Exhibit No. __ (LLM-1T)
Docket No. UG-170929
Witness: Linda L. Murray

BEFORE THE
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION Complainant, v. CASCADE NATURAL GAS CORPORATION, Respondent.	DOCKET UG-170929

CASCADE NATURAL GAS CORPORATION

REBUTTAL TESTIMONY OF LINDA L. MURRAY

March 23, 2018

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I. INTRODUCTION

Q. Would you please state your name and business address?

A. Yes, my name is Linda Murray. My business address is 555 South Cole Road, Boise, ID 83709.

Q. What is your position with MDU Resources Group, Inc.?

A. I am the Director of Human Resources.

Q. What are your duties and responsibilities?

A. I am responsible for the strategic direction and administration of all disciplines in the Human Resources (HR) department for Cascade Natural Gas Corporation (Cascade or Company) and Intermountain Gas Company (Intermountain) including compensation and benefits, talent acquisition and development, labor and employee relations and governmental compliance with employment and employee relations for Cascade and Intermountain.

Q. Would you please describe your educational and professional background?

A. I have worked in the Human Resources field for more than 30 years. For the past 10 years, I have been employed by MDU Resources Group Inc., as the Director of Human Resources, working its subsidiaries, Cascade and Intermountain. Prior to joining the MDU Resources Group, Inc., I worked in a variety of human resource positions including as Compensation and Benefits Manager. I hold senior professional certifications from the Human Resource Certification Institute and the Society for Human Resource Management.

Q. What is the purpose of your testimony?

A. My testimony explains the Company's process for setting total compensation for its employees, including both base pay and incentive compensation (or "pay-at risk"). In addition, my testimony responds proposals made by Staff, Public Counsel and the

Northwest Intermountain Gas Users (NWIGU) that certain portions of the Company's incentive compensation be disallowed.

II. CASCADE COMPENSATION PHILOSOPHY

Q. Please describe Cascade's general approach to setting total compensation for employees—including incentive compensation.

A. There are three basic principles underlying Cascade's approach to employee compensation—all designed to minimize costs while allowing the Company to attract and retain the qualified employees required to deliver safe and reliable service to our customers.

First, Cascade has adopted a Total Rewards philosophy, which provides our employees with a Total Rewards package. The Total Rewards package includes both total cash compensation and benefits. The two key components of total cash compensation are base pay and incentive compensation.

Second, Cascade makes every attempt to compare its wages and at-risk incentive compensation with that available in the relevant labor market, and to set total cash compensation at the market average for comparable jobs. We are finding that the market for employees with the skills and experience we require is very competitive in the areas where we do business. For that reason, the two components of cash compensation we offer must together provide the same general pay levels and benefits as are included in the packages provided by the Company's competitors for labor.

Third, the Company believes that, in order to encourage employee engagement and to help employees better understand the importance of operating our business effectively, a certain percentage of each employee's market compensation should be "at risk." Accordingly, under Cascade's incentive plan, each employee has the opportunity to receive total cash compensation and benefits at the market average, so long as the employee performs at an acceptable level. However, employees will earn less than the average remuneration when performance is less than acceptable and, conversely, will earn higher than the average remuneration when performance is exceptional. Importantly, however, our program is structured such that total compensation to all employees is aligned with the market average.

Q. Please explain how the Company determines the market average when it sets the base pay and incentive compensation components of total cash compensation.

A. When market pricing a position within the organization, we pull data from a variety of survey and online sources for industry salary surveys, including the American Gas Association, Mercer, EAP Data Information Solutions, Willis, Towers, Watson, World at Work and Kenexa Compensation Analyst, among others. We then analyze the median base pay and target incentive compensation data to determine a market average.

Q. How do you assess whether incentive compensation remains consistent with industry standards?

A. We continue to monitor industry trends concerning incentive compensation. According to a 2017 American Gas Association Compensation Survey, the majority of participating utilities provided incentive compensation or pay-at-risk to all levels of employees. In 2014, the World at Work incentive pay practices survey, which included 350 publicly traded companies, indicated that 99% had short-term incentives. In 2016, Vivient Consulting conducted an incentive study and reported that, based on the World at Work short-term cash incentive programs that were reported, 94% of participants offer incentive compensation. Based on this ongoing research, incentive compensation remains strong in the workplace. We will continue to watch these programs, as we do base pay, to ensure that we continue to provide competitive total compensation.

Q. Do you have additional processes in place to ensure that the Company is not paying or incentivizing more than the minimum necessary to attract and retain a qualified workforce?

A. Yes. Periodically the Company contracts with an outside independent consultant to review compensation programs and practices. For instance, in 2013, the Company contracted with Aon Hewitt to provide a third-party review of base compensation and incentive compensation. This independent review will be done again in 2018 to assure that appropriate levels of base pay, incentive compensation, and benefits are available to attract and retain talent in order to continue to provide safe reliable service to our customers.

Q. What was the result of the 2013 Aon Hewitt review?

A. The Aon Hewitt review indicated that Cascade's compensation programs, including incentive programs, are well designed and utilize high quality and established external survey sources to ensure that the programs align well with other utilities and industries that compete for the same types of employees. Aon Hewitt also found that employees' eligibility for incentive pay is consistent with other utilities, and that the plan metrics include a significant and appropriate portion of incentive compensation focused on customer service and cost management. The report that Aon Hewitt prepared in 2013 is included as Confidential Exhibit No. ____(LLM-2C).

Q. Do you follow the processes described above to ensure that the total compensation of all employees is at market—including executives and senior management?

A. Yes. We follow the same processes to ensure that the total compensation for all employees is set at market.

III. INCENTIVE PAY

Q. Please provide a high-level description of Cascade's incentive pay plan.

A. All employees of the companies within the MDU Utility Group are covered by the same incentive pay plan, when we refer to as the Employee Incentive Plan (Plan). The Plan is made available to all non-bargaining unit employees who are classified as regular full or part-time and is structured to provide incentive compensation to employees that perform adequately across multiple measures, including managing costs, providing outstanding customer service, and training and developing a quality workforce. The total payout under the Plan is determined for each year, and employees are awarded a portion of the total payout based on individual performance. goals.

Q. How is the total payout determined?

A. The total payout is determined based on the Company's achievement of three major goals: (1) the Financial Goal, which is based on the Company's earnings; (2) the Operations and Maintenance Expense Goal which is based on the Company's meeting an expense target; and (3) the Customer Service Satisfaction Goal, which is determined by the results of the JD Powers and Associates survey. Each of these three goals is weighted equally in the determination of how much should be paid, and the percentage impact on the payout differs based on the employee's pay grade. A copy of the 2016 Employee Incentive Plan is attached as Exhibit No. ____(LLM-3).

Q. Please describe the rationale for each goal.

A. The Financial Goal is designed to encourage employees to spend dollars wisely, work efficiently and safely, increase efficiencies in work processes and eliminate redundancies, and to suggest and justify capital projects that will increase efficiencies and return more than the cost of capital over the life of the project. The O&M Goal is similarly designed to encourage employees to seek efficiencies. The Customer Service Goal is designed to heighten employees' awareness of the customer experience—whether or not their jobs provide them with direct customer contact.

Q. Is the Plan structured to pay out incentives to employees every year?

A. No. Before incentives are paid out the Company must meet a minimum earnings target of 85 percent of the Company's pre-established goal.

Q. Do senior management employees have a separate incentive plan?

A. Yes. Senior management employees—as identified by pay grade-- are covered by the Senior Management Incentive Plan (Management Incentive Plan)

Q. How does that plan differ from the Incentive Plan discussed above?

A. The Management Incentive Plan is identical to the Incentive Plan applicable to the general employee group with one key exception. The payout is determined by the achievement of a Leadership Goal, in addition to the Financial, Operations and Maintenance, and Customer Satisfaction Goals. A copy of the Senior Management Incentive Plan is attached as Exhibit No. ____(LLM-4).

Q. Please describe the Leadership Goal and how incentives paid for the attainment of that goal benefit utility customers.

A. Attainment of the Leadership Goal is contingent on all senior management employees personally reviewing the results of the prior years' employee survey for their responsibility area, leading a discussion with employees about those results, and developing and implementing action plans based on those results.

Q. How do Cascade's customers benefit from the Employee and Management Incentive Plans?

A. The incentive plan benefits Cascade's customers by motivating a workforce to focus on controlling costs while at the same time increasing customer satisfaction. Moreover, we find that the Incentive Plan—as part of the Total Rewards philosophy--is key to attracting and maintaining the highly skilled workforce required to operate and maintain the utility, which directly benefits our customer base because it ensures we have qualified people performing the work of providing a safe and reliable system for our customers.

Q. Does the Company have separate incentive plans for executives?

A. Yes. We have two additional incentives made available to our MDU Resources Group executives—the Executive Incentive Compensation Plan (Executive Incentive Plan) and the Long-Term Performance-Based Incentive Plan (LTP Plan). Awards made under these plans are tied primarily to financial goals for the Company.

Q. Please state the amount of incentive payments included in the Company's test year revenue requirement.

A. Cascade included employee incentive payments in the amount of $1,765,931 in the test year revenue requirement. Of this amount, a total of $1,136,795 represent incentives that were cross-charged from affiliates.

Q. Did parties propose adjustments to Cascade's incentive compensation?

A. Yes. Staff, Public Counsel, and NWIGU each propose adjustments related to incentive compensation.

Q. Could you please summarize Staff's proposed adjustment and Staff's rationale?

A. Yes. Staff witness Kristen Hillstead proposes removing incentive pay associated with meeting the Company's financial goals. While Staff proposes allowing incentive payments for meeting the Operations and Maintenance Goal and Customer Satisfaction Goal, Staff believes that customers do not benefit from incentives related to a utility reaching an earnings target.[1] Staff reasons that "the Commission has determined that incentives tied to financial goals . . . must be disallowed."[2] The revenue requirement impact of Staff's proposed adjustment is a decrease of $1,482,800.

Q. Can you tell how Staff has calculated its adjustment?

A. It appears that eliminated all incentives paid out by affiliates, and all incentives paid out by Cascade, except those associated with the O&M and Customer Service goals.

Q. Could you please summarize Public Counsel's proposed adjustment to incentive compensation and rationale?

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[1] Exh. KMH-1T at 13:12-13, 15:1-2.)

[2] Exh. KMH-1T at 13:14-15. Staff cites to Avista's 1999 GRC (Exh. KMH-1T at 13:18-21.) and *WUTC v. Wash. Nat. Gas Co.*, Docket No. UG-920840, 4th Supp. Order (1993) (Exh. KMH-1T at 13:23-14:3.).

A. Public Counsel's witness Donna Ramas also proposes to remove the portion of the incentive compensation expense for Cascade employees based on achieving earnings goals, arguing that such goals benefit shareholders and not customers[3] Public Counsel also proposes to remove incentive payments made by affiliates because the Company did not demonstrate that the payments to affiliates are not based on meeting financial goals. [4] The revenue requirement impact of Public Counsel's adjustment is a decrease to revenues of $1,452,623.

Q. Can you tell how Public Counsel calculated its adjustment?

A. It appears that Public Counsel eliminated all incentives paid out by affiliates, and all incentives paid out by Cascade, except those associated with O&M, Customer Service and Integrity Leadership goals.

Q. Please summarize NWIGU's incentive compensation adjustment and rationale.

A. NWIGU's witness Bradley Mullins recommends removing the cost of incentive awards allocated from affiliates to Cascade because the Company has not demonstrated that those amounts benefit ratepayers.[5]

Q. Can you tell how NWIGU calculated its adjustment?

A. Yes. NWIGU appears to have eliminated all incentives except those paid out to Cascade employees.

Q. Is there overlap in the parties' proposed adjustments?

A. Yes. While the adjustments proposed by the parties differ in the total revenue requirement impact, the parties are generally focused on two issues: (1) incentive compensation tied to financial performance, and (2) incentive compensation for affiliates.

Q. Does the Company agree to any of the adjustments made by the parties?

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[3] Exh. DMR-1T at 49:15-16.
[4] Exh. DMR-1T at 50:7-11.
[5] Exh. BGM-1T at 13:16.

A. In principle, yes. The Company agrees that the costs associated with the Executive Incentive Plan and the LTP should be removed from the case--- because the goals on which those incentives are based on either primarily and completely financial in nature. However, the Company believes that the entire expense associated with the Employee Incentive Plan and the Management Incentive Plan should be recovered.

Q. Please describe the impact of removing incentives related to the Executive and LTP Plans.

A. After incentives paid out for the Executive and LTP Plans are removed, the adjusted amount the Company proposes to recover for incentives is $947.134.71-- which reflects a $818,795.82 downward adjustment to the total amount included in the Company's initial case for incentive payments. I have provided the breakout of the total incentives and the identification of the executive incentive in Exhibit No. ____(LLM-5).

Q. How did you calculate these amounts?

A. Because the Company does not track incentives paid out by plan on an allocated basis, this calculation required the Company to review the total incentives by plan and then apply allocations based on salary allocation factors of executives and employees to derive at amounts that ultimately were recorded at Cascade and further to Washington.

Q. Does the removal of the incentives paid out under the Executive and LTP Plans resolve the disagreements among the parties?

A. No, not entirely. Staff, Public Counsel and NWIGU all propose to eliminate all affiliate allocated incentives paid out—not just those associated with the Executive and LTP Plans. That proposal may have been made because the Company had not confirmed what portion of affiliate incentives were related to the Executive and LTP Plans. But to be clear, a portion of the affiliate incentives paid out are in fact made under the Employee and Senior Management Plans and should be recovered because they provide significant benefits to customers and are consistent with plans for which the Commission has allowed recovery in other cases.

In addition, Staff and Public Counsel propose that only two-thirds of the incentives paid directly to Cascade employees be recovered, apparently because one of the three goals on which those incentives are paid is financial in nature. The Company disagrees with this approach for two reasons. First, this Commission has a policy of allowing recovery of employee incentive payments so long as customers benefit from those plans—even if some of the goals are financial in nature. Second, Cascade believes that the achievement of financial goals do benefit both utility customers and shareholders, and that incentives paid out for the achievement of such goals should be recoverable as part of an overall incentive plan that includes goals that focus more directly on customer benefits.

Q. Please explain your statement that the Commission has a policy of allowing recovery of incentive payments, even those that that include some goals that are financial in nature.

A. This precise issue arose in UE-100749, in which various parties sought disallowance of portions of PacifiCorp's incentive payments on a variety of grounds, including that some of the goals on which the payments were paid out were designed to enhance shareholder as opposed to customer value. The Commission rejected these arguments stating its reluctance to "delve too deeply in to the Company's management of its human resources and the manner in which it determines overall compensation." In the end, the Commission concluded that, when reviewing compensation, including incentives, it would "inquire only whether that compensation exceeds the market average, is unreasonable, and offers benefits to ratepayers.[6] The Commission has reaffirmed this policy in recent cases where it has specifically approved incentive payments made under

[6] *WUTC v. PacifiCorp*, Docket UE-100749, Order 06 at 86 (Mar. 25, 2011).

plans that include financial goals, and that require achievement of financial goals to "trigger" payment under the plan.[7]

Q. Please respond to Staff's statement that the Commission has specifically disallowed incentives tied to financial goals.

A. In making this argument, Staff points to Commission orders in a 1999 Avista general rate case.[8] However, as described in the Commission's orders, those plans were weighted more heavily on financial performance than Cascade's. For instance, the Commission pointed out that in Avista's case, only one of the employee groups had goals related to customer service—and that two-thirds of that team's goals were based on financial performance.[9] Most importantly, as discussed above, since that case was decided, the Commission has clarified its policy on incentive payments, confirming that utilities may recover the cost of incentives in plans that include financial incentives—including plans such as Cascade's that contain a trigger mechanism based on financial performance.[10]

Q. Do you agree with Staff, NWIGU and Public Counsel's implication that incentive payments tied to financial goals have no benefit for utility customers?

A. No, I do not. Both customers and shareholders benefit from a utility that enjoys strong earnings. Shareholders benefit from strong earnings directly, through an increase in the value of their investments. However, customers benefit as well—if indirectly. It is undisputed that a utility with strong earnings will enjoy stronger credit ratings, which result in lower costs of capital. These lower costs of capital result in a lower revenue requirement, and ultimately lower rates.

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[7] *WUTC v. Puget Sound Energy, Inc.*, Dockets UE-111048 and UG-111049 (consolidated), Order 08 at 42 (May 7, 2012) (approving PSE's adjustment of incentive pay in its entirety, despite half of the incentive's link to financial results).
[8] Exh. KMH-1T at 13:15-14:3.
[9] *WUTC v. Avista Corp.*, Dockets UE-991606 and UG-991607, Third Supplemental Order at ¶ 269 (Sept. 29, 2000) (noting that "two-thirds of that team's award is based on net operating income").
[10] Dockets UE-111048 and UG-111049 (consolidated), Order 08 at 42.

Q. You mentioned that the Commission has stated that it would allow recovery of compensation, including incentives, so long as the overall compensation is not above market, is reasonable, and provides benefits to utility customers. Is the Company's overall compensation consistent with market?

A. Yes. As described above, Cascade has numerous processes in place to ensure that the Company's compensation is set at a level that is consistent with market compensation, and competitive enough to attract and retain top quality talent.

Q. Has any party argued that Cascade's overall compensation is above market—for any group of employees?

A. No.

Q. As you mentioned, the Commission also requires that total compensation be reasonable and benefit customers. Do you believe that you have demonstrated that this is the case?

A. Yes. Cascade believes that compensation is reasonable when it is set at market average. And, as discussed above, we believe that all of our incentive plans benefit customers by promoting cost savings and efficiencies, safety, and customer service.

Q. Please respond to Staff and Public Counsel's proposal to remove incentive compensation allocated to Cascade from its affiliates, based on the argument that these incentives are tied to shareholder and not customer benefits.

A. As discussed above, the Company agrees to remove from the case all incentives paid out under the Executive and LTP Plans—because those incentives are provided for meeting goals that are either primarily or fully financial in nature. However, to the extent affiliate incentives are paid out under the Employee and Management Incentive Plans, we believe those should be fully recoverable.

Q. Mr. Mullins states that Cascade has conceded that incentive compensation for affiliates are not tied to ratepayer benefits.[11] **Do you agree?**

A. No. NWIGU states that Cascade made this concession in its response to Staff Data Request 109.[12] Cascade does not understand this claim. The fact is that Cascade employees benefit from the allocation of labor from affiliates in the form of significant synergies, and the skill and oversight of the corporate parent. Therefore, to the extent that incentives payments made to affiliate employees under the Employee and Senior Management Plans are properly allocated to Cascade, we believe customers benefit.

IV. SISP and SERP

Q. Does Staff propose an adjustment related to the costs of Supplemental Executive Retirement Plan (SERP) and Supplemental Income Security Plan (SISP)?

A. Yes. Staff proposes that these costs be removed from the test year revenue requirement because they related to retirement benefits that are offered only to executives, and because the Commission has disallowed such costs.

Q. Do you agree with Staff's adjustment?

A. Yes. Cascade agrees to remove these costs from the case, which decreases revenue requirement by $133,420.

V. PRO FORMA AND RESTATING WAGE ADJUSTMENTS

Q. Please summarize the Company's proposed adjustments to test year wages included in the revenue requirement in this case.

A. To adjust test year wages for the case, the Company made the following adjustments:

- Annualized test year wages for the 3.1 percent increase approved for union employees on April 1, 2016;

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[11] Exh. BGM-1T at 13:6-7 ("Cascade also indicated that the incentive payments cross charged from affiliates were not tied to any of the ratepayer benefit categories detailed in the response.").
[12] Exh. BGM-1T at 13:6-7.

- Added 2017 actual wage increases of 3.1 percent for union employees, and an average 3.97 for non-union employees;
- Added 2018 estimated increases for union and non-union employees of 3.1 percent and 4.0 percent respectively; and
- Reflecting 2017 and 2018 increases for allocated wages.

These adjustments result in a decrease to net operating income of $934,593.

Q. Does Staff propose a restating wage adjustment?

A. Yes. Ms. Hillstead explains that while the Company identified its wage adjustment as a pro forma adjustment, it actually has both a restating component (annualizing the test year wages for the union increase) and a pro forma component (for 2017 and 2018 increases). So, Staff proposes that these be separated out.

Q. Does the Company agree with this approach?

A. Yes. The Company agrees with Staff's clarification.

Q. Do any parties propose changes for the pro forma pieces of the adjustment?

A. Yes. Staff and Public oppose inclusion of adjustments for 2018 union and non-union wage increases. Public Counsel also opposes inclusion of the adjustment for both 2017 non-union wage increases.

Q. What reasons do Staff and Public Counsel give for opposing the inclusion of 2018 wage increases?

A. Staff and Public Counsel point out that the Company has not yet executed a new contract with union employees that sets wage increases for 2018—and so the Company's number is an estimate only. Staff also points out that the Company's responses to data requests indicate that the non-union increase for 2018 is based on budgets only, and for that that reason is not known and measurable.

Q. What is the Company's response with respect to non-union wage increases for 2018?

A. We have compiled the actual data supporting the increases to our non-union employees that was granted on January 1, 2018—which is a total increase of 3.64 percent. Our overall budgeted increase for 2018 is the 4.0 percent included in this case. However, we agree that off that amount, the 3.64 percent which has actually been granted is the amount that is known and measurable and should be included in this case. Exhibit No. ___(LLM-6) page 2 of 2, shows the wage increases granted as of January 1, 2018.

Q. What is your response with respect to the union increase for 2018?

A. The Company is currently in negotiations with the union and so we do not yet know that the wage increase will be for 2018. We will keep the Commission and the parties updated. The current contract is set to expire March 31, 2018, so the expectation is a contract will be in place well before the scheduled hearing in May.

Q. What reasons does Public Counsel make for opposing the 2017 non-union wage increases?

A. Public Counsel opposes the Company's 2017 non-union wage increases with the argument that the Company's workpapers suggest that one group of employees—the financial services group—received only a 3.8 percent wage increase. Public Counsel suggests that this fact indicates that the Company's 4 percent increase included in the case is not known and measurable.[13]

Q. Did non-union employees actually receive a total 4 percent wage increase in 2017?

A. The workpapers relied on by Public Counsel do not include actual increases granted. In response to Public Counsel's concerns we reviewed actual person by person increases to verify the actual increase granted in 2017. As shown in Exhibit No.__(LLM-6) page 1 of 2, the actual known and measurable wage increase granted for non-union employees for 2017 was 4.67 percent—which is the amount that should be included in the case and is reflected in Mr. Parvinen's revenue requirement calculations.

[13] Exh. DMR-1T at 12:12-15.

Q. Is the Company updating is revenue requirement in this case to capture the actual known and measurable wage increases for non-union employees for 2017 and 2018?

A. Yes. Mr. Parvinen's revenue requirement calculation included the annualization of the 2017 wage increase as adjustment R-7 in Exhibit No. ____(MPP-11). The Pro forma wage adjustment in Column P-2 of the same exhibit reflects the 4.67 percent 2017 non-union increase, the 3.64 actual 2018 non-union increase and 3.1 percent as a placeholder for the 2018 union contract, which will be adjusted for the actual union contract once ratified well before the May hearing dates. [

Q. Does this complete your testimony?

A. Yes, it does.