

Direct Testimony
Laura A. Patterson

Before the South Dakota Public Utilities Commission of
the State of South Dakota

In the Matter of the Application of
Black Hills Power, Inc., a South Dakota Corporation

For Authority to Increase Rates
In South Dakota

Docket No. EL12-____

December 17, 2012

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EXHIBITS

None

1 **I. INTRODUCTION AND QUALIFICATIONS**

2 **Q. PLEASE STATE YOUR NAME, BY WHOM YOU ARE EMPLOYED, AND**
3 **COMPANY ADDRESS.**

4 A. My name is Laura A. Patterson and I am employed by Black Hills Service
5 Company, a wholly-owned subsidiary of Black Hills Corporation (“BHC” or
6 “Corporation”). My business address is 625 9th Street (4th Floor), Rapid City, SD
7 57701.

8 **Q. PLEASE DESCRIBE YOUR POSITION WITHIN THE COMPANY AND**
9 **AREAS OF RESPONSIBILITY.**

10 A. I am the Director of Compensation, Benefits and Human Resources Information
11 Systems (“HRIS”) for BHC. In my position, I am responsible for partnering with
12 business leaders to design and execute compensation and benefits strategies and
13 plans. I also provide input related to strategic planning, implementation and
14 administration of compensation and benefits programs, executive plans, equity
15 programs, non-qualified plans and other initiatives. My responsibility would also
16 cover employees working for Black Hills Power, Inc. (“Black Hills Power” or the
17 “Company”).

18 **Q. WOULD YOU BRIEFLY SUMMARIZE YOUR ACADEMIC AND**
19 **PROFESSIONAL BACKGROUND?**

20 A. I have more than 23 years of experience in compensation and benefits, with
21 responsibilities including the development, management, administration and
22 regulatory compliance of such plans. I began my current position as Director of

1 Compensation, Benefits and HRIS for BHC in April 2009. Prior to this position, I
2 spent 6 years as Director of Compensation, Benefits and HRIS and 2 years as
3 Employee Benefits Manager, for PNM Resources, Inc. (PNMR), where I was
4 responsible for managing and administrating all compensation and benefit
5 programs for PNMR, its subsidiaries and for its joint venture business with
6 Cascade Investments, Optim Energy. Prior to working for PNMR, I was employed
7 as a Tax Manager and Human Capital Consultant for four years at Arthur
8 Andersen, a global tax and consulting firm. In this position, I worked with
9 organizations to identify, analyze and apply regulatory rules that govern structure,
10 compliance, and administration of employee benefit plans. Prior to Arthur
11 Andersen, I was employed as a Trust Officer at Mercantile Trust Company from
12 1995 to 1999. My primary responsibilities included managing, administration of,
13 and the sales of profit sharing, 401(k), and defined benefit pension retirement
14 plans sponsored by a wide range of clients. I have a Bachelor of Business
15 Administration degree from the University of Iowa.

16 **Q. DESCRIBE YOUR PROFESSIONAL ASSOCIATIONS.**

17 A. I serve on the Corporate Board of Directors of the International Foundation of
18 Employee Benefit Plans and serve on the Employee Benefits Committee for the
19 U.S. Chamber of Commerce. I am also a Certified Retirement Services
20 Professional.

1 **II. PURPOSE OF TESTIMONY**

2 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?**

3 A. I describe and support the general compensation program for BHC employees,
4 and particularly the employees of Black Hills Power, including the variable
5 compensation program, and explain why those programs and their associated
6 costs are reasonable and necessary to attract, motivate and retain well qualified
7 and competent employees to support utility operations, to support recovery of the
8 compensation-related expenses of BHC employees. Black Hills Power
9 employees, both non-union and union, participate in the compensation and benefit
10 plans sponsored by BHC.

11 I also describe and support the general benefits programs and policies for BHC
12 employees, particularly the employees of Black Hills Power, including the health,
13 welfare and retirement benefits, and explain why those programs and their
14 associated costs are reasonable and necessary.

15 My testimony specifically supports employee compensation related adjustments,
16 including retiree healthcare, pension plan, pooled medical, and 401(k) plan, that
17 are part of the overall benefits adjustment made in Schedule H-6 in the Black
18 Hills Power revenue requirement model.

19 In addition, my testimony will explain why the strategic workforce process
20 programs discussed in Mr. Loomis' testimony are reasonable and necessary to
21 attract, motivate and retain well qualified and competent employees to support
22 utility operations.

1 **III. COMPENSATION PHILOSOPHY AND PROGRAMS**

2 **Q. WHAT IS BHC’S GENERAL COMPENSATION PHILOSOPHY?**

3 A. BHC’s compensation philosophy is designed to attract, retain, and motivate
4 employees to achieve appropriate business results. All compensation programs
5 are designed to meet the following principles:

- 6 • *Strategically Aligned* – Compensation practices reinforce each business
7 segment’s business strategy, structure, needs and culture.
- 8 • *Externally Competitive* – Each component of compensation (including base
9 and variable compensation) should be competitive at the median of the
10 relevant labor market. Base pay is intended to compare to the market
11 median of the labor market and reflect the individual’s sustainable
12 performance levels over time. Variable compensation should also compare
13 to the market median and reflect the individual’s contribution to business
14 unit and Company results.
- 15 • *Internally Equitable* – Pay grades assigned to jobs within the Company
16 should fairly reflect their value relative to other jobs in the Company. The
17 metrics utilized for recognizing performance should inspire confidence in
18 BHC among its employees, customers and the communities it serves.
- 19 • *Personally Motivating* – The compensation system should recognize
20 employees based on differences in individual contribution.
- 21 • *Cost Effective* – programs are designed to provide maximum value to BHC
22 and its customers in relation to the cost involved.

- 1 • *Legally Compliant* – Programs are in compliance with all applicable state
2 and federal laws and regulations.

3 **Q. PLEASE DESCRIBE BHC’S COMPENSATION PROGRAMS.**

4 A. There are two primary components to the compensation program – Base Salary
5 and Variable Pay programs.

- 6 • Base Salary: Base salary represents the fixed portion of an employee’s total
7 cash compensation opportunity. Base salary compensation is determined
8 by the market value of the job, specific performance standards and
9 competencies. Base salaries are reviewed on an annual basis and merit
10 salary increases are based on individual performance and contributions.

11 Base rates of pay for Black Hills Power’s union employees are established
12 under the terms of the collective bargaining agreement with the
13 International Brotherhood of Electrical Workers (“IBEW”) Local 1250.

- 14 • Variable Pay: Variable Pay is pay at risk that is earned and is not fixed or
15 guaranteed. All BHC employees (non-union and union) participate in the
16 Annual Incentive Plan (AIP) which is described in detail later in this
17 testimony.

18 **Q. PLEASE EXPLAIN BHC’S PHILOSOPHY ON BASE PAY**
19 **COMPENSATION.**

20 A. Base pay is intended to reflect the median of the market for similar positions in
21 similar companies. There are twenty-three (23) pay grades which are used for all
22 non-executive, non-union jobs. Each grade has a minimum, midpoint, and a

1 maximum pay level. This means that the pay ranges within the grades are
2 competitive with what other companies pay for similar positions. All jobs are
3 compared to the market, where data exists, and placed in the grade where the
4 midpoint of the range is closest to the average market rate for that job. BHC
5 implemented a single, unified salary structure in early 2009 after the close of the
6 purchase of the Aquila properties. Towers Watson conducted an independent
7 market review of the BHC's positions in 2009 and benchmarked each position to a
8 BHC salary grade based midpoint, which were designed to closely reflect the
9 market median values. Subsequent to the market review of all positions in 2009,
10 the Human Resources Compensation Department periodically reviews each
11 position in the company to ensure that current compensation remains within the
12 competitive range.

13 Market rates are determined by utilizing compensation survey data where
14 companies report actual compensation paid to employees by position. The survey
15 most widely used by BHC is from Towers Watson, as they are recognized
16 nationally as the leader in the energy services / utility market place.

17 **Q. IN ADDITION TO THE TOWERS SURVEY, ARE THERE ANY OTHER**
18 **SURVEYS THAT BHC UTILIZES TO ENSURE THAT ITS OVERALL**
19 **COMPENSATION IS COMPETITIVE IN COMPARISON WITH OTHER**
20 **COMPANIES?**

21 A. Yes. BHC also utilizes surveys conducted by Aon Hewitt, Mercer, the Edison
22 Electric Institute (EEI), ECI, the EAPDIS, LLC, and other surveys, including

1 several specific to wages by state. The surveys provide compensation and other
2 data for each position by company size, revenue, and number of employees so that
3 BHC can match each of its positions to positions in the market that are most
4 similar in duties and most similar for the company size/revenue.

5 **Q. HOW DO THE COMPANY'S COMPENSATION STRATEGIES**
6 **COMPARE TO THE CURRENT MARKET?**

7 A. The BHC Compensation Department reviews the pay structure annually to see
8 how the structure and pay practices reflect the market. As of November 1, 2012,
9 the average base pay for non-union employees of Black Hills Power was 96% of
10 the market median, indicating Black Hills Power employees' base pay rates were
11 somewhat lower than the market median.

12 **Q. DOES BHC HAVE A VARIABLE COMPENSATION COMPONENT OF**
13 **ITS TOTAL COMPENSATION PHILOSOPHY?**

14 A. Yes. The Black Hills Corporation Annual Incentive Plan (the "AIP" or the "Plan")
15 is designed to motivate and reward employees for achieving and exceeding goals
16 that benefit our customers and our shareholders. The AIP is designed to reward
17 eligible employees, including both non-union and union employees of Black Hills
18 Power, who contribute to the success of the Black Hills Corporation and/or their
19 assigned Business Unit; reward employees who contribute to the quality of service
20 provided to customers including, but not limited to, the provision of safe, reliable
21 and affordable service; motivate work performance and behavior that supports the
22 Corporation's financial and non-financial goals and increase the employee's

1 understanding of the Corporation's business objectives and performance.

2 **IV. COMPANY ANNUAL INCENTIVE PLAN**

3 **Q. PLEASE DESCRIBE BHC'S ANNUAL INCENTIVE PLAN.**

4 A. The purpose of BHC's Annual Incentive Plan is to promote BHC's pay for
5 performance philosophy, to provide competitive incentive opportunities that are
6 consistent with other companies in the industry, and to focus employees on
7 important performance objectives. BHC's Annual Incentive Plan helps to ensure
8 its total pay position is competitive with market practices for BHC employees, that
9 its total compensation expense varies with BHC's performance on measures
10 important to the customers, and provides a tool to align employees' interests with
11 customer and community interests.

12 **Q. WHAT PERFORMANCE GOALS ARE MEASURED UNDER THE AIP?**

13 A. An eligible employee can earn an incentive award based on that employee's
14 performance toward goals designed to achieve business unit operational
15 performance targets. The components of the incentive award for plan year 2011
16 were as follows:

- 17 • An employee could qualify for up to 50% of the maximum possible award
18 for goals tied to customer satisfaction, cost control, safety, reliability,
19 operations efficiency, and other business unit operational measures;
- 20 • An employee could qualify for up to 25% of the maximum possible award
21 for the achievement of business unit financial performance; and
- 22 • An employee could qualify for up to 25% of the maximum possible award

1 if BHC realizes established earnings per share (“EPS”) targets.

2 Each goal is measured independently and goal performance that meets or exceeds
3 the threshold level will be used to calculate the incentive award. Achievement of
4 financial results is not a condition to award incentive for achievement of other
5 goals. An employee can earn from 0% to 150% of the target percentage incentive
6 based on achievement against each of the AIP goals. Performance below
7 threshold results in a zero payout for the associated goal. Achievement of a goal’s
8 “target” performance results in a payout of 100% of the payment relative to that
9 goal. There is also a Maximum payout, which means that if performance exceeds
10 target, no more than 150% of the target payment will be made relative to that goal.

11 **Q. HOW DOES THE AIP PROVIDE VALUE TO CUSTOMERS?**

12 A. The AIP provides direct and indirect value to customers in a number of different
13 ways. For example, AIP goals are aligned with BHC’s high-level objectives and
14 strategic framework. Business unit goals are primarily designed to improve the
15 performance of utility operations by focusing on improvements to safety,
16 reliability, and customer satisfaction. Examples of Black Hills Power’s business
17 unit goals include:

- 18 • Continuous improvement in results from customer satisfaction surveys.
19 These results are measured each quarter.
- 20 • Service reliability metrics.
- 21 • Increase in number of completed service orders per day.
- 22 • Reduction in labor cost per service order.

- 1 • Reductions in O&M expense resulting from Continuous (Process)
2 Improvement projects.
- 3 • Reduction in number of lost time accidents, preventable vehicle accidents,
4 and OSHA recordable accidents.

5 However, it is important to understand that with actual base salaries for Black
6 Hills Power’s employees falling somewhat below the market median levels, total
7 compensation would be significantly less competitive without the incentive plan
8 component. An employee’s total cash (base salary *plus* AIP incentive award)
9 earnings potential depends on both competitive base salary and on a competitive
10 AIP incentive compensation opportunity awarded for the achievement of key
11 operating and strategic goals.

12 **Q. HOW WOULD AVERAGE BASE SALARIES BE AFFECTED IF AIP**
13 **INCENTIVES WERE ELIMINATED?**

14 A. If BHC did not offer employees the opportunity to earn AIP incentive
15 compensation, BHC would need to make-up the difference by increasing base
16 salaries in at least an equivalent amount, which would result in higher fixed costs
17 for salaries and benefits. An alternative to variable compensation would be for
18 BHC to raise all employees base pay to reflect the median variable compensation
19 earnings provided by other utilities. While this would provide a competitive total
20 compensation rate that is “fixed and measurable”, it would de-link those costs with
21 customer performance measures and increase overall costs as many of our benefits
22 are also tied to base pay rates.

1 **Q. PLEASE FURTHER EXPLAIN HOW CUSTOMERS BENEFIT FROM A**
2 **TOTAL COMPENSATION PACKAGE THAT INCLUDES THE AIP.**

3 A. Attracting and retaining a highly skilled and experienced workforce enables BHC
4 to continue to provide service that is efficient, effective, safe and reliable and
5 helps avoid high costs associated with employee turnover. AIP business unit goals
6 support the strategic objectives of BHC, which include achieving high levels of
7 customer satisfaction, improving operations and safety, and delivering excellent
8 service.

9 **Q. ARE THERE OTHER ASPECTS OF BHC'S COMPENSATION**
10 **STRUCTURE THAT DRIVE CUSTOMER BENEFITS?**

11 A. Yes. The AIP also provides direct and indirect benefits to customers in that BHC
12 has a common pay structure for all of its business units. This means that BHC can
13 more easily relocate employees among company business units, reduce the cost of
14 maintaining numerous payroll systems, reduce the cost of training employees on
15 benefits, and better manage the cost of administering compensation plans than
16 would be possible with multiple compensation schemes.

17 **Q. WHO IS ELIGIBLE TO PARTICIPATE IN THE AIP?**

18 A. With very limited exception, all regular full-time and part-time employees, both
19 union and non-union, who are hired and working by October 1 of the Plan Year
20 are eligible to participate in the Plan for that plan year. Part-time employees who
21 work a minimum of 20 hours per week are eligible for a pro-rata award based on
22 their actual wages for hours worked. Pro-rata awards for the number of months

1 actively employed at each eligibility level during the Plan Year will also be paid to
2 Participants who are newly hired on or by October 1 of the Plan Year; who are
3 promoted, transferred or demoted during the Plan Year; who are on leave of
4 absence for any full months during the Plan Year; who are on military leave for
5 any months during the Plan Year; who leave the Company due to Disability during
6 the Plan Year; who leave the Company due to Retirement during the Plan Year;
7 who are laid off under a severance agreement with the Company during the Plan
8 Year; and who die during the Plan Year.

9 **Q. PLEASE PROVIDE ADDITIONAL DETAIL REGARDING THE**
10 **METHODOLOGY FOR DETERMINING AIP COMPENSATION.**

11 A. A set of goals with “threshold,” “target,” and “maximum” performance metrics are
12 established at the beginning of each calendar year for each identified business unit.
13 The Company establishes its incentive targets to achieve the market median
14 incentive opportunity of similar companies. The “Threshold” is the minimum
15 performance level that must be met for the year – if the Threshold is not met, no
16 incentive payment is made relative to that goal. Target performance for each goal
17 is set at a level of an “expected” result, with sufficient stretch, necessary for a
18 successful year. The goal is to provide Black Hills Power employees with a total
19 compensation package that is competitive with other companies when Black Hills
20 Power achieves target performance levels on annual incentive goals. Operational
21 (non-financial) goals can be based on Reliability of Service, Safety, Customer
22 Satisfaction, Effective Use of Capital, expense management (reductions in

1 controllable O&M), and Continuous (Process) Improvement. The “Reliability”
2 goal consists of the “System Average Interruption Duration Index (SAIDI)”
3 measure, which is commonly used as a reliability indicator by electric utilities, and
4 which measures the average outage duration for each customer served. The
5 “Safety” measures include chargeable vehicle incidents and lost time injury
6 incidents, both of which have implications for cost and service to customers. The
7 “Customer Satisfaction” measure includes 5 customer service quality metrics
8 including customer service call time and emergency service call times.
9 “Continuous (Process) Improvement” goals reflect initiatives to reduce on-going
10 cost of service and focuses employees on identifying additional opportunities to
11 increase process efficiency and effectiveness for our customers. By having a
12 portion of the incentive program tied to the business unit, employees and
13 management are held accountable for seeing that the overall operation of the
14 delivery of services occurs in the most efficient manner possible. The business
15 unit component of the AIP ensures that management and employees understand
16 that strong performance for the customer unrelated to financial results will be
17 recognized and rewarded.

18 **Q. PLEASE EXPLAIN WHY TYING THE AIP GOALS TO EARNINGS PER**
19 **SHARE AND OPERATING INCOME BENEFITS CUSTOMERS.**

20 A. Earnings Per Share (EPS) and Operating Income are easily recognized
21 benchmarks for successful and productive companies that are meeting their
22 customers’ needs. They provide company-wide objective measures of

1 performance, and cannot reasonably be separated from customer interest. The
2 customers benefit directly when they are being serviced by a financially secure
3 company which is able to meet their needs efficiently and economically. A
4 company cannot be successful and financially secure if the company does not
5 attract and retain qualified and motivated employees who strive to meet customer
6 expectations and requirements. One of the most readily measurable standards of
7 long-term financial viability is EPS.

8 Company financial health and customer interests go hand in hand. Customers
9 benefit because the overall financial health of the company affects its perceived
10 financial welfare, general economic welfare, and thus ultimately it's financing
11 rates. Employees have a direct impact on EPS and Operating Income through
12 goals and performance relating to cost control efforts, efficiencies gained through
13 business process improvement projects and other work which also results in
14 benefits to customers.

15 Also, it is important to remember, as noted above, the overall payment of
16 compensation and benefits to employees is competitive with market rates for those
17 employees.

18 **V. INDUSTRY COMPENSATION COMPARISONS**

19 **Q. DO OTHER COMPANIES IN THE UTILITY INDUSTRY USE A**
20 **COMPARABLE VARIABLE COMPENSATION MECHANISM?**

21 **A.** Yes. Other utilities do provide incentive or variable compensation as part of their
22 compensation packages, as do companies in other industries. Without a similar

1 plan, BHC's total compensation package may not be competitive with other
2 utilities.

3 **Q. ARE YOU AWARE OF ANY STUDIES THAT SUPPORT THIS**
4 **CONCLUSION?**

5 A. Yes. Aon Hewitt Associates, an international business consulting firm that
6 specializes in compensation issues, conducted a survey of broad-based variable
7 pay plans in September 2011 titled "Salary and Variable Compensation
8 Measurement Special Report – U.S. Edition," which includes 70 energy / utility
9 companies. Results from the survey indicate the following:

- 10 • 92% of participating companies offered at least one broad-based variable
11 compensation plan covering 98% of total U.S. employees, an increase from
12 89% in 2007 and from 80% in 2002 as companies continue to turn to
13 variable pay as a means to attract, retain and award performance. All 70
14 energy / utility companies offer at least one broad-based incentive plan and
15 all cover 100% of their employees.
- 16 • 87% of the participating companies in the survey have an annual incentive
17 program with a plan design similar to BHC's AIP, where awards are based
18 on the combined achievement of Company financial and business unit
19 operating performance.
- 20 • 91% of the participating companies reported the benefits realized from their
21 variable pay plan and the improved business results outweighed the cost.
- 22 • Notable outcomes reported by companies with a variable pay plan similar

1 to the AIP include reduced costs, increased productivity, increased quality,
2 increased customer satisfaction, and increased employee morale.

3 Other surveys published in 2011 include:

- 4 • Mercer: 91% of employers provide short-term incentive or variable pay
5 plans, an increase from 78% in 2004.
- 6 • World at Work: 90% of employers provide short-term incentive or variable
7 pay plans, an increase from 77% in 2004. Of those providing a short-term
8 incentive plan, 98% of hourly employees (average payout was 5%) and
9 100% of salaried employees (average payout was 12%) are eligible under
10 the plan.
- 11 • Pearl Meyer & Partners: 90% of utilities in the survey provide a short-term
12 incentive plan to all employees.

13 **Q. HOW DOES BHC MAKE IMPROVEMENTS TO ITS AIP?**

14 A. Through its annual planning process, BHC routinely evaluates the effectiveness of
15 the plan in meeting its goals. BHC also continuously evaluates the AIP design to
16 ensure that it remains competitive and comparable to other utilities.

17 **VI. COMPANY RECOVERY OF EMPLOYEE**

18 **COMPENSATION EXPENSES**

19 **Q. SHOULD THE COMPENSATION MERIT INCREASE BE APPROVED?**

20 A. Yes. Recovering the actual amount of employee compensation expense is
21 necessary to attract and retain the high quality of employees that are needed to
22 serve the customers of Black Hills Power. Any review should focus on whether

1 compensation increases for employees are within a reasonable range. Under
2 existing economic conditions, independent surveys reflected that more than 96%
3 of US-based companies will award merit pay increases during 2012, with an
4 average budget of 3% to 3.4%. Non-union employee pay changes are effective
5 each March, with the most recent increase effective March 5, 2012. Increases in
6 employee compensation are known and measurable, and these increases in
7 employee compensation are supported by extensive reviews of competitive market
8 data.

9 Without merit increases, BHC would lag the median pay for these positions,
10 significantly increasing retention and performance risk, and the company will
11 incur higher costs for turnover and related issues. A summary of independent
12 surveys regarding merit pay follows:

- 13 • Mercer: The “Mercer September 2011 Compensation Planning Survey”
14 reflects that 97% of employers plan to provide merit increases to employees
15 in 2012, with an average budgeted increase at 3.0%. The utility companies
16 in the survey also reflect a budgeted increase of 3.0%.
- 17 • Aon Hewitt: The 2012 survey reflects that 98% of employers plan 2012
18 merit increases, with an average budget of 3.0%. The utilities in the survey
19 reflect a merit budget average of 3.3%. The average budget reported for
20 2011 was 3.0%.
- 21 • Towers Watson: The 2012 survey reflects that 97% of employers plan
22 2012 merit increases, with an average budget of 3.0%. This survey does

1 not reflect utility specific information. The average budget for 2011 was
2 3.0%, with 95% of employers making merit increases.

- 3 • World at Work: The 2012 survey of 5,818 employers reflects a 3.0% merit
4 increase budget average for 2012. The average merit increase reported for
5 2011 was 3.0%.

6 For those non-union employees of Black Hills Power, the merit budget was 3.0%
7 for 2011.

8 Simply put, the merit increases will be incurred, and the overall compensation to
9 Black Hills Power employees is fair and competitive as tested against prevailing
10 market comparisons.

11 **Q. SHOULD THE COMPENSATION INCREASE BE APPROVED FOR**
12 **UNION EMPLOYEES?**

- 13 A. Recovering the actual amount of employee compensation expense is necessary –
14 as described above -- to attract and retain the high quality of employees that are
15 needed to serve the customers of Black Hills Power.

16 The ratified contract between Black Hills Power and the IBEW Local 1250 Local
17 Bargaining Unit requires an increase in union employee compensation of 3.0%
18 effective April 1, 2011; an increase of 3.0% to 4.0% depending on job
19 classification effective April 1, 2012; an increase of 3.0% to 3.5% depending on
20 job classification effective April 1, 2013; and an increase of 3.25% effective April
21 1, 2014. Accordingly, the April 1, 2013 rate increase of 3.0% to 3.5% for union
22 employees is representative of the amount that Black Hills Power will be obligated

1 to pay while its rates will be in effect. Black Hills Power's union employee
2 compensation adjustment qualifies as a known and measurable change over the
3 four-year contract.

4 **VII. COMPANY BENEFITS AND PERIODIC REVIEW**

5 **Q. PLEASE DESCRIBE THE BENEFIT PLANS THAT BHC PROVIDES TO**
6 **ITS BLACK HILLS POWER EMPLOYEES?**

7 A. BHC offers a combination of company-provided and voluntary benefits.
8 Employees are enrolled in certain company-provided benefits automatically and
9 BHC pays the costs (for example, short-term and long-term disability benefits).
10 Employees choose whether or not to participate in the voluntary benefits and they
11 pay a portion or all of the costs. These company-provided and voluntary benefit
12 programs consist of: (1) medical, dental and vision plans, (2) flexible spending
13 accounts, (3) life insurance and accidental death and dismemberment insurance,
14 (4) paid time off, (5) retirement, and (6) other benefits including educational
15 assistance, holidays and other time away from work, business travel accident
16 insurance, rewards & recognition and wellness programs.

17 **Q. WHAT BENCHMARKING HAS BEEN CONDUCTED TO EVALUATE**
18 **COST/PERFORMANCE LEVELS?**

19 A. BHC solicits a number of independent reviews from external organizations and
20 consulting firms such as Towers Watson, Aon Hewitt, Mercer, etc. These reviews
21 cover a wide range of compensation and benefit program designs and costs
22 including compensation and benefit programs, HR function administrative

1 expenses, and market data for positions. BHC compares its benefit programs and
2 costs with companies from the utility sector and from general industry to ensure
3 the company can attract and retain employees with the necessary skills. BHC
4 utilizes multiple nationally recognized third-party surveys and also conducts
5 customized surveys where appropriate and necessary. These benchmarking
6 surveys allow BHC to evaluate the competitiveness and efficiencies of its benefit
7 programs and costs compared to other companies in the market. If a program does
8 not meet performance, cost or efficiency expectations, it is reviewed to determine
9 the root cause and the options or alternatives available. BHC closely monitors
10 market practices and benchmark data for costs to maintain competitive and cost
11 effective programs.

12 **Q. WHAT TYPE OF OVERSIGHT IS IN PLACE TO ENSURE THAT BHC'S**
13 **COMPENSATION AND BENEFIT PROGRAMS ARE THOSE THAT ARE**
14 **MOST BENEFICIAL FOR THE SUPPORT OF THE OPERATING**
15 **COMPANIES' UTILITY SERVICE?**

16 A. The Human Resources Department, in partnership with the business unit leaders
17 and company management, develop annual budgets and long-range plans (5
18 years), including compensation, benefit and other programs supporting the
19 business' goals and objectives. HR and key operating personnel manage these
20 budgets and review all programs for effectiveness, cost and any proposed
21 modifications. All costs are modeled to determine impacts to cost and are
22 benchmarked against the market parameters to ensure competitiveness and cost

1 effectiveness.

2 Not only is the employee compensation and benefit expense reasonable, the
3 adjustments contained on Black Hills Power Schedules H-1, H-4, H-5 and H-6 are
4 also reasonable.

5 **Q. ARE YOU AWARE OF OTHER STATE COMMISSIONS THAT HAVE**
6 **APPROVED THE EMPLOYEE COMPENSATION AND BENEFIT**
7 **STRUCTURE PROPOSED IN THIS PROCEEDING?**

8 A. Yes. Through rate case settlements and contested proceedings, commissions in
9 Nebraska, Iowa, South Dakota, Wyoming and Colorado (in the gas and electric
10 rate cases) have approved this employee compensation and benefit structure.
11 Black Hills Corporation places emphasis on maintaining a common employee
12 compensation structure and program. The same is true for its proposal related to
13 its employees living in or supporting our Black Hills Power customers.

14 **VIII. INDUSTRY WORKFORCE COMPARISONS**

15 **Q. ARE OTHER COMPANIES IN THE UTILITY INDUSTRY FACING THE**
16 **SAME WORKFORCE CHALLENGES?**

17 A. Yes. Other utilities are likely facing the same challenges as far as aging workforce
18 and scarcity of talent. BHC is implementing this strategic workforce planning
19 process in order to proactively address these challenges allowing us to stay
20 competitive in the talent market. A significant portion of the workforce could
21 retire over the next 5-7 years given 27% of BHC's utility subsidiary workforce,
22 including Black Hills Power, is age 55 or older. Approximately 47% of Black

1 Hills Power's workforce is age 50 or older as of November 1, 2012. As of 2008,
2 53% of the utilities workforce nationwide was age 45 or older. With over 50% of
3 the workforce eligible to retire within the next decade, many utilities will be
4 competing for the same qualified candidate pool to replace retiring workers. Black
5 Hills Corporation and Black Hills Power are taking actions to improve current
6 employee retention as well as offer attractive training and development
7 opportunities to new employees. As technology continues to progress and change
8 the landscape of the utility workforce skills and duties, investment in skills and
9 experience will be just as important to providing safe, reliable service as any piece
10 of equipment or infrastructure.

11 **IX. STRATEGIC PHILOSOPHY AND PROGRAMS**

12 **Q PLEASE DESCRIBE THE IMPORTANCE OF WORKFORCE PLANNING**
13 **FOR THE UTILITY INDUSTRY AND ITS APPLICATION TO BLACK**
14 **HILLS POWER?**

15 A. As noted by Richard Loomis, on behalf of Black Hills Power, the BHC strategic
16 workforce planning team reviews and will continue to monitor, numerous studies
17 that have been published concerning the aging of the national workforce necessary
18 to serve and operate the nation's utility systems. As Mr. Loomis testifies, Black
19 Hills Power must prepare to address its own workforce issues. My role will be to
20 monitor compensation and benefit packages to ensure that we manage through this
21 matter prudently.

22

1 **Q. WILL THE COMPANY PLACE STRATEGIC WORKFORCE**
2 **POSITIONS ON COMPENSATION PLANS THAT DIFFER FROM**
3 **EXISTING EMPLOYEES?**

4 A. No, the new employees would be provided the same compensation and benefits as
5 other Black Hills Power and BHC employees.

6 **X. SUMMARY OF TESTIMONY**

7 **Q. PLEASE SUMMARIZE YOUR TESTIMONY AND CONCLUSIONS?**

8 A. I describe the general compensation program for BHC employees, and
9 particularly the employees of the applicant, Black Hills Power, including the
10 variable compensation program, and explain why those programs and their
11 associated costs are reasonable and necessary to attract, motivate and retain well
12 qualified and competent employees to support utility operations, to support
13 recovery of the compensation-related expenses of Company employees.

14 My testimony specifically supports the employee compensation related
15 adjustments contained on Schedules H-1, H-4, H-5 and H-6 of the Black Hills
16 Power revenue requirement model.

17 My recommendation is for the Commission to approve the recovery of legitimate
18 employee expenses. Those expenses are necessary to pay the employees – both
19 direct and allocated -- who provide utility service to Black Hills Power customers.

20 My testimony also supports the inclusion of the Workforce Planning employee
21 costs as they are a valid and appropriate component of utility management and
22 operations.

1 Q. **DOES THIS CONCLUDE YOUR TESTIMONY?**

2 A. Yes, it does.