

Exhibit No.:

Issue: Incentive Awards

Witness: Janis E. Fischer

Sponsoring Party: MoPSC Staff

Type of Exhibit: Supplemental Surrebuttal Testimony

Case No.: ER-2001-299

Date Testimony Prepared: June 1, 2001

MISSOURI PUBLIC SERVICE COMMISSION

UTILITY SERVICES DIVISION

SUPPLEMENTAL SURREBUTTAL TESTIMONY

OF

JANIS E. FISCHER

THE EMPIRE DISTRICT ELECTRIC COMPANY

CASE NO. ER-2001-299

Jefferson City, Missouri

June 2001

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

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Exhibit No. 113
Date 6-04-01 Case No. ER-2001-299
Reporter KS

1 **SUPPLEMENTAL SURREBUTTAL TESTIMONY**

2 **OF**

3 **JANIS E. FISCHER**

4 **THE EMPIRE DISTRICT ELECTRIC COMPANY**

5 **CASE NO. ER-2001-299**

6 Q. Please state your name and business address.

7 A. Janis E. Fischer, 3675 Noland Road, Suite 110, Independence, Missouri
8 64055.

9 Q. Are you the same Janis E. Fischer who has previously filed direct, rebuttal
10 and surrebuttal testimony in this case?

11 A. Yes, I am.

12 Q. What is the purpose of your supplemental surrebuttal testimony?

13 A. The purpose of my supplemental surrebuttal testimony is to relate the
14 Staff's position that the \$323,000 of test year Incentive Awards of The Empire District
15 Electric Company (Empire or Company) should not be recovered in cost of service.

16 Q. Why is it necessary for the Staff to state its position related to this issue
17 subsequent to the filing of the Staff's surrebuttal testimony?

18 A. At the time of the surrebuttal testimony filing on May 17, 2001, the Staff
19 was still awaiting the receipt of responses to Staff Data Requests Nos. 330 and 331,
20 which were issued on May 8, 2001 and May 14, 2001, respectively. The Staff did not
21 want to definitively determine whether to include or exclude from Empire's cost of
22 service the \$323,000 of test year Incentive Awards without the additional information
23 requested from Empire.

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1 Q. Please describe the information requested in Staff Data Request Nos. 330
2 and 331.

3 A. The Staff issued Data Request No. 330 to obtain information concerning
4 the accounting treatment given by Empire to accrued Incentive Award costs in the year
5 2000, the test year for this case. (This Data Request response was received on May 18,
6 2001.) The Staff asked in Data Request No. 331 for specific documentation of goals for a
7 number of Empire's eligible employees to assess the criteria upon which the Incentive
8 Awards are typically based. (This Data Request response was received on May 25, 2001)

9 Q. What prompted the Staff's data requests in May, 2001 for additional
10 information from Empire pertaining to the Incentive Awards?

11 A. Empire did not to provide the Staff with information concerning Incentive
12 Awards in its responses to several data requests, which the Staff believes Empire should
13 have referenced the Incentive Awards in its answers. The Staff submitted Data Request
14 No. 139 on December 27, 2000 requesting the following information:

15 Please provide the amount of Discretionary Compensation
16 Awards budgeted in 1997, 1998, 1999, and 2000. Also
17 provide a list of awards presented since January 1, 1999
18 indicating 1) the recipient, b) a description of the performance
19 being recognized, c) actual dollar amount of award,
20 d) accounting treatment for these awards on Empire's books
21 and records, and e) quantify the benefit to the ratepayer of the
22 idea or performance being recognized.

23 The response to Staff Data Request No. 139 was received on January 9,
24 2001. (The Highly Confidential response to Staff Data Request No. 139 is attached as
25 Schedule 1.) The response from Empire did not include the \$323,000 Incentive Awards
26 or any indication that the Incentive Awards program existed. The Staff submitted
27 Supplemental Data Request No. 139 on March 7, 2001 and received the response from

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1 Empire on March 19, 2001. The supplement asked for Empire to update the response for
2 Discretionary Compensation Awards budgeted for 2001 and paid to Empire employees
3 for year 2000 performance in the year 2001. (The Highly Confidential response to Staff
4 Supplemental Data Request No. 139 is attached to my Rebuttal Testimony as
5 Schedule 1.) The response to the Supplemental Staff Data Request from Empire did not
6 include the \$323,000 Incentive Awards or any reference to the Incentive Awards plan.

7 Q. Does Empire have any other incentive plans for its employees?

8 A. Yes. Empire also has a Management Incentive Plan (MIP) that pertains to
9 the vice presidents and chief elected officer of the Company, and the "Lightning Bolts"
10 program for which all Empire non-union permanent full-time employees are eligible.
11 Both of these programs are discussed in my direct testimony.

12 Q. When did the Staff first become aware of the incentive plan at issue?

13 A. Although the Staff was aware of other incentive compensation programs
14 in use by Empire, the Staff first became aware of the Incentive Awards program during
15 the prehearing conference in this case, which was held April 16-19, 2001. After
16 discussions with the Company on the Incentive Awards program, the Staff submitted data
17 requests to obtain information it would normally have requested and reviewed during the
18 course of the onsite audit of Empire. In response to Staff Data Request No. 318 issued on
19 April 20, 2001, and received by me on May 10, 2001, Empire provided its
20 "Employee Handbook," which describes the Incentive Award Plan, and a listing of
21 Empire employees that had received the Incentive Awards for the years 1996 through
22 2000. The Employee Handbook indicates that employees are required to attain certain
23 goals in order to qualify for the Incentive Awards. After receiving the response to Staff

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1 Data Request No. 318, the Staff issued Data Request No. 331 to obtain necessary
2 information about specific details of the operation of the program. The details sought by
3 the Staff involved the individual goals set for Empire employees that received the
4 Incentive Awards during the test year.

5 Q. Should the Incentive Award Plan information have been provided to Staff
6 as part of the original Staff Data Request No. 139 issued in December 2000?

7 A. Yes. By not providing this information as part of its response to Staff
8 Data Request No. 139, the Staff was unable to review the information regarding the
9 Incentive Award Plan while the Staff was conducting its field audit at Empire. Not
10 providing this information put the Staff at a distinct disadvantage and directly resulted in
11 the late submission of the data requests and, ultimately, in the Staff not addressing this
12 issue until its rebuttal and surrebuttal testimony.

13 Q. Please describe in detail the information that you requested from Empire
14 in response to Data Request No. 331.

15 A. I requested the base objectives and the incentive or "stretch" objectives
16 used to determine the granting of Incentive Awards for the years 1996 through 2000 for
17 twelve named employees. Base objectives are used to determine employees' eligibility
18 for certain merit/cost of living salary increases. Incentive goals are used to determine
19 employees' eligibility for the Incentive Awards at issue in this case. From discussions
20 with Empire personnel, it was indicated that information concerning base and "stretch"
21 goals is maintained in personnel files for each individual employee. These twelve
22 employees were selected from the Incentive Awards 2000 list provided in Empire's
23 response to Staff Data Request No. 318. I selected employees from various departments,

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1 job locations and salary ranges, in an attempt to capture diverse aspects of a wide range
2 of individuals. While ideally I would have sought to review the individual base and
3 incentive objectives that had been set for more Empire employees, the small amount of
4 time remaining prior to the filing of surrebuttal testimony and the evidentiary hearing of
5 this case influenced my decision to limit my review to twelve specific employees.

6 Q. Please describe the information received from Empire in response to Staff
7 Data Request No. 331.

8 A. Empire provided the forms used to process the Incentive Awards program
9 for the employees requested and included the following statement in its response to Staff
10 Data Request No. 331:

11 **

23 **

24 Q. Is the Staff at this time able to make a determination whether to include
25 the \$323,000 associated with the test year Incentive Awards based upon the information
26 provided?

27 A. Yes. The fact that Empire did not require managers nor supervisors to
28 complete objectives for employees for the test year 2000, yet ultimately issued the
29 Incentive Awards to virtually all eligible employees, demonstrates that Empire did not

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1 adhere to its own Incentive Award Plan as outlined in the Employee Handbook, and also
2 did not meet the Commission's criteria for allowing rate recovery of incentive
3 compensation amounts.

4 Q. Based on Empire's response to Staff Data Request No. 331, respecting the
5 twelve employees which you selected, how many were given "base" and "stretch" goals
6 in the Year 2000?

7 A. Of the four employees named in Empire's response to Staff Data Request
8 No. 331 as having received goals and objectives for the test year, in actuality only three
9 had goals set in the Year 2000. In documentation in that response, it is shown that the
10 year 2000 Performance, Compensation & Career Development Review form for the
11 Incentive Awards program was used for the employee **____** but there is an
12 explanation that no goals were set for this employee for 2000. On the second page of this
13 form, the supervisor comments ** _____
14 _____
15 _____

**

16 Q. What are the criteria that the Staff relied upon to make the determination
17 of whether these Incentive Awards should be included in cost of service?

18 A. As stated in my surrebuttal testimony, the Staff applied the criteria
19 established by the Commission in Case No. EC-87-114, a Staff excess earnings complaint
20 case against Union Electric Company. The Commission Report and Order to this case
21 states as follows:

22 At a minimum, an acceptable management performance plan
23 should contain goals that improve existing performance, and
24 the benefits of the plan should be ascertainable and reasonably
25 related to the incentive plan.

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1 Q. Does the Incentive Awards program for the test year meet the
2 Commission's criteria as stated above?

3 A. No. The absence of goals/objectives for the individual Empire employees
4 does not meet the Commission's criteria of improved performance because, without pre-
5 set goals, performances cannot reasonably be judged to have "improved". In addition, if
6 goals are not known in advance by the employees, any improvement in Company
7 performance that may have occurred cannot be identified as related to the incentive plan.

8 More generally, the Staff believes that incentive compensation costs are
9 not appropriate from a ratemaking perspective if utility employees are not even aware of
10 the criteria on which compensation will be ultimately based. Unfortunately, this was
11 largely true of Empire during the test year.

12 Q. How does the Staff evaluate the part of Empire's response to Staff Data
13 Request No. 331 in which it was stated that the Incentive Awards were paid in
14 February 2001 based on the role employees played in maintaining the organization
15 through the merger process?

16 A. ** _____
17 _____ ** Improved job
18 performance would be demonstrated by exceeding the results achieved in prior years.

19 Second, the proposed UtiliCorp United, Inc. (UtiliCorp) merger was
20 entered into voluntarily by the directors and shareholders of Empire. The burdens thrust
21 upon the Company because of that decision were not unforeseeable, but accepted as a
22 consequence of the merger. The shareholders of Empire would have benefited from the
23 merger as a result of the merger premium offered by UtiliCorp for the Empire common

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1 stock. It is not known whether benefits to ratepayers would have resulted if the UtiliCorp
2 merger had been completed. **

3
4 **

5 Q. What is the Staff's position on what party should be responsible for
6 merger costs?

7 A. As expressed in its testimony filed in Case No. EM-2000-369, UtiliCorp's
8 and Empire's Joint Application to the Commission for merger approval, the Staff's
9 position is that any costs associated with the merger of Empire and UtiliCorp should not
10 be included in the cost of service to Missouri ratepayers. This view appears to be
11 consistent with that of Empire witness Myron W. McKinney, who stated in his direct
12 testimony in this rate case, on page 5, lines 15-20 that it is Empire's intention that no
13 expenses related to the merger are to be included for rate recovery.

14 In addition to not meeting the Commission's express criteria for
15 authorizing rate recovery of incentive compensation, the Incentive Awards paid out in
16 February 2001 should not be borne by ratepayers because the costs are attributable to the
17 Empire/UtiliCorp merger. Merger costs should be borne by shareholders and recorded
18 below-the-line by Empire.

19 Q. Has the Staff reviewed the base and "stretch" goals issued to Empire
20 employees for the years 1996 through 2000 that were included in Empire's response to
21 Staff Data Request No. 331?

22 A. Yes. In general, the Staff's review of the individual employee incentive
23 goals issued for the Year 2000, as well as for the years 1996 through 1999, for twelve

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1 employees generally indicates that the Incentive Awards plan in prior years also would
2 not have met the Commission's rate recovery criteria for incentive compensation. The
3 reasons for the Staff's position follow:

4 First, Incentive Award goals are repeated from one year to the next for
5 individual employees without any additional requirement to demonstrate an improvement
6 from the prior year. In one case, an employee had five goals listed as stretch goals for
7 Year 2000 that were identical to the stretch goals listed in 1996 through 1999, Empire
8 employee ** ____ **.

9 Second, many Incentive Award goals are not quantifiable, so it is difficult
10 to objectively determine whether improvement in performance has occurred. An
11 example of an Incentive Award that is not quantifiable is ** ____
12 ____ ** This
13 goal does not provide a way to measure Company morale before or after the year the goal
14 was set. A ** ____ ** is hard to measure or quantify.

15 Third, some of the Incentive Award goals appear to mirror base goals that
16 are derived from the basic job requirements. Incentive goals that are similar to basic job
17 requirements do not truly "stretch" employee performance. An example of this problem
18 is the stretch goal ** ____ ** The
19 same employee had a "base goal" of ** ____ ** Clearly this is an example
20 where the incentive goal is not "stretching" the employee to improve beyond what would
21 normally be required of all employees. In addition, the example cited above for
22 ** ____ ** would not appear to be "stretch" employee performance.
23 Employees should be expected to display positive attitudes in the performance of their

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1 job duties in order to provide a positive work environment and to promote excellence in
2 work product.

3 Finally, some employees received Incentive Awards when the Incentive
4 goals were not met. An example appears in 1998 of an employee, **_____** having
5 four incentive goals but only meeting expectations for one goal with the other three goals
6 not having been met. In addition, certain employees received Incentive Awards for the
7 year 2000 even though they had not been employed by Empire for a full year. The
8 Employee Handbook indicates that workers employed by Empire for less than a full year
9 are not eligible to receive Incentive Awards.

10 Q. Does this conclude your supplemental surrebuttal testimony?

11 A. Yes, it does.

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SCHEDULE 1

HAS BEEN DEEMED

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IN ITS ENTIRETY

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