

**EXHIBIT NO. \_\_\_(TMH-1T)**  
**DOCKET NO. UE-06 \_\_\_/UG-06 \_\_\_**  
**2006 PSE GENERAL RATE CASE**  
**WITNESS: TOM M. HUNT**

**BEFORE THE**  
**WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION**

**WASHINGTON UTILITIES AND  
TRANSPORTATION COMMISSION,**

**Complainant,**

**v.**

**PUGET SOUND ENERGY, INC.,**

**Respondent.**

**Docket No. UE-06 \_\_\_**  
**Docket No. UG-06 \_\_\_**

**PREFILED DIRECT TESTIMONY (NONCONFIDENTIAL) OF**  
**TOM M. HUNT**  
**ON BEHALF OF PUGET SOUND ENERGY, INC.**

**FEBRUARY 15, 2006**

**PUGET SOUND ENERGY, INC.**

**PREFILED DIRECT TESTIMONY (NONCONFIDENTIAL) OF  
TOM M. HUNT**

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1 **PUGET SOUND ENERGY, INC.**

2 **PREFILED DIRECT TESTIMONY (NONCONFIDENTIAL) OF**  
3 **TOM M. HUNT**

4 **I. INTRODUCTION**

5 **Q. Please state your name, business address and present position with Puget**  
6 **Sound Energy, Inc.**

7 A. My name is Thomas (Tom) McKenna Hunt. My business address is 10885 NE  
8 4th Street, P.O. Box 97034, Bellevue, Washington, 98009-9734. I am the  
9 Director, Compensation and Benefits for Puget Sound Energy, Inc. (“PSE” or  
10 “the Company”).

11 **Q. What is your educational and professional experience?**

12 A. Exhibit No. \_\_\_(TMH-2) describes my educational and professional experience.

13 **Q. What are your duties as Director, Compensation and Benefits?**

14 A. I have the overall management responsibility for the functions of compensation,  
15 benefits, payroll, and human resources reporting. I report to the Vice President of  
16 Human Resources. I manage employees who analyze and administer  
17 compensation and benefits programs for PSE employees and retirees (directly and  
18 through third party vendors), as well as employees who prepare and distribute

1 payroll. My team administers the following programs: compensation for non-  
2 bargaining unit represented employees, employee health and welfare benefits,  
3 retirement programs, short-term and long-term disability programs, and Workers  
4 Compensation. I personally analyze executive compensation programs and  
5 provide updates to the Compensation and Leadership Development Committee of  
6 the PSE Board of Directors at their regular meetings.

7 **Q. Please summarize your testimony.**

8 A. My testimony describes PSE's compensation and benefits programs, including the  
9 Goals & Incentive Plan, and demonstrates how they are competitive and benefit  
10 the Company's customers. PSE seeks to provide a competitive total  
11 compensation program to attract and retain talented employees, while carefully  
12 managing its costs.

13 PSE's compensation package includes the following major components: salaries,  
14 health benefit plans, retirement programs, and incentive plans. The designs of  
15 these programs differ according to employee population (i.e., bargaining unit and  
16 non-bargaining unit) in response to differences in market pay practices. PSE  
17 manages its compensation expenditures through a pay for performance  
18 philosophy, which directly links employee compensation to Company and  
19 individual performance on service quality and operational efficiency objectives.  
20 Additionally, PSE offers a cafeteria plan for employee benefits that incorporates  
21 employee choice and cost sharing. These components of the Company's

1 compensation strategy keep overall compensation levels competitive with market  
2 while focusing compensation on the best performing employees. This approach  
3 helps PSE limit staff turnover which decreases costs associated with employee  
4 recruiting and training. Low turnover also results in an experienced and efficient  
5 workforce, which benefits customers.

6 **II. PSE CAREFULLY MANAGES ITS COMPENSATION**  
7 **AND BENEFIT PROGRAMS TO ATTRACT**  
8 **AND RETAIN TALENTED EMPLOYEES WHILE**  
9 **CONTROLLING COSTS**

10 **A. Salaries**

11 **Q. Does the Company provide competitive pay as compared to others in the**  
12 **industry?**

13 A. Yes. PSE participates in numerous confidential salary surveys provided by third-  
14 party consulting firms in order to compare PSE's pay programs—both base salary  
15 and variable pay—to other companies in our labor markets. PSE's annual  
16 budgeted salary increase for non-represented employees has been 3% from 1998  
17 to 2004. This places PSE within the lower end of the competitive norm for the  
18 utility industry, as shown in Exhibit No. \_\_\_(TMH-3). The 2005 salary increase  
19 budget was 3.04%, compared to an expected market range between 3.0% and  
20 4.0%. Future increases are expected to match the median in the market so that  
21 PSE can maintain competitive salaries.

1 **Q. What future challenges does the Company face in its efforts to control salary**  
2 **expense?**

3 A. Like many companies in the utility sector, PSE faces the challenge of an aging  
4 workforce. PSE's average employee age is 46, and over the next 10 years, 60%  
5 of our employees will be eligible for retirement. High retirement rates in the  
6 upcoming years will likely cause increased competition for replacement workers,  
7 which in turn may cause salary expense to increase.

8 **Q. What is the Company's strategy to deal with these future challenges?**

9 A. PSE is reviewing and seeking creative ideas to increase the retention of retirement  
10 eligible employees and ensure the Company has new sources of candidates.  
11 Labor Management meetings are being held with both unions that represent PSE  
12 employees to include the union perspective in the discussions. No specific  
13 programs have been finalized yet, but the Company is actively addressing the  
14 issue.

15 **B. Employee Benefits**

16 **Q. Please describe the Company's employee benefit plans.**

17 A. The Company offers a "cafeteria" benefit plan for employees. Employees have  
18 several choices as to type of medical plan, dental plan, life insurance, etc. so that  
19 they can determine the best fit for their situations. The Company allots a yearly

1 benefit amount to each employee that will cover the cost of basic benefits for  
2 employee-only coverage. Employees who want more benefits than this allotment  
3 contribute some of their salary to cover the additional cost.

4 **Q. Does the Company provide competitive benefit plans as compared to others**  
5 **in the industry?**

6 A. Yes. PSE's benefit program plans for both salaried employees and union/hourly  
7 employees are competitive with other benefit program plans in the Energy  
8 Services marketplace, as shown in Exhibit No. \_\_\_(TMH-4) and Exhibit  
9 No. \_\_\_(TMH-5).

10 **Q. What has the Company done to manage the cost of employee health benefits?**

11 A. Rising benefits cost is a challenge facing all employers. PSE manages these  
12 rising costs with a philosophy that combines extensive employee choice and cost  
13 sharing. The Company shares medical benefit costs with employees and retirees  
14 as a way to both reduce Company costs and create more sophisticated health care  
15 consumers. The Company's retirement program also includes a 401(k)  
16 investment plan (the "Investment Plan") with a Company matching feature that  
17 encourages employees to contribute to the plan in order to maximize Company  
18 match. PSE also provides opportunities for its employees to fully utilize IRS  
19 approved tax saving plans, such as health care spending accounts and pre-tax  
20 benefit deductions.

1 To further contain costs, the Company's health care program includes health care  
2 utilization review, case management, and wellness benefits such as physical  
3 examinations and cancer screening exams for early detection and prevention.  
4 Beginning in 2005, PSE also has begun offering voluntary employee fitness  
5 campaigns, with Company-wide communications and recognition for employees  
6 who meet the activity increase goals they set for themselves.

7 **C. Retirement Benefits**

8 **Q. What retirement benefit programs does the Company provide?**

9 A. PSE recognizes that retirement programs are crucial to attracting and retaining a  
10 skilled workforce. For active employees, PSE offers a pension plan and the  
11 Investment Plan. The PSE pension plan has two formulas for calculating benefits.  
12 IBEW-represented employees have a final average pay calculation, while the non-  
13 bargaining and UA-represented employees have a cash balance calculation. The  
14 Investment Plan provides tax-deferred savings with Company-provided matching  
15 dollars. Additionally, PSE offers a Supplemental Executive Retirement Plan for  
16 executive employees.

17 For retirees, PSE offers enrollment in group medical insurance plans if employees  
18 immediately join the plan after retirement. IBEW-represented employees receive  
19 a Company contribution towards the PSE retiree medical premiums in the amount  
20 of \$6 per month for each year of service, as negotiated by the Company and the



1 union. Current employees retiring from non-bargaining positions and UA-  
2 represented positions receive no Company subsidy toward insurance premiums.  
3 Requiring retiring employees to fund their own health insurance is becoming  
4 relatively common generally, but is still somewhat unusual in the utility industry.  
5 This represents an important cost control measure for PSE given the ever  
6 increasing costs of health care.

7 **Q. Is PSE's pension plan fully funded?**

8 A. Yes, as of December 31, 2004, the pension plan had assets of \$458,980,000 and  
9 benefits obligations of \$439,737,000, as shown in PSE's Annual Report.

10 **Q. Has PSE recently made Company contributions to the Retirement Plan?**

11 A. PSE has made contributions to the Retirement Plan up to the maximum tax  
12 deductible amount allowed so that the plan could maintain a positive funding  
13 status. Each year, distributions to retirees reduce the assets of the Plan and  
14 market conditions will increase or decrease the assets of the plan, so the current  
15 positive funding status can change over time. In 2003, PSE contributed  
16 \$26,521,000, which was deductible for tax purposes.

17 **Q. How does PSE ensure that pension funds are appropriately invested?**

18 A. PSE has a professional investment advisor and a committee of Officer and  
19 Director level employees who provide oversight of the pension plan investments,

1 including review of investment allocation and fund manager performance  
2 compared to benchmarks.

3 **III. PSE'S GOALS & INCENTIVE PLAN REWARDS**  
4 **EMPLOYEES WHEN THE COMPANY OPERATES**  
5 **EFFICIENTLY AND MEETS SERVICE QUALITY GOALS**

6 **Q. Please describe PSE's Goals & Incentives Plan.**

7 A. PSE's 2005 Goals & Incentive Plan provides all employees with the opportunity  
8 for incentive payment based on Company, team and individual performance. It is  
9 a variable incentive plan. Employees are rewarded if the Company achieves its  
10 annual goals, but a portion of employees' pay is at risk if goals are not met. The  
11 amount of pay at risk escalates based on level of position in the Company, with  
12 executives assuming the larger share of risk, due to their influence and the  
13 accountability they hold in the Company.

14 **Q. How are incentive goals established for PSE employees?**

15 A. PSE's strategic objectives are established through a long-range plan approved by  
16 the Board of Directors. From the long-range plan, annual objectives relating to  
17 service quality and operational efficiency are set by the Officers and approved by  
18 the Board of Directors each year. Team and individual goals are then formulated  
19 that reflect the Company-wide objectives. The actual incentive paid may increase  
20 or decrease depending on individual or department performance. All employees  
21 are aligned to the annual goals and incented based on the Company's performance

1 outcome for the year. Employees are encouraged to contribute ideas and efforts  
2 to help the Company achieve goals, which includes customer service, safety and  
3 cost containment ideas.

4 **Q. How do incentives apply for PSE employees who are subject to collective**  
5 **bargaining agreements?**

6 A. Represented employees are subject to the same plan terms as non-represented  
7 employees, although with a lower incentive opportunity as negotiated by the  
8 Company and the unions representing PSE's employees.

9 **Q. How is PSE's incentive plan at the corporate executive level structured?**

10 A. All employees, including Directors and Officers, participate in the Goals &  
11 Incentive Plan and are linked to the PSE goals. Every employee has a goal  
12 weighting, which means that a percentage of his or her base salary is pay at risk.  
13 Officers have a higher level of pay at risk and therefore their weighting as a  
14 percent of salary is higher.

15 **Q. What is the threshold requirement for a payout under the Goals & Incentive**  
16 **Plan?**

17 A. For any incentive payment to be possible, two threshold requirements must be  
18 met: First, PSE's earnings per share ("EPS") must exceed the "trigger" level  
19 (\$1.20/share in 2005). Second, PSE must meet or exceed its required

1 performance on at least 5 of 11 of the Service Quality Index (“SQI”) goals. In  
2 order for the 2005 Goals & Incentive Plan payment to be 100% of target level,  
3 PSE’s EPS must be \$1.35/share (the middle of the Company’s guidance range to  
4 analysts) and SQI performance must be 10 out of 11. Exhibit No. \_\_\_(TMH-6)  
5 and Exhibit No. \_\_\_(TMH-7) provide an explanation of the program.

6 **Q. How does PSE’s Goals & Incentive Plan benefit customers?**

7 A. PSE’s Goals & Incentive Plan provides three distinct benefits to customers. First,  
8 the program focuses work groups and individuals on the key objectives of the  
9 Company, including safety, reliability, customer service and operational  
10 efficiency. Customer service, safety, reliability and service quality goals clearly  
11 benefit customers, and operational efficiency translates to lower rates for  
12 customers.

13 Second, the Goals & Incentive Plan slows the base wage growth that would occur  
14 in a compensation system with base salaries only. The Company’s current plan  
15 involves significant pay at risk for all employees. The most direct benefit to  
16 customers from the structure of the Goals & Incentive Plan is that total  
17 compensation is dependent on the Company achieving its strategic objectives.

18 Third, the Goals & Incentives Plan is part of a comprehensive compensation and  
19 benefits package provided to employees that makes PSE an attractive employer to  
20 skilled, experienced talent in the market place. Customers directly benefit from

1 the contributions of a strong workforce that provides high-quality and efficient  
2 service.

3 **Q. During the 2004 general rate case, Commission Staff assumed that no**  
4 **incentive payments would be made in 2004 because the Company's projected**  
5 **earnings per share were below the incentive funding trigger. Were**  
6 **incentives paid under the 2004 Goals and Incentive Plan?**

7 A. Yes. PSE made incentive payments totaling \$7,323,000 in February 2005 to  
8 2,127 PSE employees.

9 **Q. Why were incentives paid in 2004?**

10 A. PSE's 2004 reported financial results fell below the plan funding threshold  
11 because of a regulatory disallowance that was based on Company actions that  
12 occurred prior to 2004. PSE's Compensation and Leadership Development  
13 Committee of PSE's Board of Directors determined that this out of period  
14 adjustment, relating to actions taken by the Company prior to 2004, should not be  
15 counted against employee and Company performance in 2004.

16 **Q. Does that conclude your testimony?**

17 A. Yes, it does.

18 [\[BA060420003\]](#)