. PLEASE DESCRIBE YOUR EDUCATIONAL BACKGROUND.**

10 A. I received a BBA in 1987 with concentrations in both Finance and Accounting from The
11 University of Texas at Austin. I also received an MBA from the University of Texas at
12 Austin in December 2003.

13

14 **Q. PLEASE DESCRIBE YOUR PROFESSIONAL BACKGROUND.**

15 A. I began my career with Arthur Andersen as a staff auditor in 1988 in Houston, Texas. In
16 1991 I received my certification as a Certified Public Accountant. In 1992 I left Arthur
17 Andersen as an experienced senior auditor and moved to Austin to work for Southern
18 Union as a corporate accountant. I worked for Southern Union in various capacities

1 including financial reporting, gas accounting, customer billing and general ledger
2 accounting and finally as controller for the Southern Union Gas division in Austin, Texas
3 until it was sold in 2002. In 2003 I was controller of Energy Worx, a subsidiary of
4 Southern Union Company until I accepted the controller position at Missouri Gas Energy,
5 a division of Southern Union Company.

6
7 **Q. WHAT IS THE PURPOSE OF THIS TESTIMONY?**

8 A. I will respond to portions of the Staff Report- Cost of Service regarding the Company's
9 treatment of Other Post-Employment Benefits ("OPEBs") under the Statement of
10 Financial Accounting Standards No. 106 ("SFAS106") as well as Office of the Public
11 Counsel ("OPC") witness Ted Robertson's direct testimony on this issue. I will also
12 respond to Staff's comments on MGE's pre-paid pension asset and pension tracker
13 language from the Staff Report – Cost of Service, which begins on p. 56.

14
15 **SFAS 106/OPEBS ISSUE**

16
17 **Q. HOW DO YOU ADDRESS TESTIMONY THAT THE COMPANY FAILED TO
18 PROPERLY FUND ITS EXTERNAL TRUST FUND MECHANISMS FOR OPEBS
19 CALCULATED ACCORDING TO SFAS 106 (PAGES 6 AND 94 OF THE STAFF
20 REPORT AND PAGE 3 OF OPC WITNESS ROBERTSON'S DIRECT
21 TESTIMONY)?**

22 A. First, I have been advised by counsel that – contrary to the assertions of the Staff and
23 OPC witness Robertson – the Missouri statute on the topic of SFAS106, as applicable to
24 MGE, does not require any particular funding level.

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23

Second, the Company recognized the proper amounts pertaining to SFAS106 related obligations on its books according to the actuarial reports provided by the Company’s actuary. In other words, the Company has consistently booked a liability for each dollar that is owed to the Trust Fund in accordance with SFAS 106. The basis for the actuarial analysis is described in the testimony and attached schedules sponsored by MGE witness Michael Muth. The expense and liability of OPEBs have been - and continue to be - presented in conformity with Generally Accepted Accounting Principles (“GAAP”) and are subjected to external audit each year by the Company’s outside auditors, Pricewaterhouse Coopers. Additionally, OPEBs are funded to the external trust fund mechanism as these benefits are required to be paid regardless of what the level of rate relief might be received.

Third, although MGE has not funded the full extent of its SFAS 106 liability, it is not at all clear how much the Company has received in rates, which makes it difficult to compare that to the amount which was funded. In other words, in some rate cases the amount of SFAS 106 being included in rates is known, but in the case of GR-2001-292 which was a total “black box” settlement the money that MGE received from customers to pay for operating expenses has not been earmarked as to how much was intended to be applied toward OPEBs. Moreover, in most years, MGE’s actual earnings fell short of its Commission-authorized level such that all of its costs, including SFAS 106 costs, were being under-recovered to some degree. It appears that both the Staff and OPC ignore this situation.

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23

Q. IS IT ACCURATE TO SUGGEST THAT THE COMPANY RECEIVED EXACTLY \$23.7 MILLION IN RATES PERTAINING TO SFAS106 BENEFITS?

A. No. As stated previously in my rebuttal testimony, some rate cases are “black box” settlements and a number is not attached to a particular expense or rate base item. In the most recent cases, the Commission did not specify the level of recoveries pertaining to SFAS106 benefits in the Report and Order because there was no difference in the Staff reconciliation of the issues between Company and Staff for SFAS 106 expense. Therefore, it is difficult to ascertain what specific amount is theoretically recovered in rates.

Q. WOULD A TRACKER MECHANISM, AS PROPOSED IN THE STAFF’S TESTIMONY, BE A MORE APPROPRIATE METHOD FOR RECOVERY OF SFAS106 EXPENSES?

A. Yes, a tracker mechanism that is based upon an agreed to level of recovery in rates and an agreed to level of expense for the Company would be the most appropriate way to ensure amounts recovered through rates are reconciled back to the amounts expensed per the books. The Company uses similarly structured tracker mechanisms for its gas cost filings.

PENSION EXPENSE

Q. HOW DOES MGE CURRENTLY TRACK PENSION EXPENSES FOR PURPOSES OF RATE RECOVERY?

1 A. The Company currently uses a “pension tracker” that was established by stipulation in a
2 prior rate case, GR-2004-0209.

3

4 **Q. DO YOU HAVE ANY PROPOSED CHANGES TO THE CURRENT PENSION**
5 **TRACKER LANGUAGE?**

6 A. Yes, in response to Staff’s testimony filed in its Staff Report-Cost of Service on this
7 issue, Staff and MGE engaged in discussions regarding possible revisions to MGE’s
8 current pension tracker mechanism. MGE would agree to the following revised language
9 to the pension tracker mechanism:

10 1. The parties agree that the rates established in this case for MGE include an
11 allowance of \$10,000,000 for pension expense, exclusive of the amortizations of
12 the prepaid pension asset and tracker mechanism regulatory assets/liabilities. (All
13 amounts are stated prior to the transfer rate.) The Company shall be authorized to
14 record as a regulatory asset/liability, as appropriate, the difference between the
15 pension expense used in setting rates and pension expense as recorded for
16 financial reporting purposes as determined in accordance with GAAP pursuant to
17 FAS 87 and FAS 88 (or such standard as the FASB may issue to supersede,
18 amend or interpret the existing standards), and that such difference shall be
19 subject to recovery from or return to customers in future rates. The difference
20 between the amount of pension expense included in MGE’s rates and the amount
21 funded by MGE shall be included in the Company’s rate base in future rate
22 proceedings.

23
24 2. The Company shall be allowed rate recovery for contributions it makes to its
25 pension trust that exceed the ERISA minimum for the purpose of avoiding
26 Pension Benefit Guarantee Corporation (PBGC) variable premiums. Additional
27 contributions made pursuant to this paragraph will increase MGE’s rate base by
28 increasing the prepaid pension asset and/or reducing the accrued liability, and will
29 receive regulatory treatment as described in paragraph 1 of this Agreement. MGE
30 shall inform the Staff and Public Counsel of contributions of additional amounts
31 to its pension trust funds pursuant to this Paragraph in a timely manner.

32
33 3. The provisions of FAS 158 require certain adjustments to the prepaid pension
34 asset and/or accrued liability with a corresponding adjustment to equity (i.e.,
35 decreases/increases to Other Comprehensive Income). The Company will be
36 allowed to set up a regulatory asset/liability to offset any adjustments that would
37 otherwise be recorded to equity caused by applying the provisions of FAS 158 or

1 any other FASB statement or procedure that requires accounting adjustments to
2 equity due to the funded status or other attributes of the pension plan. The parties
3 acknowledge that the adjustments described in this paragraph will not increase or
4 decrease rate base.
5

6 4. Due to the Pension Protection Act of 2006 (PPA), MGE may be required to
7 make contributions in excess of the ERISA Minimum amount in order to avoid
8 benefit restrictions under the PPA. Such contributions will be examined in the
9 context of future rate cases and a determination will be made at that time as to the
10 appropriate and proper level recognized for ratemaking as a Net Prepaid Pension
11 Asset.
12

13 **Q. DOES THIS CONCLUDE YOUR REBUTTAL TESTIMONY?**

14 **A.** Yes, at this time.