

THE STATE OF NEW HAMPSHIRE
BEFORE THE
PUBLIC UTILITIES COMMISSION

DG 11-069

NORTHERN UTILITIES, INC.

DIRECT TESTIMONY OF
ELIZABETH M. SHAW

EXHIBIT EMS-1

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1 **I. INTRODUCTION**

2 **Q. Please state your name and business address.**

3 A. My name is Elizabeth M. Shaw. My business address is 6 Liberty Lane West,
4 Hampton, NH 03842.

5 **Q. What is your position and what are your responsibilities?**

6 A. I am the Manager of Benefits and Payroll for Unitil Service Corp., “(Unitil
7 Service”), which provides centralized management and administrative services to
8 each of Unitil Corporation’s affiliates (the “Unitil Companies”). My primary
9 responsibilities are managing the benefits and payroll functions.

10 **Q. Please describe your business and educational background.**

11 A. I have approximately 30 years of professional experience in the natural gas utility
12 industry. From 1977 through 1987, I worked primarily as a Rates Analyst for
13 Algonquin Gas Transmission Company which currently is a subsidiary of Spectra
14 Energy. From 1987 through 1996, I held various positions at Bay State Gas
15 Company in their Rates Department. I primarily worked on FERC-related filings
16 for Bay State Gas’s subsidiary, Granite State Gas Transmission, Inc. and on Cost
17 of Gas Adjustment (“CGA”) filings for Northern Utilities. From December 1996
18 through September 2004, I worked for Portland Natural Gas Transmission System
19 (“PNGTS”) as the Director of Administration. I was responsible for all areas of
20 Administration and Human Recourses, including benefits and payroll. I began
21 working for Unitil Service Corp. in March 2005 as a Senior Human Resources

1 Analyst and currently hold the position of Manager, Benefits and Payroll. I hold a
2 Master's Degree in Business Administration from Bentley College and a Bachelor
3 of Arts degree in Management from Boston College.

4 **Q. Have you previously testified before this Commission or other regulatory**
5 **agencies?**

6 A. Yes. While working at Bay State Gas Company I testified before the Federal
7 Energy Regulatory Commission ("FERC"), the New Hampshire Public Utilities
8 Commission and have sponsored pre-filed direct testimony in cost of gas
9 adjustment filings made with the Maine Public Utilities Commission. While
10 working at PNGTS, I sponsored pre-filed direct testimony in that company's
11 FERC rate case filing, in Docket No. RP02-13. I also recently testified before
12 the Massachusetts Department of Public Utilities Docket No. DPU 11-01.

13 **II. SUMMARY OF TESTIMONY**

14 **Q. What is the purpose of your testimony?**

15 A. The purpose of my testimony is to: (a) provide an overview of Northern Utilities'
16 compensation and benefit programs; and (b) to sponsor the pro forma adjustments
17 made to the following items of O&M Expense.

- 18 • Payroll and Related Taxes
19 • Medical and Dental Insurances

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2 **III. COMPENSATION PROGRAM**

3 **Q. Please explain the Unitil Companies' salary policy.**

4 A. The Unitil Companies' stated policy is to compensate employees at the median of
5 the marketplace for base pay and total cash compensation.

6 **Q. Did Northern Utilities perform a compensation study to justify the level of its
7 salaries and wages?**

8 A. Unitil Service performed a compensation study on behalf of Northern Utilities
9 and the Unitil Companies. The compensation study was developed with the
10 assistance of Towers Watson (formerly Towers Perrin), an internationally
11 recognized consulting firm in the area of employment compensation. The study
12 of the Unitil Companies' salaries and benefits was undertaken for the express
13 purpose of comparing them to external markets. Towers Watson assisted in
14 reviewing competitiveness of base salaries and salary ranges, reviewing and
15 recommending an appropriate and competitive cash incentive plan,
16 recommending changes to the executive plans, and evaluating and recommending
17 changes to all of the non-cash employee benefits plans.

18 **Q. On what sources did Towers Watson rely for its market compensation data?**

19 A. Towers Watson used published surveys from their own database as well as from
20 the Hay Group, Mercer, and Wyatt. Specific survey sources included: the
21 Towers Perrin Energy Services Executive Compensation Database, the Towers

1 Perrin Energy Services Middle Management and Professional Compensation
2 Database, the Hay Group Energy Services Compensation Report, the Wyatt Top
3 Management Compensation Survey, the Wyatt Middle Management
4 Compensation Survey, the Wyatt Supervisory Management Compensation
5 Survey, the Wyatt Professional Administration Personnel Survey, the Wyatt
6 Office Personnel Survey, the Mercer US Total Compensation Survey of the
7 Energy Sector, the Mercer US Executive Benchmark Database, the Mercer
8 Information Technology Compensation Survey, the Mercer Finance, Accounting
9 and Legal Compensation Survey, the Towers Perrin General Industry Executive
10 Compensation Database, and the Towers Perrin General Industry Middle
11 Management & Professional Compensation Database. In addition, Towers
12 Watson conducted a search of other utility proxy statements on file with the
13 Securities and Exchange Commission, to double-check the competitiveness of
14 certain positions.

15 **Q. Did Towers Watson recommend that the Unutil Companies adopt a**
16 **competitive position for its compensation and benefits policy?**

17 A. Yes. Towers Watson recommended that the Unutil Companies continue its policy
18 of paying at the median for base pay, total cash compensation, and total
19 compensation when compared to their database of utility companies. They also
20 concluded that median pay levels in New England are roughly equal to median
21 pay levels nationwide.

1 **Q. What was Towers Watson's conclusion about the competitiveness of the**
2 **Unitil Companies' pay structure?**

3 A. Towers Watson concluded that Unitil's pay structure was very close to the market
4 median for most job grades and for most positions. Some positions and some pay
5 grades are below market median, and Towers Watson made specific
6 recommendations for changes to these pay levels.

7 **Q. What actions have Northern Utilities and Unitil Service taken to implement**
8 **the recommendations of Towers Watson?**

9 A. Due to the recession, the Company postponed implementing any of the Towers
10 Watson recommendations in 2010; however, the Company began to implement
11 the recommendations in 2011. The Company has adjusted the pay range for
12 positions that were below the market median. Further, the Company has adjusted
13 the long term incentive compensation plan to position itself closer to the market.
14 The Company has also implemented changes in its benefits programs to increase
15 the amount that employees pay for their benefits, consistent with Towers
16 Watson's recommendations.

17 **Q. How are wages determined for union employees?**

18 A. Union wage rates are established periodically through the collective bargaining
19 process. Typically Unitil obtains contracts from our neighboring utilities in New
20 England and calculates competitive wage rates for each union position. This helps
21 set fair and equitable wage rate goals in the collective bargaining process to
22 ensure that our union salaries attract and retain qualified union employees. In

1 2009, Unitil Service performed a survey of hourly wage rates for the Unitil
2 companies compared to these other utilities. Northern Utilities' union wages
3 approximate the median in the market when compared to these contracts.

4 **IV. BACKGROUND OF PENSION AND PBOP PLANS**

5 **Q. Please describe the current Pension and PBOP plans sponsored by the Unitil**
6 **Companies.**

7 A. The Unitil Companies sponsor the Unitil Corporation Retirement Plan ("Pension
8 Plan") which provides monthly retirement income to employees who qualify for a
9 retirement benefit. The Pension Plan retirement benefits are based upon an
10 employee's level of compensation and length of service. The Pension Plan
11 currently covers approximately 834 people, including 259 people who are
12 currently receiving benefits. The Pension Plan maintains an investment trust fund
13 for the management of the Plan's assets and the funding of current and future
14 retiree pension benefits.

15 The Unitil Companies also sponsor a Plan for Postretirement Benefits Other than
16 Pension ("PBOP Plan"), which provides a variety of health and welfare benefits
17 to approximately 443 employees and 314 retirees and their beneficiaries. For
18 postretirement benefits, the PBOP Plan provides health insurance benefits for
19 retirees and their spouses under age 65 under a Consumer Directed Health Plan
20 (CDHP), a Preferred Provider Organization plan (PPO), or an Exclusive Provider
21 Organization (EPO); a Medicare Supplement insurance plan for retirees and

1 spouses over age 65, partial reimbursement of Medicare premiums, and a modest
2 paid-up life insurance benefit for retirees. Widows and widowers of deceased
3 retirees are also covered by the health insurance benefits. The PBOP Plan
4 currently maintains two Voluntary Employee Trusts and a 401(h) Account within
5 the Pension Plan to fund covered benefits.

6 With a few exceptions the Pension and PBOP Plans of the Util
7 Companies cover union and non-union employees equally and the provisions of
8 the plans and the benefits provided under the plans apply to management and non-
9 management in the same way.

10 Effective January 1, 2010, for all non-union employees and for union
11 employees of Northern Utilities in the –Company’s Maine Division, and effective
12 January 1, 2011, for union employees in the Northern Utilities’ New Hampshire
13 Division, the following changes were made to the Postretirement Benefits other
14 than Pension: Employees in these groups who retire subsequent to the effective
15 date of these changes will now pay 20% of the cost of their retiree medical
16 benefits. The new Company contribution level includes both the medical benefits
17 before age 65 and the Medicare supplement benefits after age 65. In addition,
18 future retirees will not receive the partial reimbursement toward their Medicare
19 premiums. Further, employees hired subsequent to the effective date of these
20 changes will only be provided with company subsidized medical insurance until
21 they reach age 65, but will not be eligible to receive a Medicare supplement plan
22 after age 65.

1 **Q. How long has the Pension Plan been in place?**

2 A. The current Pension Plan is a consolidated retirement plan that resulted from the
3 merger of the Exeter & Hampton Electric Company Pension Plan, the Concord
4 Electric Company Pension Plan, the Fitchburg Gas and Electric Light Company
5 (“FG&E”) Pension Plan, the FG&E - Brotherhood of Utility Workers of New
6 England, Inc. Local No. 340 Pension Plan, and the Unitil Corporation Retirement
7 Plan as adopted by Unitil Service. The final merger of all these various
8 retirement plans occurred in 1998. The Plan was amended again in 2009
9 following the acquisition of Northern Utilities, Inc. and Granite State Gas
10 Transmission, Inc.

11 The Pension Plan currently offers a defined pension benefit to all eligible
12 employees of the Unitil Companies, including the employees of Northern
13 Utilities. Certain predecessor plan benefits are grandfathered in accordance with
14 IRS regulations.

15 Effective January 1, 2010, the Retirement Plan is not available to non-
16 union new hires, and effective January 1, 2011 for all Northern Utilities – New
17 Hampshire Division union new hires. Although these new hires are not eligible
18 for any benefits from the defined benefit pension plan, they will instead receive
19 all of their pension benefits from an Enhanced 401(k) plan.

20 Current employees affected by this change had a choice of continuing to
21 participate in the Pension Plan with no change to their benefit or to receive a

1 frozen benefit from the defined benefit plan and to receive all future benefit
2 accruals from the Enhanced 401(k).

3 **Q. How long has the PBOP Plan been in place?**

4 A. The Unitil Companies have provided post-retirement health and welfare benefits
5 dating back to 1970 and earlier. More recently, from January 1993 to December
6 2003, these benefits were primarily provided by the Unitil Retiree Trust. The
7 Unitil Retiree Trust was formed as a special purpose entity in 1993 and assumed
8 the liability for the majority of retiree medical benefits. The Unitil Retiree Trust
9 was dissolved at the end of 2003, when Unitil adopted Financial Interpretation
10 Number 46 ("FIN 46"). As a result, the Unitil companies have now directly
11 assumed the liability for these benefits. The plan was amended in January 2010
12 and again in January 2011 to expand coverage to Northern Utilities union
13 employees, who previously were not eligible for any retiree medical benefits or
14 were provided a small subsidy toward the cost of these benefits.

15 **Q. Who oversees the investment of the Pension and PBOP trust funds?**

16 A. Oversight and monitoring of the investments of the trust funds is ultimately the
17 responsibility of the Unitil Corporation Retirement Plan Committee (the
18 "Committee"), which is appointed annually by the Unitil Corporation Board of
19 Directors, in conformance with the Employee Retirement Income Security Act
20 ("ERISA"). This Committee currently consists of four members: two outside
21 Board members, and two officers of Unitil Service, the Chief Financial Officer,
22 and the Vice President, Administration. The Committee relies on the advice of

1 investment managers to determine appropriate and prudent investment strategies
2 in compliance with the regulatory and prudence guidelines of ERISA. The
3 Committee also relies on the advice of its actuaries, attorneys, accountants and
4 other consultants to develop the key assumptions used by Unifil Corporation's
5 actuaries to value the Plan's assets and liabilities and determine the annual
6 pension expense, cash funding and other accounting information as required by
7 the rules and regulations of the Securities and Exchange Commission,
8 Department of Labor, Internal Revenue Service and other governing regulatory
9 agencies.

10 **V. PAYROLL AND RELATED TAXES**

11 **Q. As presented in the pro forma adjustment of O&M expenses, what does**
12 **payroll consist of?**

13 A. Payroll consists of base pay, incentive pay, overtime pay, standby pay, and
14 callout pay. Payroll does not include payments to employees for Northern
15 Utilities' wellness benefit, medical opt-out payouts and service awards.

16 **Q. Why did you exclude those elements from the adjustment to payroll?**

17 A. Although those elements of payroll are processed through payroll because they
18 are subject to withholding taxes, they are not, however, subject to the annual pay
19 rate increases, and thus are excluded from the payroll adjustment.

1 **Q. What adjustment was made to payroll?**

2 A. The payroll adjustment, as reflected on Schedule RevReq 3-4, Page 1 adjusts the
3 test year payroll charged to O&M Expense for the following:

- 4 1. Annualization of the pay rate increases for the union employees that
5 occurred during calendar year 2010; and
- 6 2. The effect of pay rate increases that occurred on January 1, 2011 for
7 nonunion employees and that will occur on June 6, 2011 for union
8 employees.

9 I have made these adjustments to the payroll for both Northern Utilities and Unitil
10 Service.

11 **Q. Please describe the adjustment to Northern Utilities' payroll.**

12 A. The first step was to annualize the effect of the 2010 pay rate increases that
13 occurred during the test year. On June 6, 2010, the union employees received an
14 average 3.29 percent pay rate increase, seven months of which are included in the
15 test year. To annualize the effect of the union rate increase, the 3.29 percent
16 increase was applied to the year to date ("YTD") June 5, 2010 union payroll. The
17 associated incremental payroll cost was added to the test period union payroll
18 costs.

19 The next step is to pro form the test year payroll to reflect the pay rate
20 increases to be experienced within the rate year. On January 1, 2011, non-union
21 employees received a three percent increase. On June 6, 2011 the union
22 employees will receive an average increase of 4.56 percent pursuant to their

1 contract. To pro form for the effect of these increases, the annualized 2010
2 payroll costs for each employee group were multiplied by their respective 2011
3 percentage increases. The incremental payroll cost for 2011 was added to the
4 annualized 2010 costs to determine the total Test Year payroll costs, as pro
5 formed for ratemaking purposes.

6 The pro formed payroll costs were reduced by the amount chargeable to
7 capital of \$1,784,035 to derive the pro formed O&M payroll of \$1,279,185. The
8 test year O&M payroll was then deducted to derive the O&M payroll increase of
9 \$65,481. See Schedule RevReq 3-4, page 1, line 9, column (f).

10 **Q. Please describe the adjustment to the Unutil Service payroll.**

11 A. The adjustment to the Unutil Service payroll was prepared in a similar manner as
12 the adjustment to the Northern Utilities non-union payroll. First, I identified the
13 payroll expense included in the monthly billings for services provided by Unutil
14 Service to Northern Utilities. The next step was to reflect the effect of the 2011
15 increase of 3 percent that occurred on January 1, 2011 for non-union employees.
16 The increase was applied to the twelve month period ended December 31, 2010,
17 and the resulting incremental payroll cost was added to the payroll for the test
18 year to determine the total test year payroll, pro formed for ratemaking purposes.
19 The pro formed payroll costs were reduced by the amount chargeable to capital to
20 derive the pro formed O&M payroll of \$2,176,985. The test year O&M payroll
21 was then deducted to derive the O&M payroll increase of \$65,481 See Schedule
22 RevReq 3-3, page 1, line 9, column (g).

1 **Q. Have you prepared a payroll tax adjustment?**

2 A. Yes, as shown on Schedule RevReq 3-18, an adjustment was prepared to pro
3 form the amount of the Social Security and Medicare taxes related to the payroll
4 adjustments described above.

5 **Q. Please describe how the payroll tax adjustment was calculated.**

6 A. Currently the amount of earnings subject to Social Security taxes is limited to
7 \$106,800. The Medicare tax applies to all earnings without any limit. A review
8 of the test year payroll indicated that one Northern Utilities and 30 Unitil Service
9 employees' earnings exceeded the \$106,800 limit subject to Social Security.
10 Thus, the payroll tax adjustment excludes the effect of the salary increase on the
11 payroll that exceeds the Social Security tax limit. To determine the additional
12 Social Security tax, the payroll was first calculated for those employees who
13 exceed the Social Security maximum after pro forming for the payroll rate
14 increases. Next, the portion of the pro formed payroll rate increase of these
15 employees that exceeded the Social Security maximum was calculated. Finally,
16 the O&M portion of those amounts was calculated and subtracted from the total
17 O&M payroll increase of \$100,199. The resulting amount was multiplied by the
18 Social Security tax rate of 6.2 percent, deriving the additional tax amount of
19 \$6,692. To determine the additional Medicare tax, the total O&M payroll
20 increase of \$100,199 was multiplied by the Medicare tax rate of 1.45 percent, as
21 shown on Schedule RevReq 3-18. The total of additional Social Security and
22 Medicare taxes is \$6,373.

1 **VI. MEDICAL AND DENTAL INSURANCE**

2 **Q. What is the purpose of the Medical and Dental Insurance adjustment?**

3 A. The Medical and Dental Insurance adjustment, as developed on Schedule RevReq
4 3-5, was prepared to pro form for changes in insurance rates and plan changes
5 that to effect during 2011.

6 I have made these adjustments to the Medical and Dental Insurances for
7 both Northern Utilities and Unitil Service.

8 **Q. What steps has Northern Utilities taken to contain the increases in its
9 Medical and Dental Insurance expense?**

10 A. Northern Utilities has taken several steps to contain these costs:

11 • Unitil continually compares the coverage and cost of its insurance
12 programs to market alternatives. This review is conducted for Northern
13 Utilities individually and as part of the Unitil Companies, to ensure that
14 the value for the cost of insurance is maintained, and that costs are
15 contained as much as feasible.

16 • On January 1, 2007, Unitil introduced as an option the Consumer Directed
17 Health Plan (CDHP) for its non-union employees. Consumer-directed
18 health plans have two parts, a high deductible health insurance plan and a
19 health savings account (HSA) funded with pre-tax dollars for out of
20 pocket medical expenses. The deductible is \$1,500 for individual coverage
21 and \$3,000 for two-person or family coverage. The premiums for the

1 CDHP have been significantly lower than the premiums for Unitil's other
2 plans that are offered to employees.

3 • Effective January 1, 2010, the CDHP was the single health plan offering
4 for its non-union employees.

5 • Effective January 1, 2010, the CDHP was offered as an option to the
6 Northern Utilities – Maine Division union employees; and effective
7 January 1, 2011, the CDHP was offered as an option to the Northern
8 Utilities – New Hampshire Division union employees.

9 • Effective January 1, 2011, a coinsurance feature of 10% was added to the
10 CDHP for non-union employees. Coinsurance is the percentage of
11 allowed charges for which the member is responsible after the deductible
12 is satisfied. In addition, the Company increased the stop-loss limit on
13 claims from \$125,000 to \$200,000. Together, these changes resulted in no
14 increase in premiums for 2011.

15 **Q. Please briefly provide some information about the current plans relevant to**
16 **this adjustment.**

17 A. Currently Unitil offers group medical coverage to its employees through Health
18 Plans, Inc. and group dental coverage through Northeast Delta Dental. Prior to
19 March 1, 2011, group medical coverage was provided through Anthem Blue
20 Cross Blue Shield. Non-union employees receive medical coverage through the
21 CDHP while union employees receive medical coverage through an Exclusive
22 Provider Organization (EPO) plan. The working rates used to develop the pro

1 forma costs are based on the rates that went into effect during 2011. The current
2 working rates for Northeast Delta Dental went into effect on January 1, 2011.
3 These rates are developed by underwriters at each insurance company and are
4 based on the Unital Companies' historical claims experience and insurance
5 industry trend analysis.

6 Northern Utilities pays 80 percent of the cost of the working rates and the
7 employees pay 20 percent of the working rate. In addition, Northern Utilities
8 contributes one third of the deductible to the employees' Health Savings
9 Accounts ("HSAs").

10 **Q. Please describe the adjustment to Northern Utilities Medical and Dental**
11 **Insurance.**

12 A. An employee participant count was developed for each plan by employee group,
13 (union and non-union), and by type of coverage, (i.e., individual, two person, or
14 family). This employee participant count excluded employees who choose to
15 opt-out of the medical plan. The 2011 rates were applied to the employee
16 participant count to derive the annual costs related to the plans. Added to these
17 costs were amounts to reflect the average annual costs for each open position,
18 payments to employees who choose to opt out of the medical plan and the
19 company contributions to the employees' HSAs. In addition, the Medical and
20 Dental insurance costs were reduced by 20%, the amount that all employees
21 contribute toward the cost of their coverage. The net Medical and Dental costs

1 were further reduced by the amounts chargeable to capital to determine
2 annualized Medical and Dental Insurance O&M expense for the test year.

3 The total of union and non-union Medical and Dental Insurance O&M
4 expense for 2011 is \$280,572. This amount was compared to the test year
5 Medical and Dental Insurance O&M expense to derive the 2011 adjustment of
6 \$53,749. See Schedule RevReq 3-5, column 3.

7 **Q. Please explain the adjustment for the Medical and Dental Insurance**
8 **included in the Unitil Service charge.**

9 A. The employees of Unitil Service, all non-union, are covered under the same
10 medical and dental plans as the non-union employees of Northern Utilities. The
11 costs are allocated among the client companies of Unitil Service on the basis of
12 labor charged. During the test year, the Northern Utilities' allocation percentage
13 was 34.35 percent. The adjustment was calculated in an identical manner as the
14 non-union Northern Utilities adjustment, except for this allocation process. To
15 pro form the effect of the 2011 working rates, a Unitil Service employee
16 participant count was developed. The employee participant count excluded
17 employees who choose to opt out of the medical plan. The working rates were
18 applied to this employee participant count to derive the annual cost related to the
19 plan. Added to these costs were amounts to reflect the average annual costs for
20 each open position, payments to employees who choose to opt out of the medical
21 plan, and the company's contributions to the employees' HSAs. Subtracted from
22 these costs were amounts that Unitil Service employees contribute toward the

1 cost of their coverage which resulted in the total pro formed 2010 Medical and
2 Dental Insurance cost. The allocation factor of 34.35 percent was applied to this
3 amount and the allocated amount was reduced by the amount chargeable to
4 capital. The resulting O&M expense was then allocated to New Hampshire based
5 on an allocation factor of 50.28%; this result was compared to the test year O&M
6 expense to derive the adjustment of (\$7,005). See Schedule RevReq 3-5, column
7 4.

8 **Q. What is the total Medical and Dental Insurance adjustment that you**
9 **propose?**

10 A. The total Medical and Dental Insurance adjustment is \$46,745. See Schedule
11 RevReq 3-5, column 2.

12 **VII. CONCLUSION**

13 **Q. Does this conclude your testimony?**

14 A. Yes, it does.