

Exhibit No.:
Issue: Incentive Compensation
Witness: Dana E. Eaves
Sponsoring Party: MoPSC Staff
Type of Exhibit: Surrebuttal Testimony
Case Nos. GR-2004-0209
Date Testimony Prepared: June 14, 2004

MISSOURI PUBLIC SERVICE COMMISSION

UTILITY SERVICES DIVISION

SURREBUTTAL TESTIMONY

OF

DANA E. EAVES

FILED

JUL 13 2004

**Missouri Public
Service Commission**

MISSOURI GAS ENERGY

CASE NO. GR-2004-0209

Jefferson City, Missouri
June 2004

Exhibit No. 809
Case No(s) GR-2004-0209
Date 6-21-04 Rptr _____

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI


In the Matter of Missouri Gas Energy's)
Tariffs to Implement a General Rate)
Increase for Natural Gas Service)

Case No. GR-2004-0209

AFFIDAVIT OF DANA E. EAVES

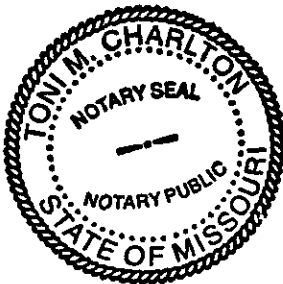
STATE OF MISSOURI)
)
COUNTY OF COLE) ss.

Dana E. Eaves, being of lawful age, on his oath states: that he has participated in the preparation of the following surrebuttal testimony in question and answer form, consisting of 4 pages to be presented in the above case; that the answers in the following 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.


Dana E. Eaves

Subscribed and sworn to before me this 10 day of June 2004.





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

1 **SURREBUTTAL TESTIMONY**

2 **OF**

3 **DANA E. EAVES**

4 **MISSOURI GAS ENERGY**

5 **CASE NO. GR-2004-0209**
6
7

8 Q. Please state your name and business address.

9 A. Dana E. Eaves, PO Box 360, Suite 440, Jefferson City, MO 65102.

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

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

13 Q. Are you the same Dana E. Eaves who has previously filed direct testimony in
14 this case?

15 A. Yes, I am. On April 15, 2004, I filed direct testimony in this case.

16 Q. What is the purpose of your surrebuttal testimony?

17 A. The purpose of my surrebuttal testimony is to respond to the rebuttal
18 testimony of Missouri Gas Energy (MGE or Company) witnesses Michael R. Noack and
19 Deborah Hayes, who both defend MGE's proposed inclusion in rates of incentive
20 compensation payments at the divisional level. I will be specifically addressing MGE
21 divisional level incentive compensation plan in this testimony and Staff auditing witness
22 Charles R. Hyneman will be addressing the corporate level incentive plan in his surrebuttal
23 testimony concerning the overall issue of corporate allocations.

24 Q. What is the Staff's position on the recovery through rates of incentive
25 compensation expenses?

1 A. To be recovered from ratepayers, incentive compensation should only reward
2 employees for performance that is both exceptional and beneficial to ratepayers; in other
3 words, employee performance that is beyond the employee's usual job description and
4 beneficial to ratepayers. To reward employees for activities that they are required to do as
5 part of their normal job duties would be duplicative of their salary expense and such amounts
6 should not be borne by the ratepayers.

7 Q. Mr. Noack on page 16 lines 6-12 discusses in the following quote from his
8 rebuttal testimony his belief that customer interests significantly drive MGE achieving
9 financial objectives.

10 To the extent any utility, including MGE, is able to achieve earnings it
11 deems reasonable, it will be less likely to make filings, such as this
12 one, seeking to implement general rate increases. Moreover, cost
13 savings and efficiencies generated between rate cases should reduce
14 the magnitude of a subsequent rate increase request to the benefit of
15 customers. Financially based incentive compensation opportunities
16 cause employees to seek out efficiencies that will help improve the
17 bottom line and increase the likelihood of an award of incentive
18 compensation.

19 Do you agree with these statements?

20 A. No. MGE's incentive compensation plan is based on its pre-tax earnings,
21 defined as net income amount before federal income taxes are subtracted. Incentive
22 compensation, based on earnings measures such as pre-tax earnings, do not necessarily
23 reflect customer interests. While some of the factors listed above directly impact ratepayers
24 if rates are reduced, one cannot conclude that other factors resulting in pre-tax earnings
25 changes, even indirectly, represent improved customer service or benefits. For example,
26 changes in weather will impact MGE's pre-tax earnings. Incentive compensation goals that
27 tie to pre-tax earnings are goals that primarily benefit shareholders. Ratepayers should not
28 bear the costs associated with incentive compensation payouts tied to these financial goals.

1 Also, if incentive compensation plan goals are financially driven, there is a risk that they may
2 be achieved at the expense of customer service.

3 Q. Mr. Noack poses this question and provides an answer in his rebuttal
4 testimony on page 17, lines 8-13:

5 Q. Does witness Eaves believe that incentive compensation can
6 have a positive effect on employees?

7 A. Yes. In response to MGE DRs 0028 and 0029 to the Staff
8 (attached as Rebuttal Schedules MRN-10 and MRN-11), witness
9 Eaves believes that not only can incentive compensation affect the
10 morale an/or job satisfaction of employees, but also can effect the
11 behavior of employees.

12 Is this an accurate representation of the answer you provided in MGE Data Request
13 Nos. 0028 and 0029?

14 A. No. I made no indication that incentive compensation plans have a "positive"
15 effect on employee morale and/or job satisfaction of employees. The Company data requests
16 asked very general questions about generic incentive plans. Based upon the information
17 provided by the Company in the data requests, I could make no specific claims regarding
18 effects of incentive compensation plans on employee behavior other than these types of plans
19 can potentially effect the morale and/or job satisfaction of employees. My responses to MGE
20 Data Requests Nos. 0028 and 0029 are attached as Surrebuttal Schedules 1 and 2 to this
21 testimony.

22 Q. Ms. Deborah Hays on page 3, lines 10-19, of her rebuttal testimony, discusses
23 a survey done by Watson Wyatt, which purports to provide percentages of companies that
24 provide incentive compensation plans for executives. Does she disclose which of these
25 companies are Missouri regulated utilities?

26 A. No, she does not.

1 Q. Is this an important distinction in your opinion?

2 A. Absolutely. Missouri regulated utilities operate in a non-competitive
3 environment and therefore may experience different market forces than publicly traded non-
4 regulated companies and/or non-regulated utilities (municipals, utilities operating in
5 jurisdictions in which some competition is allowed) face. Therefore, comparing these
6 companies to non-regulated utilities and publicly traded companies in the survey offers little
7 insight on the rate treatment to be provided to MGE's divisional incentive compensation
8 plan.

9 Q. Has the Staff had an opportunity to review the Watson Wyatt survey referred
10 to by Ms. Hays?

11 A. No. The Staff requested the survey referenced by Company witness Hays in
12 Data Request No. 309. However, the Company's response (Schedule 3 to this testimony)
13 states "Copies of the Watson Wyatt study are unavailable to MGE unless it is purchased from
14 Watson Wyatt for several hundred dollars...". The Staff finds it inappropriate for MGE to
15 rely on one page of a comprehensive survey and draw conclusions from that page, especially
16 given the fact that the Company is unable to provide a complete copy for the Staffs review.
17 The Staff would expect the Commission to weigh the fact that a complete copy of the Watson
18 Wyatt survey has not been made available for its review as well when assessing the
19 arguments made by Company witness Hays.

20 Q. Does this conclude your surrebuttal testimony?

21 A. Yes, it does.

Data Request No.

MGE-DR NO. 28

Data Information Request
from Missouri Gas Energy
to MPSC Staff
Case No. GR-2004-0209

Requested From: Dana Eaves

Date of Request: 4/22/04

Requested By: Mike Noack

Information Requested: Does witness Eaves believe that compensation practices (salary and wage levels, incentive compensation, Christmas bonuses, etc.) can affect the morale and/or job satisfaction of employees? Please describe the rationale upon which your answer is based and provide any information and material relied upon in developing the answer.

Response: Yes. Witness Eaves believes that compensation practices (salary and wage levels, incentive compensation, Christmas bonuses, etc.) can affect the morale and/or job satisfaction of employees. Witness Eaves bases this opinion on personal and professional experience.

The attached information provided to Missouri Gas Energy 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 Missouri Gas Energy if, during the pendency of Case No. GR-2004-0209 before the Missouri Public Service 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 at a 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 of data, recordings, transcriptions and printed, typed or written materials of every kind in your possession, custody or control within your knowledge. The pronoun "you" or "your" refers to the person identified in the "Requested From" block above and all other employees, contractors, agents or others employed by or acting on behalf of the organization, group or governmental unit associated with that person.

Provided By: Dana Eaves
(Please Print)

Date Signed: 5/10/04

Signed: Dana Eaves

Data Request No.

MGE-DR NO. 29

Data Information Request
from Missouri Gas Energy
to MPSC Staff
Case No. GR-2004-0209

Requested From: Dana Eaves

Date of Request: 4/22/04

Requested By: Mike Noack

Information Requested: Does witness Eaves believe that incentive compensation can affect the behavior of employees? Please describe the rationale upon which your answer is based and provide any information and material relied upon in developing the answer.

Response: Yes. Witness Eaves believes that incentive compensation practices can affect the behavior of employees. Witness Eaves bases this opinion on personal and professional experience.

The attached information provided to Missouri Gas Energy 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 Missouri Gas Energy if, during the pendency of Case No. GR-2004-0209 before the Missouri Public Service Commission, any matters are discovered which would materially affect the accuracy or completeness of the attached information.

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Provided By: Dana Eaves
(Please Print)

Date Signed: 5/10/04

Signed: Dana Eaves

Missouri Public Service Commission**Respond Data Request**

Data Request No.	0309
Company Name	Missouri Gas Energy-Investor(Gas)
Case/Tracking No.	GR-2004-0209
Date Requested	05/25/2004
Issue	Expense - A&G - Employee Benefits
Requested From	Kimm Henzi
Requested By	Dana Eaves
Brief Description	The Watson Wyatt Survey
Description	Please provide a complete copy of The Watson Wyatt Survey as referenced on page 3 in the Rebuttal Testimony of Company witness Deborah Hays.
Response	Copies of the Watson Wyatt study are unavailable to MGE unless it is purchased from Watson Wyatt for several hundred dollars. One page from the study was referenced to show that incentives are commonly provided in all types of companies including the utility industry. The Watson Wyatt study is the property of CBIZ, and CBIZ has not agreed to provide a complete copy of the study to MGE or Ms. Hays.
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-2004-0209** 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-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-Investor(Gas)** and its employees, contractors, agents or others employed by or acting in its behalf.

Security :	Public
Rationale :	NA

With Proprietary and Highly Confidential Data Requests a Protective Order must be on file.

Schedule 3