STATE OF ILLINOIS

ILLINOIS COMMERCE COMMISSION

MIDAMERICAN ENERGY COMPANY	)	
	)	
Proposed general increase in electric rates.	)	**DOCKET NO. 14-0066**
	)	
	)	

SURREBUTTAL TESTIMONY
OF
Melissa A. Grannes

Q. Please state your name and business address.

A. My name is Melissa A Grannes. My business address is 666 Grand Avenue, Des Moines, Iowa 50309.

Q. Are you the same Melissa A. Grannes who previously submitted direct and rebuttal testimony in this proceeding?

A. Yes, I am.

<u>Purpose of Testimony</u>

Q. What is the purpose of your surrebuttal testimony?

A. The purpose of my surrebuttal testimony is to address Illinois Commerce Commission Staff (Commission Staff) witness Bridal's recommendation to disallow costs associated with MidAmerican Energy Company's Performance Incentive Plan (PIP). In my surrebuttal testimony, I address Mr. Bridal's four overall objections, which are based on theories of excess discretion, the PIP's not having rigid percentage figures for its six core principles and its 39 detailed goals (this subject is based on the 2012 plan), the role of the

utility's financial strength in the PIP design, and the role of data involving the Company's cross-state activities and performance. I conclude that the PIP is reasonable and benefits customers and that Mr. Bridal has not stated sound reasons for denying recovery of these costs.

Q. Please summarize your surrebuttal testimony.

A. My surrebuttal testimony makes the following points.

1. I disagree with a characterization of incentive compensation as containing excess discretion. Each year the goals revolve around a set of six core principles, which are important for any public utility. As I noted in earlier testimony, those principles address Customer Service, Employee Commitment (which includes among other things the Company's emphasis on having employees return home each day free of any workplace injuries), Financial Strength, Environmental Respect, Regulatory Integrity and Operational Excellence. While some goals easily lend themselves to quantifiable metrics, other goals do not. Sound business judgment needs to be applied in assessment of goals.

2. Incentive compensation essentially removes a portion of base pay to make the pay at risk with incentive payments tied to performance. Overall compensation is aligned with market rates. The goal process is designed to keep employees focused on matters of importance to our customers and a well-run utility business. MidAmerican has a long and consistent history in which it has paid out between 85% and 100% of its budgeted goal annual levels.

3. While most goals benefit every electric and gas customer in every state in which MidAmerican provides service, certain goals are specific to the jurisdictions MidAmerican serves, including Illinois. In order to ensure appropriate allocation of incentive compensation expense based on these goals, Illinois customers are allocated incentive compensation expenses based upon the overall direct charging and allocation of labor resources to support Illinois electric operations.

Q. Are you presenting any Exhibits to your surrebuttal testimony?

A. Yes, I am sponsoring Company Exhibit MAG 3.1, Schedule A – Public and Confidential 2012 MEC Goals: Explanation of Operational Goals impacting Illinois Customers.

Q. Please describe Commission Staff witness Bridal's recommendation for the Performance Incentive Plan Expense.

A. Mr. Bridal provided Schedule 12.01, which outlines an adjustment to remove 100% of the amount of the PIP incentive compensation included in the operating statement. (Bridal Rebuttal, ll. 3-14) He contends that the PIP is subjective or discretionary in nature, is based on various goals which do not have percentages assigned, is based partially on the financial strength of the utility, and is based in part on certain goals that are not associated with Illinois electric jurisdictional utility service. (Bridal Rebuttal, ll. 77-80)

Q. Does the PIP include an improper or excessive degree of subjectivity or discretion?

A. No. In my direct and rebuttal testimony and schedules, and in the discussion in my surrebuttal below and attached schedules, I have shown that the PIP is carefully designed, in terms of its core principles and its goals, and in terms of how it is implemented, to reflect sound business judgment. The track record of the PIP shows that is the case, and the Commission previously has approved the recovery of PIP costs. The PIP should be judged based on how it actually works, not hypothetical scenarios in which it is misapplied. I discuss this point further below.

Q. In justifying his proposed disallowance, does Mr. Bridal address the total compensation paid to MidAmerican employees covered by the PIP?

A. No.

Q. Why is Total Compensation important in the discussion of incentive recovery?

A. Both base pay and incentive compensation are needed to bring compensation levels to market pay levels. The Company establishes its base pay and incentive compensation based on the market. (See Grannes Direct testimony, ll. 42-72). We pay rates at the median of the market. Ensuring that pay is at market levels is critical to attracting and

retaining qualified employees. We not only review our total compensation to market, but also benchmark the portion of pay that is at risk via an incentive program by comparing our incentive targets with those of other peer utility companies (see Grannes Direct testimony, ll. 70-72 Exhibit MAG 1.1, Schedule A). In other words, by seeking to recover base pay plus incentive payouts, all we seek is recovery of justifiable compensation expenses.

Q. Mr. Bridal states that Staff did not evaluate a proposal to pay employees with base salary and no pay at risk. (Bridal Rebuttal, ll. 259-266) Does his statement refute any of the points you have made about total compensation, including it being set at market levels and that pay at risk trades off with base pay such that the former reduces the latter?

A. No. In addition, the Company has provided unrefuted evidence that the total compensation level is reasonable. There is no factual basis for suggesting or implying that if the total compensation level was paid through base pay, Staff would have had an objection to any of the base pay, much less a valid one.

Q. How does money spent on the Performance Incentive Plan benefit customers?

A. Because there is no guarantee of incentive compensation if employees do not meet goals that fulfill important operational objectives, any dollars not spent on base pay and transferred to incentive pay are at risk to the employee. (*see* Grannes Direct testimony, ll. 74-101) Employees understand that incentive compensation is not guaranteed and that they must complete their annual goals in order to be eligible to receive an award. Customers benefit as employees will complete these goals, improving utility service, in

order to receive their incentive compensation. Customers also benefit to the extent that the total incentive payout is less than what paying salaries only at market levels would be.

Q. How do customers benefit from achievement of employee goals?

A. Because the goals themselves are organized around the Company's six core principles: customer service, employee commitment, financial strength, environmental respect, regulatory integrity and operational excellence, all of the core principles benefit customers and for what it is worth, they are in alignment with what the Commission may consider as acceptable incentive metrics under Section 16-108.5 of the Illinois Public Utilities Act, although this is not a formula rate case under that provision. While I am not an attorney, it is difficult to think that the metrics in that Section mandate or even suggest that proper pay-at-risk systems that benefit customers should not yield cost recovery.

Q. Do you have an Exhibit that shows the connection of PIP goals to customer benefits?

A. Yes. Schedule A illustrates how the 2012 MidAmerican Energy Company goals provide operational benefits to our Illinois electric customers. Of the 37 specific goals, 24 of them have an Illinois operational component. Illinois electric operations constitutes roughly 10% of our customers. It is not practical to set goals in a way that each and every goal must benefit our customers in exactly the same proportion. This schedule addresses Mr. Bridal's concerns regarding perceived similarity between MidAmerican and Commonwealth Edison ICC Order Docket 13-0318 pp. 44-45.

Q. Why do you disagree with Mr. Bridal's contention that MidAmerican Energy Company's authorization of incentive compensation under the PIP is discretionary and not based on accomplishment of goals?

A. The Company has always reviewed its performance against goals and has paid out PIP awards at some level in each year from 2003-2013. The detailed review undertaken by MidAmerican's president of 2012 accomplishments is set forth in ICC Staff Ex. 12.0, Attachment B, pp. 1-5. A Schedule showing the 2003-2013 PIP award history is set forth in ICC Staff Ex. 12.0 at Attachment B, p. 2 of 5. Guiding these awards are metrics built into the goals that are established each year against which performance is measured. The measurement for 2012 is shown in ICC Staff Ex. 12.0, Attachment A and the 2012 evaluation of MidAmerican Energy Company's performance with regard to the goals in ICC Staff Ex. 12.0, Attachment B, pp. 3-5.

Q. But Mr. Bridal suggests that these payouts are not strictly based on the performance of these goals. Please address his contention.

Q. I acknowledge that the Company uses reasoned judgment in determining whether to pay, but payout is not guaranteed and instead is based on a thorough review of performance to goals. The review of goal performance can lead to different conclusions about the level of achievement each year. The 2003-2013 PIP payouts have ranged from 85-100% with an average payout being at 96% (ICC Staff Ex. 12.0, Attachment B, response to RWB 11.03(b), p. 2). The 2012 PIP test year payout level was at 100%. In addition, payout is not arbitrary as the Company has paid out every year for the past 10 years.

Q. Do you agree with Mr. Bridal that the Company did not adequately address why it is important for the Company goals to be discretionary (Bridal Rebuttal, ll. 172-174)?

A. No. As noted at my rebuttal testimony at ll.103-105, the Company reviews performance both at the company level and individual level by assessing under what conditions the

goals were achieved or what conditions might have led to the goals not being achieved. The same is true for the Company as it is for the individual; there may be certain macroeconomic factors over which the Company has little or no control. An example of this in 2012 would be environmental regulations that were overturned or revised subsequent to the time we established the goal (*see* Schedule A, goal 8, regarding2012 the Cross State Air Pollution Rule). We do not think we should pay out at less than target when there were forces beyond the Company's or its employees' control that prevented goal achievement.

Q. Please explain why you do not agree with Mr. Bridal's concern that there should be some fixed percentages assigned to the goals. (Bridal Rebuttal, ll. 85-110)

A. Mr. Bridal argues that lack of percentages associated with a goal prevents a determination of its accomplishment: "the degree to which the costs related to PIP incentive compensation are associated with specific dollar saving or other tangible benefits to ratepayers cannot be determined." The goals are established and evaluated around acceptable metrics, not fixed levels of improvements. The goal achievement will reflect improving over time to benefit the customer (e.g. Grannes Rebuttal Exhibit MAG 2.1 Customer Satisfaction Schedule A, O & M per Customer Schedule B and Safety Incident Rate Schedule C). By not agreeing that fixed payout would occur at the point of goal achievement, it is possible effort would cease at that level and a maximum outcome would not be reached. In any event, the facts I have provided show that the six core principles and the more detailed goals are designed and applied in a manner that is reasonable and benefits customers.

Q. Staff witness Bridal again takes issue with the financial strength core principle, and with six goals related in various respects to that principle. (Bridal Rebuttal, ll. 139-171). Is his conclusion on this subject a sound reason to disallow recovery of PIP expense?

A. No. I have discussed this subject in my rebuttal testimony, and the points made by Mr. Bridal do not overcome the points I made there. Financial strength is one of the six core principles, but financial strength is clearly a basic concern for a sound utility (and its regulator) and is not the same thing as a metric based solely on net income or earnings. With respect to the six goals related to financial strength (out of 39 goals), as Mr. Bridal seemingly acknowledges, four of the six benefit MidAmerican's Illinois electric customers. One of the goals addresses keeping capital costs and operations and maintenance expenses below budget. MidAmerican was successful in keeping capital costs under budget. Operation and maintenance costs for the supply (i.e. generation) business were below budget. Electric delivery costs were above budget, but that was partly due to April and August 2012 storms. Two financial strength goals benefited customers through the attainment lower fuel adjustment clause charges than budgeted and managed in a way to reduce price volatility. A fourth financial strength goal addressed contracts with outside vendors. With respect to that goal, MidAmerican was able to keep such expenditures below budget.

Again to reiterate, as an example of the Company paying out PIP even with mixed results on financial strength, we paid out PIP at 100% in 2012 even though we did not meet our net income goal. *See also*, my direct testimony on page eight, lines 135-142. In 2008, we also did not achieve the net income goay and yet we paid out PIP at 100%. Moreover, in

2012, 33 of the 39 goals were not financial in nature. *See* Schedule A. Mr. Bridal's recommendation to disallow the entirety of PIP cost recovery related to a subset of financial strength goals is not sound or reasonable.

Q. Finally, Staff witness Bridal also takes issue with the fact that four of the Company's 39 goals are not associated with Illinois utility service and one is associated with the Company's gas utility service. Please address this concern.

A. Mr. Bridal is right that a few goals involve specific services territories, and that most other goals involve the Company as a whole which includes Illinois as well as activities and performance outside of Illinois. However, those facts should in no way justify complete disallowance of incentive compensation costs. Most of the 2012 goals refer to the total company and thus are intended to achieve beneficial results in the entire MidAmerican Energy Company service territory, including Illinois. These include customer satisfaction and reliability metrics. Those few goals that single out specific states are related to requirements specific to the state and will be allocated to that state as appropriate. For example, goal 17 is specific to Illinois and is intended to complete the Illinois Commerce Commission-ordered National Electrical Safety Code corrective action plan, adhering to the plan to finish all work by December 31, 2012. This Illinois-specific goal and all other goals are shown on MidAmerican Exhibit 3.1, Schedule A, which outlines how the 2012 MidAmerican Energy Company goals benefit Illinois electric customers.

Q. Does this conclude your surrebuttal testimony?

A. Yes, it does.