

Exhibit No. _____

Issue:

Witness: Myron W. McKinney

Type of Exhibit: Supplemental Surrebuttal Testimony

Sponsoring Party: Empire District

Case No.: *ER-2001-299*

Date Prepared: June 4, 2001

**Before the Public Service Commission
of the State of Missouri**

SUPPLEMENTAL SURREBUTTAL TESTIMONY

OF


MYRON W. MCKINNEY

FILED
JUN 4 2001
Missouri Public
Service Commission

AFFIDAVIT


STATE OF MISSOURI)
) ss
COUNTY OF JASPER)

On the 4th day of June, 2001, before me appeared Myron W. McKinney, to me personally known, who, being by me first duly sworn, states that he is the President and Chief Executive Officer of The Empire District Electric Company and acknowledged that he has read the above and foregoing document and believes that the statements therein are true and correct to the best of his information, knowledge and belief.



Myron W. McKinney

Subscribed and sworn to before me this 4th day of June, 2001.



Notary Public

My commission expires:

DORIS K. ADAMS
NOTARY PUBLIC - NOTARY SEAL
STATE OF MISSOURI
COUNTY OF COLE
My Commission Expires May 20, 2002

Exhibit No.: _____
Issue: Incentive Pay
Witness: Myron W. McKinney
Type of Exhibit: Supplemental Surrebuttal Testimony
Sponsoring Party: The Empire District Electric Company
Case No.: ER-2001-299
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SUPPLEMENTAL SURREBUTTAL TESTIMONY
OF
MYRON W. MCKINNEY
THE EMPIRE DISTRICT ELECTRIC COMPANY
BEFORE THE
MISSOURI PUBLIC SERVICE COMMISSION
CASE NO. ER-2001-299

1 Q. PLEASE STATE YOUR NAME.

2 A. Myron W. McKinney.

3 Q. ARE YOU THE SAME MYRON W. MCKINNEY WHO PREVIOUSLY FILED
4 DIRECT, REBUTTAL, AND SURREBUTTAL TESTIMONY IN THIS CASE?

5 A. Yes, I am.

6 Q. WHAT IS THE PURPOSE OF YOUR SUPPLEMENTAL SURREBUTTAL
7 TESTIMONY?

8 A. The purpose of this testimony is to respond to the supplemental surrebuttal testimony of
9 Staff witness Janis E. Fischer regarding Staff's position that \$323,000 of test year (total
10 Company) Incentive Awards should not be recovered in the cost of service.

11 Q. IN MS. FISCHER'S SUPPLEMENTAL SURREBUTTAL TESTIMONY SHE STATES
12 THAT EMPIRE DID NOT PROVIDE STAFF WITH INFORMATION CONCERNING
13 INCENTIVE AWARDS. HOW DO YOU RESPOND?

14 A. There was no intention on Empire's part to fail to provide the data requested.

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1 Empire has a long history of working in a cooperative manner with the Staff to provide
2 complete and full information which enables the Staff to perform its audit responsibilities
3 in the most efficient way possible. Empire has always been forthcoming with whatever
4 information was requested to the best of our ability and knowledge. We have never
5 attempted to conceal or fail to provide information in response to a Staff data request.

6 Q. ARE YOU PERSONALLY FAMILIAR WITH STAFF DATA REQUEST NO. 139?

7 A. Yes, I am. The request asked for Discretionary Compensation Awards budgeted in 1997,
8 1998, 1999, and 2000, and information regarding recipients, dollar amounts, accounting
9 treatment, and ratepayer benefits. Upon receiving the data request, I looked back to an
10 identical Staff data request in the Company's 1997 rate case (Case No. ER-97-81) to
11 determine precisely how this request had been handled in that case. The data we supplied
12 in response to Staff data request No. 139 in this case was consistent with the information
13 we supplied in the prior case which, to the best of my knowledge, had been entirely
14 acceptable; however, I believe a matter of terminology has perhaps confused the matter.

15 Q. WOULD YOU PLEASE DEFINE THE PAYROLL TERMS WHICH MIGHT HAVE
16 LED TO THIS CONFUSION?

17 A. Yes. For non-bargaining unit, non-officer employees, there are three separate
18 components of compensation.

19 1. Merit Increases are adjustments to an employee's pay based on the job value for his or
20 her position and the contribution they have made to the business. Merit Increases are
21 awarded annually, are permanent increases to base salary, and are tied to the value of the
22 job as determined through a surveying process to insure that the Company's pay practices

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1 are in line with industry, state and local values. Once an employee reaches job value,
2 there is no method to receive additional base compensation unless the value of the job
3 increases.

4 2. Incentive Awards (which are at issue) are a part of Empire's Pay for Performance Plan
5 ("the Plan") under which lump sum awards are made for meeting or exceeding incentive
6 objectives. Incentive awards are made annually to employees who have met certain
7 "stretch" objectives. These are one-time payments which do not add to the employee's
8 base salary. In order to receive an Incentive Award, the employee must achieve the goals
9 for the year in question.

10 3. Discretionary Awards are one-time payments made each year at the discretion of the
11 CEO from a fund approved by the Board of Directors. Discretionary Awards are
12 commonly known in the Company as "Lightning Bolts". They are typically paid for
13 work on a special project or special effort, or for overall outstanding performance.
14 Discretionary awards have been paid since 1988. The total amount of these payments
15 have ranged from \$1500 in 1988 to \$89,200 in 1999. In the test year in this case, 32 such
16 payments totalling \$28,000 were made. While the Company considers these payments to
17 be an important part of the total compensation program, it has agreed not to contest
18 Staff's disallowance of these amounts in this case.

19 Q. WHAT INFORMATION WAS PROVIDED IN THIS CASE RESPONSE TO STAFF
20 DATA REQUEST NO. 139?

21 A. The listing of Discretionary Awards as requested and as provided in prior cases. The
22 \$323,000 at issue here are not Discretionary Awards, but rather are Incentive Awards.

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1 Q. WHAT IS YOUR UNDERSTANDING OF WHETHER OR NOT THE STAFF HAD
2 BEEN AWARE OF THE INCENTIVE AWARDS PRIOR TO THIS CASE?

3 A. My understanding is that the Staff had been aware of the Incentive Awards from its work
4 in prior cases.

5 Q. PLEASE EXPLAIN.

6 A. As I mentioned, the Incentive Awards were included in the Company's 1997 case and,
7 while that case resulted in a stipulated settlement, Staff work papers in that case indicate
8 the inclusion of Incentive Payroll, so the Incentive Awards should not have been a new
9 item to Staff.

10 Q. ON PAGE 4 OF HER SUPPLEMENTAL SURREBUTTAL TESTIMONY, MS.
11 FISCHER REFERS TO "MERIT/COST OF LIVING SALARY INCREASES". HOW
12 DO YOU RESPOND?

13 A. This is not an accurate depiction of Empire's compensation plan.

14 Q. PLEASE EXPLAIN.

15 A. The Company does not utilize "Cost of Living" increases. Instead, the Company
16 compensates its employees for the value of the job as determined by the survey process
17 which includes surveys of local employers, the Missouri State Chamber of Commerce
18 surveys, and National Industry Data provided by the Edison Electric Institute. There are
19 no automatic cost of living increases in Empire's compensation plan. The Company's
20 compensation plan is based on the idea of pay for performance which relates to the value
21 of the job and the efforts the employee makes relative to that job.

22 Q. HOW WOULD YOU CHARACTERIZE 2000?

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1 A. It was not a normal year as far as the Company and its employees were concerned.

2 Q. WHY?

3 A. Because of the pending merger with UtiliCorp United Inc., the Company spent the entire
4 year trying to perform the most basic of tasks. The Company spent most of the year with
5 a critical shortage of employees. Vacancies ran three times the normal amount and it
6 became virtually impossible, because of the pending merger, to hire employees with any
7 experience levels to fill the existing slots. As a result, those employees who stayed with
8 us were asked to take on additional responsibilities and work longer hours.
9 Consequently, the normal process of setting base and stretch goals was, for the most part,
10 not achieved. Simply stated, it became more important to keep the lights on and render
11 timely, accurate bills than to go through the process of establishing goals. In effect, the
12 organization stretched to achieve just that, keeping the lights on. As a consequence,
13 during 2000 the Company did not perform well in establishing and documenting the
14 goals and stretch goals that normally determine the Incentive Awards.

15 Q. WHY THEN DID EMPIRE GRANT THE INCENTIVE AWARDS THAT ARE AT
16 ISSUE HERE?

17 A. Because our employees truly did "stretch" to continue providing high quality service to
18 our customers and that, as a consequence, the customers were generally unaware of the
19 challenges we were facing. That is a tribute to our employees and their efforts during the
20 year, and, therefore, employees were deserving of the Incentive Awards which had been
21 accrued throughout the year 2000.

1 Q. MS. FISCHER ALLEGES ON PAGE 8 OF HER SUPPLEMENTAL SURREBUTTAL
2 TESTIMONY THAT THE INCENTIVE AWARDS RELATED MORE TO
3 SHAREHOLDER INTEREST. HOW DO YOU RESPOND?

4 A. This is an unfounded allegation. The Incentive Awards were made as a direct result of
5 providing service to ratepayers. If the shareholder interests were to prevail, the Company
6 would never make Incentive Awards but would try to maintain the lowest possible level
7 of employees and lowest possible level of compensation. In fact, the whole premise that
8 seems to drive Staff's position on this issue is that shareholder interests and ratepayer
9 interests must be diametrically opposed. This premise, however, is completely false. It is
10 the Company's view that a well-trained, highly motivated, properly compensated
11 workforce is advantageous to both shareholder and customers and that balancing and
12 coordinating these interests is an integral role of in the operation of our business.

13 Q. WHAT WAS THE TOTAL PERCENTAGE INCREASE IN COMPENSATION FOR
14 THE AFFECTED WORK GROUP?

15 A. Including the Merit Awards (in the amount of \$295,000) and the Incentive Awards (in the
16 amount of \$323,000), the total increase for this group for 2000 was 5.1% which, in a time
17 of full employment and upward wage pressures, is certainly within the realm of reason.
18 Keep in mind that Empire's compensation levels are at or below average to begin with, so
19 a 5.1% total increase, including the Incentive Award portion which presents a little over
20 one-half of the amount, is reasonable. If we had simply increased base pay by 5.1%, I
21 doubt that the Staff would have disallowed any of this amount. The fact that a portion of

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1 the increase is not permanent base pay, but is tied to an incentive plan, should not distract
2 from the overall reasonableness of the increase.

3 Q. DOES THE COMPANY INTEND TO INCLUDE FOR RATE RECOVERY ANY
4 EXPENSES RELATED TO THE FAILED MERGER WITH UTILICORP?

5 A. No. As stated in my Direct Testimony, this is not Empire's position and the Company
6 has made an honest and sincere effort to insure that those costs are not included in this
7 case. For the Staff to attempt to link these Incentive Awards to the merger costs requires
8 an extraordinary leap of logic. Legitimate merger costs have been and continue to be
9 recorded below the line by Empire.

10 Q. WHAT IS YOUR REACTION TO THE STAFF'S DISCUSSION OF THE EMPLOYEE
11 INCENTIVE GOALS FOR THE YEARS 1996 THROUGH 1999?

12 A. The Staff has selected examples of what it perceives to be failures of the managers to
13 select adequate goals or stretch goals, or goals that are not quantifiable, or that may be
14 repeated from year to year. In many repetitive type jobs, such as Call Center work, the
15 same set of stretch goals may be used year after year, since the work doesn't change
16 appreciably from year to year. There is no requirement in the Company's Plan that the
17 goals always be quantifiable. There are quality aspects of completing work that defy
18 measurement and it is the responsibility of managers who are close to that work to make
19 such determinations. While second guessing is always a popular spectator sport, it adds
20 little to the value of the process. In this regard, the Staff was selective in its analysis.
21 The Staff could have described the positive examples of learning new processes and new
22 systems, participating in the development and design of new procedures, leading in the

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1 development of a plan to expand plant to meet customer needs, and achieving work in
2 excess of normal job expectations, all of which are included in the material provided in
3 response to Date Request No. 331.

4 Q. DO YOU HAVE ANY OTHER COMMENTS ON THE PLAN IN RESPONSE TO THE
5 STAFF'S SUPPLEMENTAL SURREBUTTAL TESTIMONY?

6 A. Yes. The plan has been in existence at Empire since 1996. It is an attempt to instill the
7 idea that superior performance will generate greater compensation. The amounts accrued
8 for Incentive Awards are part of the Company's normal total compensation package. In
9 effect it puts a portion of the employee's pay at risk. The Plan was designed by a team of
10 employees working with upper management to break the old paradigms that dictated
11 across-the-board raises. The system is not perfect, but it is serving to make the changes
12 envisioned. The Company admits that 2000 was a year in which it fell short in the
13 execution of the system, but to throw out the Plan in its entirety is to throw out the baby
14 with the bath water. The Plan does not apply to officers, but is intended to provide
15 incentive compensation to a broad range of other employees ranging from those
16 compensated on an hourly basis to those on fixed salaries. The Plan is about changing the
17 expectations of the organization. To measure it against the management incentive plan
18 referenced in Case No. EC-87-114, involving Union Electric Company, is not
19 appropriate.

20 Q. WHY?

21 A. My understanding of the management incentive plan which was the subject of the Union
22 Electric case is that it was a plan which dealt with corporate goals and objectives and

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1 applied to management employees. Empire's plan, on the other hand, concerns
2 individual goals and objectives and is not available to employees at the officer level.

3 Q. DO YOU HAVE ANY CLOSING REMARKS ON THIS ISSUE?

4 A. Yes. Empire continues to believe that the \$323,000 at issue should be included in cost of
5 service in this case. Recognizing, however, that due to the pending merger our execution
6 in the year 2000 was not up to our usual standards, a possibility would be for the
7 Commission to include a four-year average expenditure for Incentive Awards, but to
8 deduct the \$323,000 from the total. The net result would make the issue worth
9 approximately \$223,500 on a total Company basis. This would preserve the Plan, which
10 the Company believes has great merit, but would recognize the Company's actual
11 performance in executing the Plan during the test year.

12 Q. DOES THIS CONCLUDE YOUR SURREBUTTAL TESTIMONY?

13 A. Yes, it does.