

MONTANA-DAKOTA UTILITIES CO.
A Division of MDU Resources Group, Inc.

Before the Public Service Commission of North Dakota

Case No. PU-10-124

Rebuttal Testimony
of
Mark A. Del Vecchio

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

2 A. Yes. My name is Mark A. Del Vecchio and my business address is
3 1200 West Century Avenue, Bismarck, North Dakota 58503.

4 **Q. Who are you employed by and what is your position?**

5 A. I am employed by MDU Resources Group, Inc. (MDU Resources)
6 as Vice President – Human Resources.

7 **Q. Describe your education and work experience.**

8 A. I have a Bachelor of Arts degree in Psychology from the College of
9 St. Thomas and a Master of Arts degree in Industrial Relations from the
10 University of Minnesota. I also hold a Juris Doctor degree from William
11 Mitchell College of Law.

12 My work experience includes 15 years in various human resource
13 positions both at the field and corporate level with large, multi-national
14 companies and seven years consulting on compensation, benefits, and
15 executive compensation for client companies. In 2003, I joined MDU
16 Resources as the Director of Compensation and Benefits where I was
17 responsible for program design, funding, compliance, and administration
18 of base pay, variable pay, long-term incentive, health, welfare, and
19 retirement programs. I also led the SEC compliance effort regarding proxy
20 statement preparation. In 2007, I assumed my current position of Vice

1 President – Human Resources. In my current position, I maintain
2 responsibility for many of the duties I was assigned as Director of
3 Compensation and Benefits; but I am also now responsible for strategy
4 development, Board interface, and assisting MDU Resources' Business
5 Units on their human resource initiatives.

6 **Q. Have you reviewed the testimony of Mr. George Mathai in this**
7 **proceeding?**

8 A. Yes, I have.

9 **Q. Do you agree with Mr. Mathai's recommendation to exclude 60**
10 **percent of the incentive compensation paid to employees of**
11 **Montana-Dakota from consideration in establishing retail electric**
12 **rates for Montana-Dakota?**

13 A. No. Incentive compensation is a well recognized component of
14 employee compensation and is a legitimate business expense in providing
15 utility services to the Company's customers.

16 **Q. Describe the general components and objectives of an employee**
17 **compensation package for MDU Resources of which Montana-**
18 **Dakota is a subsidiary of.**

19 A. Employee compensation packages generally consist of three
20 components: (a) base salary; (b) benefits; and (c) incentive compensation.
21 Base salary targets, employee benefit levels, and incentive opportunity
22 targets are established to ensure the ability to attract and retain the talent
23 necessary to run the MDU Resources' various business lines. The
24 Company's ability to maintain a competitive total remuneration package
25 helps avoid employee turnover. High employee turnover could impede the
26 safe and reliable delivery of low-cost service.

1 **Q. Is incentive compensation unusual as a component of employee**
2 **compensation for investor owned public utilities?**

3 A. No, it is not unusual; it is the norm. For example, Mercer
4 Consulting, a large compensation, benefits, and actuarial consulting firm,
5 reported in their 2008 / 2009 U.S. Compensation Planning Survey, that
6 over 80% of companies in the energy industry provides annual incentives
7 for their employees.

8 **Q. Why does MDU Resources and Montana-Dakota include incentive**
9 **compensation as a component of employee compensation?**

10 A. Incentive compensation aligns a portion of the employee's
11 compensation for the performance of his/her duties and responsibilities
12 with specific goals and objectives of the Company. It places that portion
13 of the employee's compensation at risk if these goals and objectives are
14 not achieved.

15 **Q. Do you agree with Mr. Mathai's observation that performance**
16 **incentives are beneficial to both shareholders and customers?**

17 A. Incentive compensation, like base salary and benefits, is paid to the
18 employee for performance of the assigned job duties and responsibilities.
19 The performance of these duties and responsibilities, in furtherance of the
20 Company's utility business is of course beneficial to both the owners of the
21 business as well as the customers of the business. This is no different
22 than compensation paid to employees of any business – performance of
23 the employees' duties benefit both the owners and customers of the
24 business.

25 **Q. Does this apply even when one of the considerations of the incentive**

1 **compensation is financial performance of the Company?**

2 A. Yes. To achieve sufficient earnings quality means, among other
3 things, operations and maintenance costs are controlled, the electric
4 system is running efficiently, and assets are utilized to their fullest extent.
5 These are achieved through successful performance of employees' job
6 duties. Achieving earnings quality and operational goals means the
7 Company has efficiently utilized its assets and avoided unanticipated
8 costs. This, in turn, promotes the longevity of the utility system and
9 reduces the need for price increases.

10 **Q. Why do you disagree with Mr. Mathai's recommendation that a**
11 **portion of incentive compensation should be excluded from**
12 **consideration in determining the Company's revenue requirement for**
13 **setting rates?**

14 A. Employee compensation, including incentive compensation, is a
15 prudent and legitimate business expense. While prudent and legitimate
16 expenses incurred in furtherance of the Company's business certainly
17 benefit both owners and customers, recovery of a Company's prudent and
18 legitimate business expense through its prices is necessary to the long
19 term sustainability of the business. If a portion of the Company's prudent
20 and legitimate business expenses are excluded from recovery in setting
21 the Company's rates, the Company is denied a fair opportunity to earn the
22 required return on its invested capital.

23 **Q. Do MDU Resources and Montana-Dakota review their employee**

1 **compensation packages to assure they are both competitive and**
2 **reasonable?**

3 A. Each year MDU Resources' major business units, including
4 Montana-Dakota, review the base salary structure of approximately one-
5 third of the jobs in their general compensation plans. MDU Resources
6 uses two major salary survey sources – Salary.com and WM Mercer to
7 price positions (i.e., determine a competitive salary). Montana-Dakota
8 uses Towers Perrin, Watson Wyatt, Salary.com and American Gas
9 Association for benchmarking studies regarding salary.

10 Positions are grouped together according to their current salary
11 class. Data points from the salary survey sources are averaged and
12 compared to the midpoint of the salary class for each position. For the
13 majority of positions the Company is usually competitive (i.e., the salary
14 class midpoint is close to the average of the surveys); however, from time
15 to time there are aberrations. These positions are generally watched for a
16 couple of years and then a decision is made as to whether the position is
17 slotted in the correct salary class. Also, the aggregate average of the data
18 points is compared to the midpoint of each salary class, which indicates
19 whether or not our structure is aligned with the market. In our most recent
20 review, the midpoint of the vast majority of the MDU Resources and
21 Montana-Dakota salary classes were less than five percent above or
22 below the survey averages.

23 From an incentive compensation standpoint, the analytical

1 framework is identical to the above mentioned approach on base salaries;
2 we compare a position's target incentive percentage to the target incentive
3 percentage noted in the various salary surveys. We conduct this analysis
4 every three or four years, and the most recent analysis, which was two
5 years ago, was not retained. In general, however, MDU Resources' target
6 incentives were slightly above the market survey incentives while
7 Montana-Dakota's were roughly aligned with the market survey.

8 Finally, benefit packages of our major business units are
9 periodically reviewed to assure they are competitive, reasonable and
10 consistent with those offered by other employers in similar industries. In
11 recent years the employee benefit plans at MDU Resources and Montana-
12 Dakota have been revised significantly. For example, as discussed in the
13 direct testimony of Mr. David Goodin, the defined benefit pension plan was
14 frozen and the defined contribution plan increased, the utility discount for
15 active employees was eliminated, and the retiree medical plan was
16 substantially revamped.

17 **Q. Did you review Mr. Mathai's recommendation to exclude 50 percent**
18 **of the fees and expenses incurred for the Company's Board of**
19 **Directors?**

20 A. Yes, I did.

21 **Q. Do you agree with Mr. Mathai's recommendation?**

22 A. No, I do not.

23 **Q. Please explain why you do not agree with the recommendation.**

1 A. Like employee compensation, fees and expenses incurred for the
2 Company's Board of Directors are prudent and legitimate business
3 expenses. Recent statutory and regulatory requirements imposed on
4 publicly traded companies such as the Sarbanes-Oxley Act of 2002 have
5 necessitated a heightened involvement by an independent board of
6 directors on the oversight of the Company's business activities. The fees
7 and expenses incurred for an independent board of directors is essential
8 to the Company's ability to raise capital at competitive rates to fund its
9 ongoing operational needs. Mr. Mathai recognizes that these expenses
10 benefit both the Company's customers and shareholders, but then
11 arbitrarily recommends exclusion of 50 percent of these legitimate
12 expenses. Like all legitimate business expenses, the director fees and
13 expenses are incurred in furtherance of the Company's business which
14 must be recovered in its prices. The fact that oversight of the Company's
15 business provides benefits to both shareholders and customers is not a
16 basis for exclusion in setting rates.

17 **Q. Does this conclude your rebuttal testimony?**

18 A. Yes, it does.