

Exhibit No.:

Issues: Payroll; Payroll Taxes; Incentive
Compensation; Employee Benefits;
and Fuel Inventories

Witness: Graham A. Vesely

Sponsoring Party: MoPSC Staff

Type of Exhibit: Direct Testimony

Case No.: ER-2001-672

Date Testimony Prepared: December 6, 2001

MISSOURI PUBLIC SERVICE COMMISSION
UTILITY SERVICES DIVISION

DIRECT TESTIMONY

FILED³

DEC 6 2001

OF

Missouri Public
Service Commission

GRAHAM A. VESELY

UTILICORP UNITED INC.
d/b/a MISSOURI PUBLIC SERVICE

CASE NO. ER-2001-672

Jefferson City, Missouri
December 2001

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GRAHAM VESELY
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d/b/a MISSOURI PUBLIC SERVICE
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1 **DIRECT TESTIMONY**
2 **OF**
3 **GRAHAM VESELY**
4 **MISSOURI PUBLIC SERVICE**
5 **A DIVISION OF UTILICORP UNITED**
6 **CASE NO. ER-2001-672**

7 Q. Please state your name and business address.

8 A. Graham Vesely, Noland Plaza Office Building, 3675 Noland Road,
9 Suite 110, Independence, MO 64055.

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

11 A. I am a Regulatory Auditor for the Missouri Public Service Commission
12 (Commission).

13 Q. Please describe your education background.

14 A. In May of 1985, I received a Bachelor's degree in Civil Engineering from
15 Saint Martins College, Olympia, Washington. In May of 1998, I completed an MBA
16 degree with a focus in Accounting from Central Missouri State University, Warrensburg,
17 Missouri. I am a Certified Public Accountant with a permit to practice in Missouri.

18 Q. Please describe your employment history.

19 A. In May of 1985, I was employed as a Facilities Maintenance Engineer by
20 the United States Air Force. From March 1988 until May 1995, I was employed by the
21 Army Corps of Engineers as a member of a construction management group. At that
22 time, I began working with the engineering firm of Malsy & Associates, Lincoln,

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1 Missouri, as a Civil Engineer. On February 26, 1999, I began my current employment
2 with the Commission.

3 Q. What is the nature of your duties while in the employ of this Commission?

4 A. I am responsible for assisting in the audits and examinations of the books
5 and records of utility companies operating within the state of Missouri.

6 Q. With reference to Case No. ER-2001-672, have you made an investigation
7 of the books and records of Missouri Public Service (MPS), a division of UtiliCorp
8 United Inc. (UCU or Company) relating to the proposed rate application?

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

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

12 A. I am responsible for payroll expense, payroll taxes, incentive
13 compensation, employee benefits , and the rate base component of fuel inventories.

14 **PAYROLL EXPENSE**

15 Q. Please explain the payroll adjustments you are sponsoring.

16 A. As Staff Accounting witness Phillip K. Williams explains, in his direct
17 testimony, the Staff is filing a calendar year 2000 test year updated for known and
18 measurable events through June 30, 2001. I have therefore developed the normalized
19 MPS payroll expense by annualizing payroll costs at June 30, 2001 for all MPS/UCU
20 departments. This approach takes into consideration actual numbers of employees, as
21 well as authorized wages paid as of June 30, 2001.

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1 After determining the reasonableness of doing so, I have also included an
2 allowance for overtime and other so-called "other than standard" labor costs by including
3 them at the test year level.

4 Because a scheduled two percent union wage increase went into effect on
5 October 1, 2001, I reflected its impact although it took place after the known and
6 measurable period. Further, in my payroll expense calculation, the Staff estimated a pay
7 raise (3.98%) for employees of Enterprise Support Function (ESF) departments.
8 According to the Company, this increase is scheduled for January 1, 2002, which is
9 within the true-up period ending January 31, 2002.

10 Q. Why has the Staff included an estimate for payroll increases through
11 January 31, 2002 in cost of service?

12 A. The Company requested a true-up audit in order to capture significant new
13 items through January 31, 2002. The Commission authorized a true-up in this case, as
14 discussed in the direct testimony of Staff witness Williams. The estimated wage
15 increases included in Staff's direct filing will be updated to reflect MPS's actual wage
16 increases with actual employees through January 31, 2002 during the true-up audit.

17 Q. Please list the adjustment numbers you are sponsoring to include the effect
18 of the payroll annualization process discussed above.

19 A. I am sponsoring adjustments: S-13.3, S-14.1, S-16.1, S-17.1, S-20.1,
20 S-21.1, S-22.1, S-23.1, S-24.1, S-25.3, S-27.1, S-28.1, S-30.1, S-31.1, S-32.1, S-36.3,
21 S-37.3, S-38.3, S-39.3, S-40.2, S-41.3, S-43.3, S-45.1, S-46.3, S-47.3, S-48.3, S-49.3,
22 S-50.3, S-51.3, S-52.3, S-53.2, S-54.2, S-55.1, S-56.3, S-57.1, S-58.4, S-60.1, S-61.3,

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1 S-62.3, S-63.3, S-64.3, S-65.1, S-66.1, S-67.3, S-68.3, S-69.3, S-70.3, S-71.3, S-73.3,
2 S-74.3, S-75.3, S-76.3, S-77.3, S-78.3, S-79.3, S-81.3, S-90.3, and S-91.3.

3 Q. How did you account for the payroll costs of UtiliCorp corporate
4 departments and other business units that provide service to MPS?

5 A. These costs have been allocated to MPS using an appropriate allocation
6 factor arrived at by Staff Accounting witness Charles R. Hyneman.

7 Q. Please list the adjustment numbers you are sponsoring to reflect the
8 payroll effects of the Staff including the St. Joseph Light and Power division into UCU's
9 corporate allocation pool.

10 A. I am sponsoring adjustments: S-13.5, S-14.2, S-16.2, S-17.2, S-20.3,
11 S-21.3, S-22.4, S-23.4, S-24.3, S-25.4, S-27.2, S-28.2, S-30.3, S-31.4, S-32.3, S-36.5,
12 S-37.5, S-38.5, S-39.5, S-40.3, S-41.5, S-43.5, S-45.3, S-46.6, S-47.7, S-48.7, S-49.6,
13 S-50.5, S-51.5, S-52.5, S-53.3, S-54.4, S-55.2, S-56.5, S-57.2, S-58.6, S-60.3, S-61.6,
14 S-62.6, S-63.7, S-64.7, S-65.3, S-66.3, S-67.6, S-68.7, S-69.5, S-70.5, S-71.6, S-73.5,
15 S-74.5, S-75.5, S-76.5, S-77.5, S-78.5, S-79.4, S-81.4, S-90.5, and S-91.5.

16 Q. Please list the adjustment numbers you are sponsoring to reflect the
17 payroll effects of the Staff's changes to UCU's allocation methodology.

18 A. I am sponsoring adjustments: S-13.8, S-14.5, S-16.4, S-17.4, S-20.5,
19 S-21.5, S-22.7, S-23.7, S-24.4, S-25.11, S-27.4, S-28.4, S-30.5, S-31.6, S-32.7, S-36.9,
20 S-37.11, S-38.10, S-39.8, S-40.5, S-41.10, S-43.10, S-45.7, S-46.11, S-47.11, S-48.11,
21 S-49.11, S-50.10, S-51.8, S-52.10, S-53.9, S-54.9, S-55.6, S-56.10, S-57.6, S-58.11,
22 S-60.7, S-61.11, S-62.11, S-63.13, S-64.11, S-65.7, S-66.7, S-67.11, S-68.12, S-69.8,

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S-70.10, S-71.12, S-73.10, S-74.8, S-75.9, S-76.8, S-77.9, S-78.8, S-79.8, S-81.8, S-90.8,
and S-91.8.

INCENTIVE COMPENSATION

Q. Please explain what is meant by incentive compensation.

A. Incentive compensation is additional compensation, above base wages/salary, that employees receive if certain pre-set *goals* are met.

Q. What is the nature of Staff's review in auditing this area?

A. Among other things, the Staff's audit scope includes a review of the goals of the plan and a determination as to who benefits by achieving the goals and, therefore, who should pay for achieving the goals. Historically, the Staff has recommended that ratepayers pay for progress made towards accomplishing goals of improving safety and/or controlling costs, and that goals intended to improve the Company's earnings /rate of return should be assigned to shareholders.

Q. Has the Commission previously expressed policies concerning appropriate rate treatment of incentive compensation plans?

A. Yes. In the Report And Order issued in Case Nos. TC-89-14, et al., Southwestern Bell Telephone Company (SWB), the Commission stated:

In the Commission's opinion the results of the parent corporation, unregulated subsidiaries, and non-Missouri portions of SWB, are only remotely related to the quality of service or the performance of SWB in the state of Missouri. Achieving the goals of SBC [the parent company] and unregulated subsidiaries is too remote to be a justifiable cost of service for Missouri ratepayers. Accordingly, the Staff's proposed disallowances in the senior management's long term and short term incentive plans...should be adopted.

Q. Has the Commission elsewhere addressed its policy concerning incentive compensation plans?

1 A. Yes. In the Report And Order issued pursuant to Case Nos. TC-93-224,
2 et. al., SWB, the Commission reiterated its position expressed in Case No. TC-89-14, and
3 accepted the Staff's proposed disallowances of both short-term and long-term incentive
4 costs. In particular, with regard to the long-term plan, the Commission stated:

5 The structure of the plan provides an implicit incentive for
6 participants to try to increase SBC's stock price. This in turn
7 could encourage senior managers to spend a greater percentage of
8 time on non-regulated companies and discourage time and effort
9 spent on Missouri operations...The likelihood of SBC managers
10 emphasizing whatever they perceive will cause the market to react
11 favorably to SBC stock, including giving priority to unregulated
12 subsidiaries, further convinces the Commission that Missouri
13 ratepayers should not fund the long term incentives.

14 Q. What types of incentive compensation plans does the Company have?

15 A. The Company has an Annual (short-term) Incentive Plan, and an
16 Executive Long-Term Incentive Plan.

17 **Annual Incentive Plan**

18 Q. What is the purpose of the Annual Incentive Plan?

19 A. UCU's response to the Staff's Data Request No. 88 (Supplemental A)
20 identifies the purpose as follows:

21 **PURPOSE**

22 The purpose of the UtiliCorp United ("UCU" or "UtiliCorp")
23 Annual Incentive Plan is to reward the accomplishments of
24 business goals set by UCU and to motivate participants to
25 accomplish significant business group and individual goals.
26 Achievement of these goals will further enhance UCU's mission to
27 create shareholder value by providing superior energy solutions for
28 our customers. The following guidelines outline the
29 implementation policies and procedures for the Plan document
30 approved by the Board.

31 Incentives are tailored to meet specific needs of each organization.
32 This requires separate descriptions. Participants will receive a
33 separate attachment explaining the Plan implementation applicable

1 to a specific job or organization. If you have any questions, please
2 contact your supervisor, local Employee Relations Representative,
3 or the Compensation Department.

4 Q. Which UtiliCorp employees are covered by the Annual Incentive Plan?

5 A. Continuing, from UCU's response to the Staff's Data Request No. 88
6 (Supplemental A), eligibility is identified as follows:

7 **ELIGIBILITY**

8
9 Company employees are eligible under the Plan unless they are in
10 one of the following groups, as determined by UCU management:

- 11
12 • Sales employees participating in a commission plan
13 • Employees participating in a separate annual bonus/incentive
14 plan
15 • Employees covered by a collective bargaining agreement
16 • Employees working under contract or hired in a temporary
17 position

18 Q. How are incentive payments determined under the Annual Incentive Plan?

19 A. Incentive payments are made based on achievement of three separate
20 components:

- 21 1. UCU Financial Goals
22 2. Business Group/Department Goals
23 3. Team/Individual Goals.

24 Q. What do the above goals consist of?

25 A. The UCU financial goal specifies achieving a certain earning per share
26 (EPS) level. The business group goal specifies achieving a certain earnings level. The
27 team/individual goals aim to increase productivity by focusing on specific work
28 improvement at a hands-on level for the particular employee.

29 Q. Were incentive payments charged to MPS in the Company's case for
30 achieving financial goals of a business group or unit of UCU?

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1 A. Yes. Incentive payments made for achieving an earnings goal of
2 UtiliCorp Energy Delivery (UED) were included in the Company' case. The Company
3 describes UED as the business unit that encompasses all of UCU's electric and gas
4 delivery activities nationwide.

5 Q. Is the Staff recommending any disallowance of payments made under the
6 Annual Incentive Plan?

7 A. Yes. The financial goals of achieving a certain level of parent company
8 (UCU) earnings per share (EPS), and the UED financial goal of reaching a certain
9 earnings level, closely meet the Commission's reasons for disallowance cited in Case
10 No. TC-89-14 and TC-93-224. The financial results of UCU's multinational operations,
11 as well as those of UED's interstate operations are too remotely affected by MPS's
12 Missouri operations to justify recovery from Missouri ratepayers. Therefore, the Staff
13 proposes an adjustment to reduce the annualized level of incentive compensation by all
14 the payments made for UCU and UED financial goals.

15 Q. Have you included in the cost of utility service incentive payments made
16 for achieving goals that relate to improved MPS utility service?

17 A. Yes. The Staff is not recommending any disallowances of annual
18 incentive payments made for team/personal goals of improving work performance.

19 Q. Please list the adjustment numbers you are sponsoring to reflect the Staff's
20 partial disallowance of annual incentive payments.

21 A. I am sponsoring adjustments: S-13.6, S-14.3, S-16.3, S-17.3, S-20.4,
22 S-21.4, S-22.5, S-23.5, S-25.5, S-27.3, S-28.3, S-30.4, S-31.5, S-32.4, S-36.6, S-37.6,
23 S-38.6, S-39.6, S-40.4, S-41.6, S-43.6, S-45.4, S-46.7, S-47.8, S-48.8, S-49.7, S-50.6,

S-51.6, S-52.6, S-53.4, S-54.5, S-55.3, S-56.6, S-57.3, S-58.7, S-60.4, S-61.7, S-62.7,
S-63.8, S-64.8, S-65.4, S-66.4, S-67.7, S-68.8, S-69.6, S-70.6, S-71.7, S-73.6, S-74.6,
S-75.6, S-76.6, S-77.6, S-78.6, S-79.5, S-81.5, S-90.6, and S-91.6.

Long-Term Executive Incentive Plan

Q. Please describe the Long-Term Executive Incentive Plan.

A. UCU's response to the Staff's Data Request 88 identified UCU's Long-Term Executive Incentive Plan components as follows:

PURPOSE

The UtiliCorp United (UCU) Executive Long-Term Incentive Plan is designed to share and reward long-term success of significant business goals set by UCU management and to motivate participants to achieve goals which lead to increased total return to shareholders. The achievement of these goals enables the Company to continue to provide outstanding service to its ratepayers and other customers while enhancing the value of the Company for its shareholders.

ELIGIBILITY

Participation is limited to a select group of executive management designated by the CEO and President and approved by the Compensation Committee of the UCU Board of Directors (Compensation Committee). The designation of the executive management group is based on the executive's significant impact upon the long-term growth and profitability of UCU.

PERFORMANCE OBJECTIVE

The Performance Objective is based on UCU's Total Shareholder Return (TSR) over a three-year period, which will be measured and ranked against the TSR performance of a key group of 12 energy and utility companies over the same period. The key group was selected based on recognition as:

- A member of UCU's Peer Group;
- One of UCU's major competitors; and/or
- A Best Practice company that UCU should emulate and try to exceed

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1 TSR has two components: change in the price of UCU's common
2 stock, and dividends paid for a designated period. There are
3 several steps involved in calculating TSR for a cycle.

4 The first step is to determine the net change in stock price over the
5 period. The beginning stock price is the average price of a share of
6 UCU common stock in the December immediately preceding the
7 beginning of the performance cycle. The ending stock price is the
8 average share price for the last month of the performance cycle.
9 The difference between these two values is the net change.

10 The second step is to add together the dividends paid on a share of
11 UCU common stock for this same performance period.

12 Finally, add together the net change in stock price and dividends
13 paid and divide that total by the average stock price at the
14 beginning of the performance cycle. This percent is the total return
15 to shareholders for this period, and is the number that is ranked
16 against the TSR for the key comparator group that serves the
17 performance measure under this plan.

18 Q. Has the Staff proposed any disallowances of the Long-Term Executive
19 Incentive Plan payments?

20 A. This plan is a clear-cut example of incentives to achieve goals that benefit
21 shareholders. Shareholders, through their representatives on the Board of Directors, are
22 at liberty to make arrangements they consider to promote their financial interest. As it is,
23 this plan does not meet previously cited Commission standards for rate recovery; thus the
24 Staff has made an adjustment to remove all amounts booked by MPS under this plan.

25 Q. Please list the adjustment number you are sponsoring to reflect the Staff's
26 disallowance of the Long-Term Executive Incentive Plan.

27 A. Adjustment S-85.5 reflects this disallowance.

28 **PAYROLL TAXES**

29 Q. Please explain your adjustment S- related to payroll taxes.

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1 A. This adjustment serves to ensure the appropriate level of Social Security
2 (FICA), medicare, state unemployment (SUTA), and federal unemployment (FUTA)
3 taxes associated with the Staff's annualized payroll are included in rates.

4 Q. Please briefly explain how you computed the correct level of payroll taxes.

5 A. From the historical record it is possible to determine a ratio of each payroll
6 tax to payroll expense during the test year. Applying these ratios to the current
7 annualized level of payroll expense produces the best available estimate of payroll taxes
8 on a going forward basis.

9 **EMPLOYEE BENEFITS**

10 Q. Please describe your adjustment S- 85.10 related to 401(k) benefits?

11 A. The 401(k) benefits matching expense incurred by MPS in the test year
12 represents a certain percentage of base payroll. I have maintained this same percentage,
13 but multiplied it by the Staff's annualized level of payroll to produce the Staff's 401(k)
14 benefit level. The difference between this and the test year level gives rise to my
15 adjustment

16 Q. Please describe adjustment S-85.11 reflecting the Staff's annualization of
17 health and dental benefits.

18 A. MPS employees may opt between coverage under either a health
19 maintenance organization (HMO), or the Company-sponsored preferred provider
20 organization (PPO) plan. In either case, health and dental costs are shared between
21 employer and employees. Employees who waive all coverage are given a \$570
22 allowance in their cafeteria plan to be used for covered items. The Staff's adjustment

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reflects the difference between annualized employer costs and those incurred in the test year.

Q. Please list employee benefits charged to MPS that you are recommending be included in cost of service, exclusive of disallowances previously discussed.

Resource Code	Staff Annualization Description	MPS Juris Electric Expense
1709	401K Employer Share	1,556,023
1711	Employee Stock Contribution Plan (ESCP)	706,957
1715	Benefits Health and Dental	2,174,418
1716	Benefits Life Insurance	94,795
1717	Benefits Educational Reimbursement	24,222
1718	Benefits AD&D Insurance	21,336
1725	Benefits Supplemental Retirement	34,688
1726	Benefits Restricted Stock	30,199
1727	Benefits LT & ST Disability	64,094
1729	Benefits Great Pursuits	50,079
1799	Benefits Other	127,434
	Annual Incentive Compensation	1,678,752
	Union Incentive Compensation	138,664
	Total	7,601,660

A. The Staff has included in its filed case the incentives and benefits levels shown above, on an annualized basis, allocated as appropriate to electric operations, without further proposed disallowances.

FUEL INVENTORIES

Q. What was your responsibility in this case with regard to the determination of fuel inventory levels?

A. My responsibility was to determine an estimate of an appropriate level of inventories for coal and oil maintained at UtiliCorp's generating facilities. Coal inventories are maintained at the Jeffrey Energy Center and the Sibley plant. Oil inventories are maintained at the Nevada and Greenwood facilities.

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1 Q. What inventory levels has the Staff included in this case for UtiliCorp's
2 generating facilities?

3 A. The Staff has included a 61-day supply for coal inventories at the Sibley
4 plant, and a 72-day supply at Jeffrey. The numbers of days are consistent with the
5 inventory policies of both Sibley and Jeffrey generating facilities. The inventory tonnages
6 represent coal quantities sufficient for the respective number of average-burn days, as per
7 the results of the generation levels determined using the production cost model. A 13-
8 month average has been used for oil inventories for purposes of this case.

9 Q. Does this conclude your direct testimony.

10 A. Yes, it does.

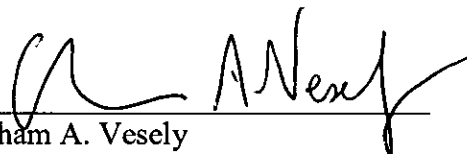
BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of the Application of the Tariff)	
Filing of Missouri Public Service (MPS))	
A Division of UtiliCorp United Inc., to)	Case No. ER-2001-672
Implement a General Rate Increase for Retail)	
Electric Service Provided to Customers in the)	
Missouri Service Area of MPS)	

AFFIDAVIT OF GRAHAM A. VESELY

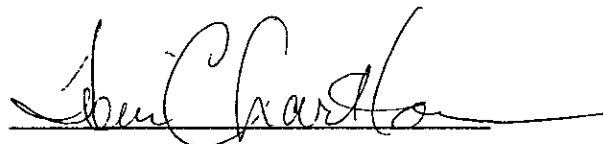
STATE OF MISSOURI)	
)	ss.
COUNTY OF COLE)	

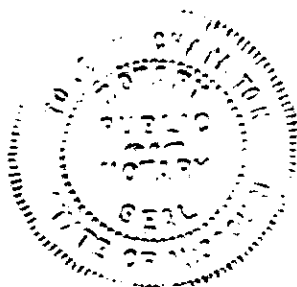
Graham A. Vesely being of lawful age, on his oath states: that he has participated in the preparation of the foregoing Direct Testimony in question and answer form, consisting of 13 pages to be presented in the above case; that the answers in the foregoing Direct Testimony were given by him; that he 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.



Graham A. Vesely

Subscribed and sworn to before me this 5th day of December 2001.





TONI M. CHARLTON
NOTARY PUBLIC STATE OF MISSOURI
COUNTY OF COLE
My Commission Expires December 28, 2004