BEFORE THE
NEW YORK STATE
PUBLIC SERVICE COMMISSION

--x

Proceeding on Motion of the Commission as to the Rates, Charges, Rules and Regulations of Central Hudson Gas & Electric Corporation for Electric Service — Case 17-E-____

--x

--x

Proceeding on Motion of the Commission as to the Rates, Charges, Rules and Regulations of Central Hudson Gas & Electric Corporation for Gas Service — Case 17-G-____

--x

DIRECT TESTIMONY OF
SHARON A. MCGINNIS
(STAFFING, COMPENSATION, AND BENEFITS)

July 28, 2017

DIRECT TESTIMONY OF SHARON A. MCGINNIS

TABLE OF CONTENTS

DIRECT TESTIMONY OF SHARON A. MCGINNIS

I. INTRODUCTION

Q. Please state your name and business address.

A. My name is Sharon A. McGinnis. I am employed by Central Hudson Gas & Electric Corporation ("Central Hudson" or the "Company"), and my business address is 284 South Avenue, Poughkeepsie, New York 12601.

Q. In what capacity are you employed by Central Hudson Gas and what is your scope of responsibilities?

A. I am the Vice President of Human Resources & Safety. I am responsible for the staffing, training and development of Central Hudson employees, employee and labor relations, and the development and administration of compensation and benefits policies and procedures for Central Hudson. I am also responsible for Central Hudson's safety program as well as the Company's Legal Compliance, Ethics and Privacy programs and policies.

Q. Please summarize your educational background and professional experience.

A. In 1991, I received a Bachelor of Science in Business Administration from State University of New York at New Paltz. I have worked at Central Hudson since June 2009. Prior to June 2009, I worked at the Dow Jones Local Media Group as Vice President of Human Resources. During my career I have held positions with responsibility for labor relations, employee relations, employee benefits, compensation, training and development, employment, payroll, and safety.

DIRECT TESTIMONY OF SHARON A. MCGINNIS

Q. Have you previously testified before the New York State Public Service Commission ("PSC" or the "Commission")?

A. Yes, I testified in Central Hudson's last two rate cases, Cases 14-E-0318 and 14-G-0319 regarding staffing, compensation and benefits.

II. PURPOSE OF TESTIMONY

Q. What is the purpose of your testimony in these proceedings?

A. The purpose of my testimony is to address employee compensation and benefits (health care, pensions, including the Supplemental Executive Retirement Plan ("SERP"), and other post-employment benefits ("OPEBs")) as well as staffing. I describe the Company's overall approach to compensation for management employees and the basis for Central Hudson's view that its approach to compensation and benefits is appropriate. I describe generally the retirement benefits offered by the Company. I have also developed a forecast of the staffing level for the twelve months ending June 30, 2019 ("Rate Year") and quantified the cost associated with the incremental positions and provided that estimate to the Revenue Requirements Panel.

Q. Are you sponsoring any exhibits?

A. Yes, I am sponsoring the following exhibits:

1. Exhibit __ (SAM–1) (Actual Permanent Employees as of March 31, 2017); and
2. Exhibit __ (SAM–2) (Incremental FTEs and Descriptions).

DIRECT TESTIMONY OF SHARON A. MCGINNIS

III. BENEFITS

Q. Has the Company adopted any further structural changes to its pension, OPEBs, or health plans subsequent to those described in Cases 14-E-0318 and 14-G-0319?

A. No, we have not. The Company previously closed its defined benefit pension plan to employees hired on or after January 1, 2008 (management employees) and on or after May 1, 2008 (bargaining unit employees). The cost reductions that resulted from closing the plan are reflected in current rates and in the historic period.

Q. How has the Company continued to manage OPEB expense?

A. The Company continues to control and reduce costs associated with its OPEB program through the structural changes to the program reflected by the Commission in Cases 14-E-0318 and 14-G-0319. These cost control measures include: 1) closing the retiree life insurance and retiree health coverage plans to new hires; 2) implementing a maximum amount or "cap" on Company contributions for retirement health insurance plan participants who are eligible for Medicare; 3) implementing cost sharing mechanisms for new and existing retirees for retiree health and prescription drug plans; and 4) reducing the life insurance plan for eligible non-union employees hired before January 1, 1984. Since the elimination of retiree life insurance plans and retiree health care plans primarily affect new hires, the Company will continue to experience increasing control and/or reduction in OPEB plan costs as a growing percentage of OPEB plan participants will become subject to these cost control measures.

Q. Has the Company considered and rejected any further initiatives to reduce or control OPEB expense?

A. No.

Q. Has Central Hudson modified its contribution levels for the defined contribution plan since the Commission's Order Approving Rate Plan ("2015 Rate Plan") in Cases 14-E-0318 and 14-G-0319?

A. Yes, effective July 1, 2017 and as part of the new five-year collective bargaining agreement discussed later in this testimony, the Company has modified the matching contribution it makes to the defined contribution ("DC") plan for its union employees hired before May 1, 2008 from 46% of the first 6% of base wages that an employee defers to 50% of the first 6% of base wages that an employee defers. This change is not currently reflected in the determination of revenue requirements, but will be incorporated at the time of Brief on Exceptions when the Company updates for latest known contribution levels to the Savings Incentive Plan ("SIP"), as requested by the Revenue Requirements Panel.

Q. Has Central Hudson introduced any new employee benefits since the 2015 Rate Plan?

A. Yes. Central Hudson introduced the Employee Share Purchase Plan ("ESPP").

DIRECT TESTIMONY OF SHARON A. MCGINNIS

Q. What is the Employee Share Purchase Plan?

A. The ESPP is a voluntary benefit that allows employees the opportunity to purchase shares of Fortis Inc. common stock on the Toronto Stock Exchange. It was first offered to employees in May 2017. Employees may invest between 1% and 10% of their annual base pay to the program, with the aggregate contribution not to exceed 10% of their annual base pay in any calendar year. Central Hudson will contribute 10% of the employee’s contribution to purchase shares, as well as an amount equal to 10% of all dividends payable on the employee’s ESPP shares, as long as the employee remains in the plan.

Q. Why does Central Hudson believe this is a benefit to employees and customers?

A. The ESPP gives full-time and part-time employees, including executives, a convenient way to become Fortis Inc. shareholders and build their long term equity savings. In addition, it is an effective tool for attracting, retaining, and motivating employees to achieve corporate goals, resulting in better service to our customers.

Q. What is the projected expense associated with the ESPP and how was the projection developed?

A. The total projected expense associated with the ESPP is $94,396 in 2017, $250,825 in 2018, and $294,807 for the Rate Year. These expenses are allocated to electric and gas expense based on the normalized labor distribution as calculated by the Revenue Requirements Panel. As such, the revenue requirement for the Rate Year includes expense of $151,590 for electric operations and $45,607 for gas operations for this program. In order to develop the projection, the Company gathered participation and contribution data from a sample of Fortis subsidiaries who currently offer the plan to employees. We assumed a gradual phase-in of participation over the first two years to arrive at the average participation noted by the other Fortis subsidiaries, with participation leveling out once the plan is established. This projection was provided to the Revenue Requirements Panel.

IV. <u>COMPENSATION</u>

Q. Please describe Central Hudson's overall compensation strategy and philosophy.

A. Central Hudson believes that there are several components to compensation, with each component contributing to the total compensation package. It is this total compensation package (not its individual components in isolation) that is evaluated in the employment market. Therefore, the Commission should evaluate the Company's total compensation package, including incentive compensation, as a whole rather than consider its components individually.

Q. Why is it important to Central Hudson to maintain a total compensation program that is competitive in the employment market?

A. Maintaining a total compensation program that is competitive in the employment market is crucial to Central Hudson's ability to retain the high quality employees it currently employs and to attract high quality candidates for existing or new staffing requirements. The Company's ability to attract high quality candidates is imperative not only to meet the incremental staffing needs as described later in testimony, but also to fill anticipated vacancies, as a significant number of experienced employees prepare to retire. The Company will be seeking new, high quality employees to fill these positions. Maintaining the competitiveness of Central Hudson's total compensation program has become even more important as the portion of our workforce without a defined benefit pension and without life and health coverage in retirement continues to grow. If Central Hudson is unable to maintain a competitive total compensation program, it may put the Company's ability to respond to emergencies, operating performance, customer service quality, and customer satisfaction at needless risk of deterioration.

Q. Do the age demographics of Central Hudson's employees track the demographics of the utility industry in general?

A. Yes. Central Hudson's demographics indicate that roughly 15% of the workforce will retire within the next five years. As a result, Central Hudson will need to attract new high quality employees and retain existing high quality employees. To augment recruiting efforts, the Company has begun using headhunters for hiring select management positions. The fee for this service as provided by Robert Half staffing agency is 30% of the candidate's starting salary. It is assumed that, on average, the Company will use a headhunter to recruit and fill three open positions annually. This information, along with the assumptions for the cost projection, was provided to the Revenue Requirements Panel and is reflected in the 'Consulting and Professional Services' element of expense.

Q. Please describe Central Hudson's cash compensation program for non-executive, non-unionized employees and how Central Hudson manages the costs of the program.

A. Central Hudson has adopted a strategy to compensate employees with base salaries at the 50th percentile of overall compensation for comparable jobs in the Northeast United States. We employ the services of Pearl Meyer & Partners, a nationally recognized compensation consultant, to establish the range of those salaries. We believe paying at the median level provides the Company with the ability to attract new qualified employees and retain its existing quality employees. Targeting compensation at the median level keeps the Company competitive and manages costs through adherence to this level of compensation.

Q. Is the compensation approach applied to Central Hudson's executives similar to the approach described above for the non-executive, non-unionized employees?

A. Yes, it is. Central Hudson uses Frederic W. Cook & Co., Inc. ("Cook"), a nationally recognized executive compensation consultant, to establish the median level of salaries for Central Hudson's executives. Through the use of this consultant, Central Hudson benchmarks its executive positions to the 50th percentile of overall compensation for comparable jobs in similarly sized companies.

Q. Why did the Company utilize different compensation consultants for compensation benchmarking purposes?

A. The industry practice is to utilize an executive compensation consultant that does not have a management consulting business in order to establish an atmosphere of independence and the Company agrees it is sound business practice to employ two different and independent compensation consultants. The retention and use of Cook as an executive compensation consultant was within the discretion and responsibility of the Governance and Human Resources Committee of Board of Directors of the Company, while the Human Resources division determined which compensation consultant the Company would use for the management organization.

Q. Was a collective bargaining agreement in place between the Company and its union workers during the historic period (twelve months ending March 31, 2017)?

A. Yes. A five year collective bargaining agreement that became effective on May 1, 2011 and was extended by one year was in effect through the historic period, covering about 575 employees. There is another collective bargaining agreement for about 25 employees in the System Operations area that is effective from April 1, 2016 through March 31, 2018, which was also in effect through the historic period.

DIRECT TESTIMONY OF SHARON A. MCGINNIS

Q. Will these same collective bargaining agreements be in place during the forecast Rate Year period?

A. No. A new, five-year collective bargaining agreement was ratified on May 5, 2017, by IBEW Local 320, the union that represents the majority of Central Hudson's unionized workers. In January of 2018, the Company and union will begin negotiating a new contract for System Operations.

Q. What are the negotiated wage increases for union employees from the end of the historic year ended March 31, 2017 through the Rate Year?

A. The current labor agreement ratified May 5, 2017 provides for a 2.75% wage increase on May 1, 2017 and another 2.75% wage increase on May 1, 2018. Subsequent wage increases of 3.0% per year will take effect on May 1 of each of the next three years. These approved wage increases are reflected in the calculation of labor expense included in the revenue requirement. The current labor agreement expires on April 30, 2022.

Q. What are the projected payroll increases for non-union employees from the end of the historic year ended March 31, 2017 through the Rate Year?

A. An assumed overall compensation increase of 3.0% from the March 31, 2017 level was employed effective March 1, 2018 and March 1, 2019 to forecast the Rate Year payroll for non-union employees.

DIRECT TESTIMONY OF SHARON A. MCGINNIS

Q. What elements of employee compensation are reflected in the Company's revenue requirement?

A. The Company is requesting revenue requirements for all base wages and overtime compensation for its unionized workforce. In connection with non-union employees, the Company is requesting the following:

- For its management Foreman positions, the Company is requesting revenue requirements for base salaries and overtime;
- For all other non-Foreman, non-executive management positions, the Company is requesting revenue requirements for base salaries only; and
- For its Executive management positions, the Company is requesting revenue requirements associated with base salaries and short-term incentive compensation.

Q. Why is the Company requesting revenue requirements associated with both base salaries and incentive compensation for its Executive management positions?

A. The Company's executive compensation program is designed to offer compensation opportunities that are competitive with opportunities offered by comparable companies in the markets in which the Company competes for executive talent. This program consists of base salary, short-term and long-term incentives, and retirement benefits and is geared to be close to market median levels. Studies conducted by Cook found that the Company's executive pay practices, inclusive of incentive compensation, are consistent with its compensation philosophy which targets compensation in the median range. Cook studies also confirmed that executive compensation levels, inclusive of incentive compensation, are aligned with market median practice.

Q. Is the Company seeking revenue requirements for the long-term incentive component of executive compensation?

A. No. The Company is not seeking revenue requirements for the long-term incentive component of executive compensation because of its focus on financial metrics and total shareholder returns, rather than on metrics tied to the delivery of safe and reliable service to customers.

Q. Why is the Company seeking revenue requirements for the short-term incentive component of executive compensation?

A. The short-term incentive compensation component of executive compensation provides benefits to ratepayers in that it is designed to reward achievement of safety and reliability targets including:

- Commission gas safety code rule compliance;
- Eight key Commission gas safety metrics;
- All Injury Frequency Rate;
- Preventable Motor Vehicle Accidents;
- System Average Interruption Frequency Index ("SAIFI"); and
- Customer Average Interruption Duration Index ("CAIDI").

DIRECT TESTIMONY OF SHARON A. MCGINNIS

Q. What is the Company required to demonstrate in order for incentive compensation to be included in its revenue requirements?

A. In its Order Establishing Rates for Electric Service for Orange and Rockland, issued June 17, 2011 in Case 10-E-0362, the Commission provided two alternative methods by which a company can demonstrate that incentive compensation should be included in revenue requirements. First, a company may "demonstrat[e] that overall base pay, including [incentive compensation], was reasonable relative to similarly situated companies, and that the inclusion of [incentive compensation] in base pay did not render the Company's total compensation unreasonable." Case 10-E-0362 at 39. Alternatively, a company can make "a very clear, affirmative demonstration that these above base pay incentive compensation programs are designed to return quantifiable or demonstrable benefits to ratepayers in a financial sense or in terms of reliability, environmental impact, or customer service." Id. at 38.

Q. Do the Commission's standards for recovery of incentive compensation differ for executive and non-executives?

A. No. The Commission's standards announced in Case 10-E-0362 do not make any distinction between executive and non-executive incentive compensation; both are evaluated under the same standards.

DIRECT TESTIMONY OF SHARON A. MCGINNIS

Q. Is the Company's total executive compensation, including its short-term incentive compensation, reasonable in relation to similarly situated companies?

A. Yes. As discussed previously in my testimony, the total compensation package offered by the Company, including the Company's short-term compensation, is geared to be close to the median level of compensation at similarly situated companies. The Cook studies performed at the Company's request confirmed that the total executive compensation level, including both short- and long-term compensation, are aligned with the Company's practice to meet the market median. Therefore, the Company satisfies the Commission's first standard for the inclusion of short-term executive incentive compensation in the Company's revenue requirement.

Q. Is the Company's short-term incentive compensation for executives "designed to return quantifiable or demonstrable benefits to ratepayers in a financial sense or in terms of reliability, environmental impact, or customer service"?

A. Yes. As discussed previously in my testimony, short-term incentive compensation for the Company's executives is tied to several safety and reliability metrics designed to better serve ratepayers. The performance standards for short-term incentive compensation include targets directly tied to the Company's performance towards the Commission's gas safety rules and metrics as well as well-known electric reliability indices, SAIFI and CAIDI. Further, as discussed earlier in my testimony, the Company is not requesting to include incentive compensation related to long-term financial goals in its revenue requirement. Therefore, the Company satisfies the Commission's second standard for the inclusion of short-term executive incentive compensation in the Company's revenue requirement.

Q. Describe the compensation program for non-executive, non-union employees.

A. The Company employs an annual merit compensation increase for non-executive, non-union employee compensation. An annual merit compensation increase is established utilizing guidance from our compensation consultants and does not contain any additional bonus or incentive-based compensation for the non-executive, non-union employees.

Q. Is the overall compensation increase set within the basic parameters of the general market-based wage increases, excluding compensation for traditional incentive-based compensation?

A. Yes.

V. <u>STAFFING</u>

Q. What was the Company's staffing level as of the end of the historic period?

A. As of March 31, 2017, Central Hudson had 1,009 employees, including officers, full-time management employees and full- and part-time union employees.

DIRECT TESTIMONY OF SHARON A. MCGINNIS

Q. How does the staffing level at March 31, 2017 compare to what was approved in Rate Year 3 of the 2015 Rate Plan?

A. The staffing level of 1,009 on March 31, 2017, is 33 higher than the 976 allowed in Rate Year 3 of 2015 Rate Plan.

Q. Can you identify where the additional 33 positions were assigned in the organization?

A. No. Because the allowed staffing levels included in the revenue requirement in the 2015 Rate Plan reflect a staffing level reached through settlement negotiations on a global basis, it is impossible to identify the staffing level by position that was provided for in rates. It should also be noted that, in July 2015, the first month of Rate Year 1 ("RY1") in the 2015 Rate Plan, the Company had actual staffing levels that exceeded the RY1 allowed staffing level by 25 full time equivalents ("FTE").

Q. Is Central Hudson proposing to add incremental employees from the end of the historic period through the Rate Year?

A. Yes. Central Hudson proposes to add 68 incremental employees during that time, raising the staffing level from 1,009 at the end of the historic period to 1,077 for the Rate Year. Exhibit __ (SAM–2) identifies the positions that the Company proposes to add and any positions that have been filled as of the date of the filing of this testimony.

Q. Why is Central Hudson planning to add 68 incremental employees?

A. Exhibit __ (SAM-2) identifies the additional 68 positions and includes a description of why each of the 68 incremental positions is necessary. I quantified the effect of these incremental employees and provided this information to the Revenue Requirements Panel.

Q. Does the Company's proposal assume that there will be losses of existing employees between the end of the historic period (March 31, 2017) and the start of the Rate Year (July 1, 2018)?

A. The Company's proposal assumes that, if there are any losses of existing employees, they will be replaced – so that any losses will be offset by replacements. Therefore, the proposal assumes there will be a net result of zero losses of existing employees from the Company's current staffing level.

VI. SUPPLEMENTAL EXECUTIVE RETIREMENT PLAN

Q. Would you please provide an overview of Central Hudson's Supplemental Executive Retirement Plan?

A. The SERP is designed to preserve a prior benefit formula for a closed group of eligible executives. The SERP provides the executives who have a minimum of 30 years of service at the age of 61 with 57% of their pension-eligible earnings (defined as the highest 3 consecutive calendar years during the 10 consecutive calendar years immediately preceding termination of employment), less the amounts received under the Retirement Income Plan and Benefit Restoration Plan. Individuals having less service or retiring prior to age 61 have their benefits reduced according to provisions in the SERP.

DIRECT TESTIMONY OF SHARON A. MCGINNIS

Q. Are you seeking rate recovery of costs associated with the SERP?

A. Yes. We believe this program is a key component of our executive compensation program and delivery rates should be designed to allow for recovery of this cost. Preserving prior benefit formulas for a closed group of executives is a typical transition method and is an accepted practice in the employment market. Costs associated with SERP were approved by the Commission in Cases 14-E-0318 and 14-G-0319.

Q. Have any remedial actions been taken to reduce the costs of this program?

A. Yes. In 2008, we closed the Retirement Income Plan and SERP to new entrants. There are currently 6 active employees, 1 deferred vested employee, and 11 retired participants and/or surviving spouses in the SERP.

Q. Does this conclude your direct testimony at this time?

A. Yes, it does.