

KENTUCKY-AMERICAN WATER COMPANY
CASE NO. 2007-00143
COMMISSION STAFF'S THIRD
SET OF INFORMATION REQUESTS
Item 1 of 54

Witness: Nick Rowe/Michael Miller

1. Refer to Kentucky-American's Response to Commission Staff's Second Set of Information Requests, Item 4(a).
 - a.
 - (1) State whether Kentucky-American has included the total cost of the Production Maintenance Tech – Northern Division position in the calculation of its water rates.
 - (2) If yes, state the amount of this cost that should be removed from water operations and allocated to wastewater operations since the position “is essential to aid in maintaining equipment at . . . [Kentucky-American's] water and wastewater facilities in . . . [its] Northern Division.”
 - b.
 - (1) Kentucky-American states that the vacant Treatment Plant Operator is currently being “covered” by overtime. State whether this overtime is budgeted in the forecasted test-period.
 - (2) If yes, state why it is reasonable to include in forecasted operations overtime to “cover” the vacant position and employee expenses to fill the vacant position.
 - c. Regarding the Administrative Assistant – Cross Connection position, state:
 - (1) The name of the part-time employee filling the clerical needs of this position.
 - (2) The costs of this part-time employee that are included in the forecasted test period.
 - (3) Whether this part-time employee will continue to be employed after the Administrative Assistant – Cross Connection position is filled.
 - d. In its Response to Commission Staff's First Set of Information Requests, Item 1(a), W/P 3, pages 20 through 27 of 118, Kentucky-American listed vacant positions in addition to those set forth in its Response to Commission Staff's Second Set of Information Requests, Item 4(a). Beside the term “vacant” was listed a name.
 - (1) Define the term “vacant” as used in that Response.
 - (2) For each position listed in W/P 3, pages 20 through 27, in which the term “vacant” appears followed by a name,
 - (i) State whether the position is currently unoccupied.
 - (ii) State whether the named employee is currently filling job duties of the position.
 - (iii) If the position is not occupied or filled, provide the information requested in Commission Staff's Second Set of Information Requests, Item 4(a).

Response:

- a. (1) Yes.
 (2) The water plant and water distribution system for the Owenton District is fully automated through a SCADA system, while the wastewater system is not automated. Due to the complexity of the water system and the SCADA system, it is expected that 80% of the position will be charged to water and 20% to wastewater. The following is a recap of the expense applicable to the wastewater system.
- | | |
|---|------------|
| Fully Loaded Labor- (per response to PSCDR2#4d) | \$62,484 |
| Wastewater allocation factor | <u>20%</u> |
| Total | \$12,497 |
- b. (1) No.
 (2) N/A.
- c. (1) The preliminary work is not being filled by a part-time employee, but the work is being performed by Lee Ann Osborne, operations clerk. These duties have been added to her normal work-load on a part-time basis until the vacant position is filled.
 (2) Please see the response to part c. 1.
 (3) Yes.
- d. (1) The term vacant as used in the response to PSCDR2#4a indicates that the position remains vacant and no replacement had been hired at that time.
 (2) (i) The positions listed as vacant preceded with a name indicates that the position is now filled.
 (ii) Yes.
 (iii) N/A.

For electronic version, refer to KAW_R_PSCDR3#1_071607.pdf

KENTUCKY-AMERICAN WATER COMPANY
CASE NO. 2007-00143
COMMISSION STAFF'S THIRD
SET OF INFORMATION REQUESTS
Item 2 of 54

Witness: Nick Rowe/Michael Miller

2. There are expenses included in Kentucky-American's forecasted operations for services provided by "temporary employees."
 - a. State whether any of these temporary employees are performing duties that will eventually be performed by the employees who fill the vacant positions listed in W/P 3, pages 20 through 27 of 118.
 - b. If yes, state the amount of temporary employment expense included in the forecasted test year for each vacant position.

Response:

- a. No. Temporary employees are regularly utilized to fill in for vacations and to meet peak requirements that do not justify a full time employee.
- b. N/A.

For electronic version, refer to KAW_R_PSCDR3#2_071607.pdf

KENTUCKY-AMERICAN WATER COMPANY
CASE NO. 2007-00143
COMMISSION STAFF'S THIRD
SET OF INFORMATION REQUESTS
Item 3 of 54

Witness: Michael Miller

3. a. Provide all studies and analyses that Kentucky-American has performed or commissioned since January 1, 2005 that quantify the benefits that its incentive compensation pay plans provide to its ratepayers.
- b. Provide all studies and analyses that Kentucky-American has performed or commissioned that address how the cost of its incentive compensation pay plans should be allocated between Kentucky-American shareholders and ratepayers.
- c. Provide all studies and analyses that Kentucky-American has performed or commissioned that address how other utilities allocate the cost of their incentive compensation pay plans between utility shareholders and ratepayers.
- d. If no studies or analyses are submitted in response to Item 3(a)-(c), explain why, in light of the Commission's findings in Case No. 2004-00103,¹ recovery of these costs in Kentucky-American's rates is reasonable and appropriate.

Response:

- a. No such studies or analyses have been performed by the Company. However, an internet search performed by the Company located numerous studies performed by others that provide support for the utilization of an annual incentive plan as part of a total compensation plan which motivates better employees' performance. While the studies available to the Company indicate a positive effect on performance of incentive payments, there is disagreement on the precise effects and meaningfulness of the metrics. Please see attached study reports. The Company has not obtained reprint rights for several of the studies reviewed, and thus they are not attached to this response.
- b. No such studies or analyses have been performed by the Company. The Company performed a search for any such studies performed by other utilities, utility industry associations or regulatory associations, and was unable to locate any such studies by others.
- c. No such studies or analyses have been performed by the Company. The Company performed a search for any such studies by other utilities, utility industry associations or regulatory associations, and was unable to locate any

¹ Case No. 2004-00103, Adjustment of the Rates of Kentucky-American Water Company (Ky. PSC Feb. 28, 2005), at 47-49.

such study. However, please see the attached memo from Towers Perrin regarding the prevalence of such plans in the utility industry, as well as general business enterprises.

- d. The Annual Incentive Plan (“AIP”) plan payouts for employees of Kentucky American are part of a total package aimed at providing competitive market based compensation for employees. The portion of total compensation represented by the AIP is an at-risk portion intended to improve performance based on the elements measured in the plan. This motivates employees to improve performance based on plan parameters. The annual payout under the provisions of the plan are considered to be earned and a portion of total compensation.

In the prior case (Case No. 2004-00103) the majority of plan potential payout was based on the financial performance of the company. However, since that time the plan metrics have been changed significantly and the Company financial performance parameters make up only 30% of the total potential plan payout for the employees included in the requested cost of service in this case. The balance of the employee incentive awards are based on metrics related to customer satisfaction, customer service quality, environmental, health and safety, efficiency metrics, or other measures of the quality of performance of the employee. Please see the plan booklet provided in AG 1-246, and salary administration information provided in AG 1-248.

Therefore, since the issuance of the Commission’s order in Case No. 2004-00103, the Company’s AIP has been changed to reflect a greater customer service quality and efficiency focus on attaining annual payout from the plan. The company therefore believes that the balance thus achieved between plan customer service objectives, efficiency objectives and financial objectives in motivating improved performance from employees makes it appropriate to recover the costs of the AIP from ratepayers.

The Company continues to maintain that the financial element of the incentive plan is beneficial to ratepayers in that a financially healthy company is in a better position to meet its public service obligations. A financially healthy company will be able to raise capital at lower cost, will be able to better respond to changes in business conditions and water quality regulations, and will be in a better position to meet the challenges of emergencies that occur from time to time. Some of the possible actions employees can take on a day to day basis directed at improving financial performance would be reducing waste or increasing efficiencies, both of which in the long term will provide a customer benefit. It is hard to envision an action an employee could take in this category which would act only as a benefit to shareholders and not to customers. Therefore it is in the customer’s interest to have a compensation plan that motivates employees to keep the company’s financial performance in mind as they go about their duties.

The company's compensation plan targets base salaries at the 50th percentile of market based compensation, based on salary surveys it performs and which have been provided previously in AG 1-242 and AG 1-248. The AIP is intended to provide the possibility of compensation at the 65th percentile if all targets are met. It is widely recognized that such plans do have a positive impact on the performance of employees as referenced in the attached studies. The design of the company's AIP does not increase compensation to lavish levels, but provides employees the opportunity to obtain compensation above the market 50th percentile, based on plan metrics. This approach gives the Company an additional means by which to retain high performing employees for whom market based 50th percentile salaries may be inadequate, but only on the basis of exceptional performance.

The wide and growing acceptance in other utilities and business in general of total compensation plans which place a portion of an employee's compensation at risk to improve business performance demonstrates that such a plan is not speculative or improvised, but is a necessary component of a program to retain employees who are qualified and capable of performing the functions necessary to operate a complex business.

For electronic version, refer to [KAW_R_PSCDR3#3_071607.pdf](#)



Memorandum

DATE: July 10, 2007

TO: Debbie Krauss-Kelleher — American Water

FROM: Larry Parks — Towers Perrin
Jim Dickinson — Towers Perrin

RE: ANNUAL INCENTIVE PLAN PREVALENCE

As requested, this memorandum provides information on the prevalence of annual incentive plans in the utility and broader general industry.

Market References and Data Sources

Energy/Utility Industry

Data are based on the total sample of companies that provided data to our energy industry compensation databases and were collected from the following sources:

- Towers Perrin's 2006 Energy Services Industry Executive Compensation Database
- Towers Perrin's 2006 Energy Services Industry Middle Management and Professional (MMAPS) Database

General Industry

Data are based on the total sample of our general industry databases excluding a number of market segments viewed by American Water as less relevant from a competitive perspective (e.g. banking, financial services, insurance, media/entertainment, pharmaceuticals). Data were collected from the following sources:

- Towers Perrin's 2006 General Industry Executive Compensation Database
- Towers Perrin's 2006 General Industry Middle Management and Professional (MMAPS) Database

A list of the companies included in each sample is provided in the attached Exhibits.

The data presented in our analysis are collected and reported by dedicated staff within Towers Perrin's Databases Unit. Data are collected each year through a survey of participating companies. Towers Perrin makes the data generated from our surveys available exclusively to participants in the surveys and does not sell, license or otherwise make the data available to any third-party sources or authorize any third

Ms. Debbie Krauss-Kelleher
July 10, 2007
Page 2.

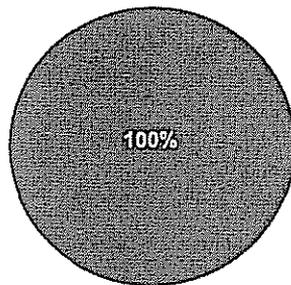
parties to use the data in any way. Data are only available for the use of participants for purposes of their individual compensation planning, and by Towers Perrin for purposes of training, quality assurance, research and development, compensation consulting services for survey participants and general promotional activities. These databases are the primary source of competitive compensation information used in our work with clients.

Results

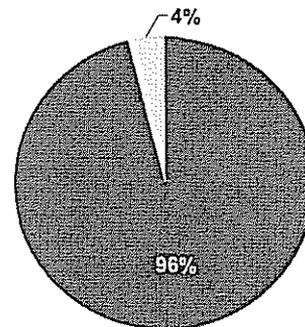
Annual incentive plans are very prevalent in both the energy/utility industry as well as the broader general industry. The following charts summarize the results of our analysis and provide data on the percent of companies that maintain a formal annual incentive plan.

Energy/Utility Industry

Executive Positions

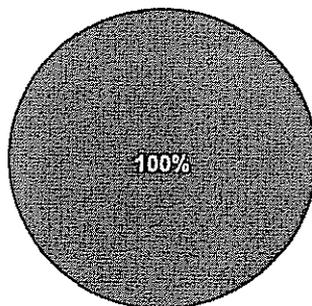


Exempt Positions

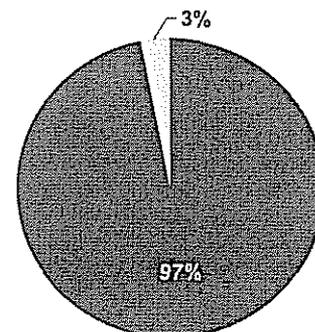


General Industry

Executive Positions



Exempt Positions



■ Maintain an annual incentive plan □ Do not maintain an annual incentive plan

Energy Services Executive Compensation Database Participants

AGL Resources	Duke Energy	NW Natural	Progress Energy
Allegheny Energy	E.ON U.S.	National Fuel Gas	Public Service Enterprise
Alleite	Edison International	New York Power Authority	Puget Energy
Ameren	Energen	Nicor	SCANA
American Electric Power	Energy East	NorthWestern Energy	Salt River Project
American Transmission	Energy	OGE Energy	Sempra Energy
Aquila	Equitable Resources	ONEOK	Southern Company
Atmos Energy	Exelon	Oglethorpe Power	Southern Union Company
Avista	FPL Group	Omaha Public Power	TECO Energy
CH Energy Group	FirstEnergy	Otter Tail	TXU
CMS Energy	Great Plains Energy	PNM Resources	Tennessee Valley Authority
CenterPoint Energy	Hawaiian Electric	PPL	UIL Holdings
Cleco	IDACORP	PacifiCorp	UniSource Energy
Colorado Springs Utilities	JEA	Pacific Gas & Electric	Unitil
Consolidated Edison	Lower Colorado River Authority	Peoples Energy	Vectren
Constellation Energy	MDU Resources	Pepco Holdings	WPS Resources
DTE Energy	MGE Energy	Pinnacle West Capital	Westar Energy
Dominion Resources	NSTAR	Portland General Electric	Wisconsin Energy

Energy Services Middle Management and Professional (MMAPS) Compensation Database Participants

AGL Resources	Dominion Resources	New York Power Authority	Public Service Enterprise
Allegheny Energy	Duke Energy	NiSource	Questar
Alleite	Duquesne Light	Nicor	SCANA
Ameren	E.ON U.S.	NorthWestern Energy	Salt River Project
American Electric Power	Edison International	Northeast Utilities	Sempra Energy
American Transmission	Energy East	OGE Energy	Sierra Pacific Resources
Aquila	Entergy	ONEOK	Southern Company
Atmos Energy	Equitable Resources	Oglethorpe Power	Southern Union Company
Avista	Exelon	Old Dominion Electric	TECO Energy
CH Energy Group	FPL Group	Omaha Public Power	TXU
CMS Energy	FirstEnergy	Otter Tail	Tennessee Valley Authority
CenterPoint Energy	Great Plains Energy	PNM Resources	UIL Holdings
Central Vermont Public Service	IDACORP	PPL	UniSource Energy
City Public Service	JEA	PacifiCorp	Unitil
Cleco	KeySpan	Pacific Gas & Electric	Vectren
Colorado Springs Utilities	Lower Colorado River Authority	Peoples Energy	WPS Resources
Consolidated Edison	MGE Energy	Pepco Holdings	Westar Energy
Constellation Energy	NSTAR	Pinnacle West Capital	Wisconsin Energy
DTE Energy	NW Natural	Portland General Electric	
Dayton Power & Light	Nebraska Public Power District	Progress Energy	

General Industry Executive Compensation Database Core Industry Participants

AAI	Cooper Tire & Rubber	Johns-Manville	Rinker Materials
ACH Food	Corn Products	Johnson Controls	Rio Tinto
AT&T	Crown Castle	KB Home	Roche Diagnostics
Aerjet	Crown Holdings	Kellogg	Rockwell Collins
Air Products and Chemicals	Cytec	Kennametal	Rohm and Haas
Alcatel USA	Dade Behring	Kerr-McGee	Russell
Alcoa	DaimlerChrysler	Kimberly-Clark	Sara Lee
Alliant Techsystems	Darden Restaurants	Kinross Gold	Schwab's
Altria Group	Dentsply	Kraft Foods	Scotts Miracle-Gro
American Airlines	Devon Energy	Land O'Lakes	Shell Oil
American Standard	Diageo North America	Lear	Sherwin-Williams
Anadarko Petroleum	Dow Chemical	Lockheed Martin	Sigma-Aldrich
Anheuser-Busch	DuPont	Lorillard	Sodexo
Apache	EMCOR Group	Lucent Technologies	Solvay America
Arby's Restaurant Group	Easiman Chemical	Marathon Oil	Sony Ericsson Mobile
ArvinMeritor	Easiman Kodak	Martin Marietta Materials	Sprint Nextel
Ashland	Ecolab	Masco	St. Jude Medical
Avaya	EnCana Oil & Gas USA	McDermott	St. Lawrence Cement
Avery Dennison	Engelhard	McDonald's	Starbucks
BP	ExxonMobil	Medtronic	Sunoco
Barrick Gold of North America	Fleetwood Enterprises	Mission Foods	Syngenta
Bayer CropScience	Fluor	Modine Manufacturing	T-Mobile
BellSouth	Ford	Molson Coors Brewing	TDS Telecom
Black & Decker	Freightliner	Monaco Coach	Tesoro
Bob Evans Farms	General Dynamics	Monsanto	Timken
Boeing	General Mills	Motorola	Trex
Boston Scientific	General Motors	NIKE	Tupperware
Bunge	Georgia Gulf	Nalco	Unilever United States
Burlington Northern Santa Fe	Goodrich	National Starch & Chemical	Union Pacific
C.H. Guenther & Son	Gorton's	Navistar International	United Parcel Service
CHS	H.B. Fuller	Nestle USA	United States Cellular
CSM North America	H.J. Heinz	Norfolk Southern	United States Steel
CSX	Harley-Davidson	Noriel Networks	United Technologies
Cadbury-Schweppes NA	Hasbro	Northrop Grumman	Valero Energy
Campbell Soup	Hercules	Novartis Consumer Health	Verizon
Carpenter Technology	Hershey Foods	Occidental Petroleum	Verizon Wireless
Charter Communications	Hess	PPG Industries	Vistar
Chemtura	Hexcel	PepsiCo	Visteon
Chevron	Honeywell	Pernod Ricard USA	Vulcan Materials
Cincinnati Bell	Hovnanian Enterprises	Phelps Dodge	W.R. Grace
Clarke American Checks	ICI Paints North America	Procter & Gamble	Washington Group International
Clorox	ITT - Defense	QUALCOMM	Wells' Dairy
Coca-Cola	International Flavors &	Qwest Communications	Wendy's International
Colgate-Palmolive	Interstate Brands	Ralcorp Holdings	Westinghouse Savannah River
Cornair	J.M. Smucker	Raytheon	Wm. Wrigley Jr.
ConAgra Foods	Jack in the Box	Reylon	
ConocoPhillips	Jacobs Engineering	Reynolds American	
Constellation Brands	Jarden	Rich Products	

General Industry Middle Management and Professional (MMAPS) Database Core Industry Participants

AAI	Cytec	Kinross Gold	Sprint Nextel
ACH Food	Dade Behring	Kraft Foods	St. Lawrence Cement
AT&T	Darden Restaurants	Land O'Lakes	Starbucks
Aerojet	Dentsply	Lorillard	Sunoco
Air Products and Chemicals	Devon Energy	Lucent Technologies	Syngenta
Alcoa	Diageo North America	Marathon Oil	T-Mobile
Alliant Techsystems	Dow Chemical	Martin Marietta Materials	Tesoro
Altria Group	DuPont	Masco	Timken
American Airlines	EMCOR Group	McDermott	Trex
American Standard	Eastman Chemical	Medtronic	Tupperware
Anadarko Petroleum	Eastman Kodak	Mission Foods	Unilever United States
Anheuser-Busch	Ecolab	Molson Coors Brewing	Union Pacific
Apache	EnCana Oil & Gas USA	Monaco Coach	United Parcel Service
Arby's Restaurant Group	Engelhard	Monsanto	United States Cellular
ArvinMeritor	ExxonMobil	NIKE	United States Steel
Avaya	Fleetwood Enterprises	Nalco	United Technologies
Avery Dennison	Fluor	National Starch & Chemical	Valero Energy
BP	Ford	Navistar International	Verizon
Barrick Gold of North America	Freightliner	Nestle USA	Vistar
Bayer CropScience	General Dynamics	Norfolk Southern	Visteon
BellSouth	General Mills	Novartis Consumer Health	W.R. Grace
Black & Decker	General Motors	Occidental Petroleum	Washington Group International
Bob Evans Farms	Goodrich	PPG Industries	Wells' Dairy
Boeing	Gorton's	PepsiCo	Wendy's International
Boston Scientific	H.B. Fuller	Pernod Ricard USA	Westinghouse Savannah River
Bunge	H.J. Heinz	Qwest Communications	Wm. Wrigley Jr.
Burlington Northern Santa Fe	Harley-Davidson	Ralcorp Holdings	
CHS	Hercules	Revlon	
CSX	Hershey Foods	Reynolds American	
Cadbury-Schweppes NA	Hess	Rich Products	
Campbell Soup	Hexcel	Rinker Materials	
Carpenter Technology	Hovnanian Enterprises	Roche Diagnostics	
Charter Communications	ITT - Defense	Rohm and Haas	
Chemtura	Interstate Brands	Russell	
Chevron	J.M. Smucker	Sara Lee	
Clarke American Checks	Jack in the Box	Schwan's	
Coca-Cola	Jarden	Scotts Miracle-Gro	
Comair	Johns-Manville	Shell Oil	
ConAgra Foods	Johnson Controls	Sherwin-Williams	
ConocoPhillips	KB Home	Sigma-Aldrich	
Constellation Brands	Keillogg	Sodexo	
Corn Products	Kennametal	Solvay America	
Crown Castle	Kimberly-Clark	Sony Ericsson Mobile Communications	

**Compensation and Incentive System
Design Study**
Independent Analysis of Incentive Compensation at the
United States Postal Service

Submitted to:

**President's Commission
on the United States
Postal Service**

June 6, 2003



President's Commission on the United States Postal Service
Compensation and Incentive System Design Study

a) Table of Contents

Section	Page Number
a) Table of Contents	2
b) Executive Summary of Recommendations	3
c) Assignment Background and Objectives	4
d) Research Methodology, History of Incentives at the USPS, and Considerations	5
e) Incentive Compensation Plan Design Best Practices	8
f) Study Findings and Recommendations	12
g) Appendix	18



President's Commission on the United States Postal Service
Compensation and Incentive System Design Study

b) Executive Summary of Recommendations

Watson Wyatt Worldwide is pleased to report the results of the Compensation and Incentive System Design Study we have conducted for the President's Commission on the United States Postal Service.

We believe it is possible to design an incentive compensation plan that will provide strategic direction and engage all employees in the goal of improving Postal Service productivity, reducing costs, enhancing customer service, and supporting the mission of the Postal Service. From our analysis, we believe that the current National Performance Assessment program (launched for fiscal year 2003 for USPS management), can be cascaded with some modification to the balance of the career employee workforce. The envisioned non-management program would be self-funded by operational financial improvement, calibrated by productivity and balanced against mission achievement.

The primary focus of a non-management program would be to reinforce and reward employees for:

- improvements in productivity
- teamwork, flexibility and responsiveness to meeting customer service levels, and
- implementing and supporting new management systems.

Our findings and recommendations are distilled from an analysis of broad USPS financial data, discussions with Postal Service associates at various levels along the spectrum, and Watson Wyatt's expertise in effective incentive plan design. At this stage of development, many of our positions are conceptual and provisional, requiring more specific Postal Service information, further modeling and testing. Significant work undoubtedly needs to be accomplished in the labor relations area. From our contact during this assignment with rank and file USPS employees, and with their bargaining unit representatives, we believe that employees appear to be more receptive to the idea of variable pay than are their union representatives.

The United States Postal Service is a complex business organization. Although change can be difficult to create within such an institution, the scale is so large that small individual improvements quickly aggregate to massive system benefits. We believe that a variable compensation program as we have described in this report can improve efficiencies in the system, and help accomplish the USPS mission on a more cost effective basis with a lower human capital content. Success will depend on proper implementation, communication, and the support of effective human resources processes such as training and performance management.



President's Commission on the United States Postal Service
Compensation and Incentive System Design Study

c) Assignment Objectives and Project Background

Assignment Objectives

Watson Wyatt was retained to assess the viability of an incentive compensation plan to engage all levels of the Postal Service workforce. The key issues addressed in our research and analysis included:

- Can an all-employee incentive compensation plan work at the USPS?
- If an incentive plan is viable at the USPS, what are the fundamental drivers for engaging the workforce?
- What are the organizational and operational considerations for a successful incentive compensation plan?

This report provides answers to the above questions as well as a recommended incentive design framework. It also includes criteria for cascading performance goals to motivate and engage USPS employees in operational improvement objectives (productivity, efficiency, quality, use of resources and customer satisfaction). The report discusses important design considerations and criteria for success. To support our recommendations and criteria, we have used published USPS performance data to illustrate various elements of our recommendations.

This report is intended as a high-level feasibility assessment and a theoretical examination of fundamental improvements that could be achieved by using an incentive compensation plan. Watson Wyatt was not contracted to provide financial modeling, assessment and analysis of current cash compensation, development of plan documents, and plan implementation and employee communication.

Background

Executive Order No. 13278 established the President's Commission on the United States Postal Service (the Commission) for the purpose of examining the state of the United States Postal Service (USPS), and to prepare and submit a report articulating a proposed vision for the future of the USPS and recommending the legislative and administrative reforms needed to ensure the viability of the USPS. The Commission sought specialized assistance from Unisys/Watson Wyatt in designing a compensation incentive system that will engage all levels of the Postal Service workforce in the goals of improving Postal Service productivity, reducing costs, enhancing customer service, and supporting the mission of the Postal Service.



President's Commission on the United States Postal Service
Compensation and Incentive System Design Study

d) Research Methodology, History of Incentives at the USPS, and Considerations

Research Methodology

Because of a compressed timeline, our research was limited to interviews at USPS headquarters, postal worker union representatives and randomly selected employee groups from Northern Virginia processing and distribution centers. We initially met with finance, human resources and labor relations executives at the Postal Service headquarters in Washington, D.C. to gather information on past and current incentive plans, operational data and labor union contacts. Next, we met individually with six labor union and management association presidents (or their designees) to discuss their viewpoints on operational improvement opportunities, the motivational effect of an incentive plan, and the overall viability of an incentive plan.¹

To gauge employee perceptions, we visited the Merrifield, Virginia processing plant to conduct focus group meetings. In total we conducted four focus groups involving approximately 40 employees. The purpose of these meetings was to gather employee perceptions and advice on opportunities for improvements within their areas of activity and their reactions to incentive opportunities.² We spoke with small (approximately 8-10 employees), yet diverse, volunteer groups of clerks, mail handlers, letter carriers and supervisors. Focus group participants were forthcoming on issues such as productivity, customer service, employee engagement and incentive compensation.

Finally, we returned to Postal Service headquarters to meet again with finance, human resources and labor relations executives to gather more refined viewpoints and data on improving productivity, reducing costs and enhancing customer service.

History of Incentives at the USPS

The Postal Service has been a pioneer in incentive pay programs within the federal government. These programs, which were designed to link incentive compensation to employee and organizational performance, have successfully improved customer service levels and productivity. Postal Service incentive plans include:

Striving for Excellence Together ("SET") – Fiscal years 1991 – 1994

Initially, this incentive plan was implemented within the mail handlers and rural carrier union represented employees and later extended to all non-bargaining employees. SET utilized two customer service measures and one organizational financial performance measure. Although the plan created organizational and employee alignment as evidenced by some employee and management collaboration, it was cancelled at its intended sunset. The payouts in the 1994 fiscal year proved to be less than meaningful to employees.

¹ See Exhibit 1 in Appendix for Union leader contacts

² See Exhibit 2 in Appendix for focus group questions



President's Commission on the United States Postal Service
Compensation and Incentive System Design Study

d) Research Methodology, History of Incentives at the USPS, and Considerations

Economic Value Added (EVA) Variable Pay Program and Individual Merit Pay Program – Fiscal years 1996 – 2001

The EVA plan was developed and implemented to reinforce the organizational directive that the Postal Service should be managed similar to a business with the goals of improved customer satisfaction, reduced costs, and improved productivity. The plan was available to approximately 83,000 Executive and Administrative Schedule (EAS) and 800 Postal Career Executive Service (PCES) employees. According to USPS reports and studies, extraordinary accomplishments were realized while EVA was in place, including significant improvements in:

- Net income
- On-time delivery
- Labor intensity (total personnel costs as a percentage of operating expense), and
- Workday injuries per 200,000 work hours.

The EVA incentive compensation plan was a team-based, gain-sharing plan that was funded by audited financial performance, and had pre-established, objective goals and targets. Despite the EVA incentive compensation plan's success, according to USPS it was cancelled after the 2001 fiscal year due to outside criticism and political pressure.

National Performance Assessment (NPA) – Effective fiscal year 2003

Similar to the previous EVA plan, the newly implemented NPA plan is based on a balanced scorecard approach of organizational measures. Objective measures, including customer service, employee productivity, and business productivity, are pre-established and results are measured for each Performance Cluster, each Area, and nationwide. The plan will be funded through improved business performance. Plan rewards (including lump sum incentive payments and base salary increases) will be allocated based on individual performance assessment. An individual's performance will be assessed such that 70% of the evaluation will be based on contribution to corporate/individual success and 30% of the evaluation will be based on contribution to core requirements of the position.

Based on individual performance and the employee's salary level relative to the salary range maximum, salary increases can range from 0% to 14%. In addition, lump sum incentive payments (as a percentage of base salary) can range from 1% to 6% for those rated as contributors to as much as 15% for those rated as exceptional contributors. According to USPS representatives, incentive payments earned above the current statutory salary cap are deferred (determination of deferral payout timing to be determined by the USPS Board of Governors).

This plan is currently available to all PCES employees and may possibly be available to both EAS and PCES employees in fiscal year 2004. It should be noted that according to USPS executives, senior management has been willing to extend these programs to collectively bargained employee groups, but has met resistance by union leadership.



President's Commission on the United States Postal Service
Compensation and Incentive System Design Study

d) Research Methodology, History of Incentives at the USPS, and Considerations

Considerations

Prevalence of Incentive Programs

Variable incentive designs have increased in popularity and prevalence nationally because they provide a means of controlling costs, supporting long-term cultural change efforts, and directing performance toward the accomplishment of business objectives. According to the 2002-2003 Industry Report on Technician and Skilled Trades Personnel Compensation report published by Watson Wyatt Data Services, 68% of survey respondents (or 996 organizations covering 405,302 employees) indicated they currently have a bonus or variable pay program in which technician and skilled trades personnel participate. Of the 405,302 incumbents for whom data were reported, 34.6% received variable pay awards in 2001 averaging 5% of base pay.

Although employers with collectively bargained workforces are not specifically segregated in the study, not-for-profit organizations (whose not-for-profit status may be likened to that of the USPS) are well represented. The report indicates that approximately 48% of not-for-profit organizations currently have a bonus or variable pay program. Additionally, in this same survey, another 14% of survey respondents (or 593 organizations) indicated that they will install new variable pay programs for technician and skilled trades personnel in the next two years. Not-for-profits reported an even higher rate of 18%.

The National Compensation Survey: Occupational Wages in the United States, January 2001 (released in January 2003) prepared by the U.S. Department of Labor Statistics indicates that among the blue collar occupational group, employees with wages that are at least partially based on productivity payments such as piece rates, commissions, and production bonuses earn approximately 12% more per hour than those workers whose wages are based solely on an hourly rate or salary. Although no conclusions are drawn by the Department of Labor on this differential, it might be indicative of higher overall pay for higher personal performance. In other words, those employees that are focused on performance objectives tend to achieve those objectives and are rewarded.

Incentive Plans in Collectively Bargained Environments

The 2002 Employer Bargaining Objectives survey of establishments with collective bargaining agreements was conducted by the Bureau of National Affairs. Among other things, the survey examined the prevalence of incentive and variable pay plans in current contracts. According to their research (all employers, both manufacturing and non-manufacturing), 16% of employers utilize group incentive plans, 10% utilize gain-sharing plans, 9% utilize individual incentive plans, and 7% utilize profit-sharing plans. These percentages are approximately 50% higher for manufacturing (processing) concerns. Also, according to the research report 10% of the surveyed employers hope to establish at least one new incentive in their next agreement, and 7% will bargain to expand one or more current variable pay systems.



President's Commission on the United States Postal Service
Compensation and Incentive System Design Study

e) Incentive Compensation Plan Design Best Practices

Role of Incentive Plans

Rewards are fundamentally communication vehicles, sending messages that are consistent with, and that reinforce, other messages employees are receiving about business goals, desired behaviors and culture. Organizations that use incentive plans effectively recognize that an incentive plan is but one component of the total reward philosophy of the organization. Other essential components to engage and reward the workforce include wages, benefits and recognition programs, as well as opportunities for skill training, communications, performance management, employee involvement and safe working environments.

As organizations are pressured to achieve higher levels of performance and productivity, they are searching for ways to leverage limited resources. Variable incentive pay is the number one design used to influence short- to mid-term business results. Coupled with astute strategy, solid leadership and good working conditions, variable pay incentive designs can:

- Communicate priorities to indicate the relative importance of certain objectives and goals of the organization
- Engage employees in business success by sharing the gains realized from changed behaviors
- Reward valued skills and behaviors
- Create business literacy by educating employees on how and why their contributions will benefit them and their organizations
- Create esprit and solidarity through a common cause and renewed energy, and
- Contribute to a compelling place to work.

In highlighting the qualities of an effective incentive plan, it is also important to consider what an incentive plan cannot do. An incentive plan cannot:

- Replace trusted, quality leadership
- Create results where barriers exist that inhibit performance (for example, technology deficiencies or process inefficiencies)
- Fix an outdated or ill-conceived business strategy, or
- Meet all of an organization's human resources objectives.

Because the purpose of variable incentive plans is to energize and focus employee efforts, the design must "fit" the culture and specifically address the needs of the organization. To this end, the design process is often iterative and complex. An effective plan design must be based on a philosophical underpinning, clearly defined objectives, line of sight metrics, appropriate performance periods, reasonable investment returns and, most importantly, communication, coaching and performance management. More information about these and other factors is presented below.



President's Commission on the United States Postal Service
Compensation and Incentive System Design Study

e) Incentive Compensation Plan Design Best Practices

Factors Influencing the Effectiveness of Incentives

An effective incentive program motivates employees toward desired performance behaviors that translate into results for the organization and rewards for the employees participating in the program. An effective Postal Service incentive plan should cause employees to do something that they would not otherwise do if the plan did not exist.

Although a variety of issues can impact the effectiveness of an incentive plan, the items below constitute key elements that should be considered when assessing the Postal Service's ability to translate an incentive plan idea into a viable, robust reward tool. The greater the degree to which these elements exist in the USPS, the more likely it is that an incentive plan will produce the desired performance and a reward that is considered worthwhile by participants.

Plan Design

- The plan design effectively aligns strategic operating priorities with desired employee behavior
- Performance metrics appropriately balance competing priorities, including productivity and quality
- Stakeholders concur that targeted performance levels are realistic and potential incentive payments are fair, thereby creating a "win-win" work environment

Simplicity

- The plan design (including measures, relevance to employee behaviors, and payout potential) must be easy to understand by all employee levels
- The plan should be simple enough that it easily engages employees to work toward USPS objectives (simplicity must relate to complexity of jobs participating)

Implementation and Communication

- The design and related implementation communications are pre-tested for clarity and understanding
- Communication of performance results and progress toward goal attainment is comprehensive and clear
- The measurement, tracking and reporting process is regarded by all as credible and reliable

Line-of-Sight

- Employees must believe they are able to make an impact on the objective being measured through their performance
- An action causes a reaction (positive or negative) – individual performance or impact is recognized by the immediate supervisor



President's Commission on the United States Postal Service Compensation and Incentive System Design Study

e) Incentive Compensation Plan Design Best Practices

- Employees understand and embrace the performance measures
- Performance measures should cascade down through the USPS (i.e., narrower in scope with each descending responsibility level, but still aligned with the strategies supported by the NPA plan)

Integration of Plan with other Organizational Processes and Systems

- The incentive plan performance measures are integrated within a rigorous performance management process that sets expectations, measures performance, and provides feedback to employees about how well they are meeting expectations
- The performance management process translates, encourages and reinforces behaviors that lead to positive results
- A process exists for employees to provide feedback regarding barriers to performance improvement and to participate in problem solving aimed at eliminating barriers and improving business performance

Return on Investment

- To be successful, the plan must generate more return for the USPS than is paid to employees
- Positive financial returns must be carefully balanced against other non-financial measures

Culture and Organizational Context

- A level of open communication and trust exists among peer employees and between levels within the USPS
- Units, divisions and departments embrace teamwork, especially where work processes cross such boundaries
- Consistent messages are sent about what's important and required from employees in terms of results and behaviors

A well designed and implemented incentive plan can actually facilitate a change of culture over time. For example, an incentive plan that focuses on measures that span work groups, encourages employees to think about work beyond their own team and to focus on the "hand-offs" that occur from one group to another.

The Design Process

As indicated earlier, the design process is iterative. While there is a logical, sequential design process to follow, individual design decisions often overlap and should not be considered final until all design features have been finalized. Following is an outline of the primary design steps:



President’s Commission on the United States Postal Service
Compensation and Incentive System Design Study

e) Incentive Compensation Plan Design Best Practices

Design Step	Key and Design Issues
Develop Philosophical Underpinning	<ul style="list-style-type: none"> • Where does variable incentive pay fit into USPS total reward philosophy? • When do we use it and what is the value proposition to employees? To the organization?
Establish Plan Objectives and Purpose	<ul style="list-style-type: none"> • Overall purpose and expected outcomes of the design
Select Plan Participants	<ul style="list-style-type: none"> • Eligibility, including collectively-bargained employees • Impact on cross-organizational processes
Develop Performance Measures/Metrics	<ul style="list-style-type: none"> • Desired results / work behaviors • Business success factors • Line-of-sight; simplicity
Perfect Targets, Leverage and Administrative Mechanisms	<ul style="list-style-type: none"> • Formulas (based on stretch performance) • Modifiers / triggers • Performance period and payout frequency • Performance tracking and reporting capability
Assess Plan Funding and Return on Investments	<ul style="list-style-type: none"> • Budget • Evaluation of effectiveness
Prepare for Plan Implementation and Ongoing Performance Management	<ul style="list-style-type: none"> • Communications • Coaching and feedback • Integration with other operating and performance management initiatives

It is critical to include in the design process ample time to adequately identify, evaluate and balance performance metrics. The performance metrics must be properly matched to employee level for engagement purposes. It would not be prudent to establish performance metrics for craft employees that bear no relation to their everyday responsibilities (i.e., no line-of-sight).



President's Commission on the United States Postal Service
Compensation and Incentive System Design Study

f) Study Findings and Recommendations

Can an all-employee incentive compensation plan work at the USPS?

From Watson Wyatt's point of view, an organization-wide incentive program with set targets and cascading performance goals designed to motivate individuals and engage all USPS employees in specific behaviors related to improving productivity, reducing costs and enhancing customer service makes very good sense. We believe, if designed correctly, it could result in improved financial performance and help illuminate improvement opportunities between operating units engaged in collection, processing and delivery. We are of the opinion that an organization-wide incentive design would also enhance solidarity among the ranks and serve to create line-of-sight for employees between their contributions and attainment of USPS's operating objectives.

Obviously, there are important considerations in evaluating the viability of an all employee incentive plan, such as union and employee support. Further, the plan must be designed to be self funded.

If an incentive plan is viable at the USPS, what are the fundamental drivers for engaging the workforce?

Inasmuch as the National Performance Assessment Program has recently been put in place for USPS management, we have focused our recommendations on the creation of a complimentary, cascaded design for the 754,000 USPS field career employees. Our preliminary incentive design criteria for these employees are that the plan would be:

1. Self-funded
2. Calibrated by productivity and mail volumes
3. Triggered by mission achievement.

Following are recommended design criteria:

1. **Self Funded:** The new plan should be self-funded, which means that USPS shares a portion of improved economic gains with employees.
2. **Calibration:** We believe that metrics that correlate with improved financial results should be used to set targets, track progress and determine award values for employees. From the USPS 2002 Annual Report we calculate that fully 79% of USPS's 2002 operating costs are related to the provision of compensation and benefits for employees. Therefore, we believe that good measures for tracking improved financial results are those associated with improved productivity and efficiency. For this reason, we believe that a target set around "Pieces per Employee" that move through the postal service system will appropriately track and report operating efficiencies for employees engaged in mail collection, processing and delivery. As a safeguard for service quality, it is anticipated that



President's Commission on the United States Postal Service
Compensation and Incentive System Design Study

f) Study Findings and Recommendations

a second measure, such as percentage of ontime delivery, would serve as a "trigger" or threshold under which productivity improvements would be penalized.

Total Factor Productivity (TFP) which the Postal Service has used to track productivity for several years, is an alternative metric to Pieces per Employee. However, as it incorporates labor and capital productivity, it is further removed from the labor component of the productivity equation. Further, even when process improvements are achieved via, for example, new technology or other capital investments, eventual cost reductions (a key goal) are primarily realized by lower labor content.

We believe that the Pieces per Employee measure has several very functional attributes:

- It is simple to understand by all employees
- Its line of sight is short, relating to the work of nearly every Postal Service field employee
- The numerator of the formula, i.e., pieces of mail processed through the system, and the denominator, employees, are currently tracked and publicly reported by the Postal Service
- Employees are likely to trust the reported numbers
- The measure is the essence of productivity; performance can be enhanced by processing more with static resources and/or reducing resources, and
- The measure could be the foundation of a communication program to educate employees on the interrelationships between employees and departments/units on getting the mail collected, processed and delivered.

One of the few shortcomings of this measure is that its relation to cost reduction or revenue generation is indirect. That is, individual and group productivity can improve in an environment of escalating costs for compensation, benefits, equipment, etc., and the improvements are obscured.

3. **Mission:** According to USPS officials, failure to achieve on-time delivery service levels over a period of time is predictive of decreased mail volume and heightened customer dissatisfaction. Inasmuch as achievement of the USPS's universal distribution mission is financially bolstered by first class mail and package services, customer loyalty is an important component of the USPS business model. As such, our recommendation is to use achievement of customer



President’s Commission on the United States Postal Service
Compensation and Incentive System Design Study

f) Study Findings and Recommendations

service guarantees at current national levels as a “proxy” for customer loyalty and satisfaction and to set a performance threshold below which the plan does not pay, regardless of improvements in productivity.

Measurement of Pieces Per Employee

We recommend that the “Pieces per Employee” (PPE) performance be measured at the district or “cluster” level and be conducted on a quarterly basis. The performance bonus pool would be generated on a quarterly basis for PPE over a threshold and paid to employees within 30 days of quarter’s end. It is also our recommendation that the measurement of pieces of mail be done as it is currently. To convey the message that performance is in the control of front-line employees, it is recommended that the numerator of “employees” be defined as field career employees assigned to a Performance Cluster or appropriate district. Removed from this group are all employees participating in the National Performance Assessment, other headquarters personnel and all non-career employees.

Illustration of Past Pieces Per Employee Results

The following table, from data disclosed in the USPS 2002 Annual Report, shows the PPE for the last five years:

Pieces Per Employee Results 1998-2002				
Year	Field Career Employees ³	Pieces of Mail (millions)	PPE	% Change from Prior Year
2002	743,000	202,822	273,000	+ 0.55%
2001	764,000	207,463	271,500	+ 1.23%
2000	775,000	207,882	268,200	+ 4.56%
1999	786,000	201,644	256,500	+ 1.75%
1998	781,000	196,905	252,100	

From our calculations, over a five year period, a compounded annual rate of improvement of 1.6% was accomplished with only the existing recognition and reward programs. From remarks of Postmaster General Potter in the 2002 Annual Report, the 2002 results contributed to Postal Service cost avoidance of \$2.8 billion. For illustrative purposes, the USPS might consider an annual PPE productivity improvement of 1.6% as a threshold level of improvement, at or below which no additional rewards should be made. The portion of financial gain above the threshold to share between employees and the USPS must be modeled.

³ Exclusive of headquarters and non-career employees.



President's Commission on the United States Postal Service
Compensation and Incentive System Design Study

f) Study Findings and Recommendations

Plan Cost and Return on Investment Illustrations

To assess whether the underlying plan design concept is viable, it is necessary to illustratively model plan costs and return on investment. The modeling is based on information found in the USPS 2002 Annual Report.

Total direct compensation, i.e., salaries and wages, in 2002 were disclosed to be \$36.9 billion for all USPS employees. Based on our assumption that, on average Headquarters compensation is 120% of field career compensation, and non-career employee compensation is 20% of field career, we arrive at an average annual total pay for field career at \$47,800. This would include overtime pay. It is estimated that benefits would add an additional 30%, or \$14,400 to the average total annual cost per field career employee, for a total of \$62,200. A more detailed analysis can be conducted as the bonus plan design is refined.

Watson Wyatt surveys show that many organizations pay bonuses to employees below the management levels, as presented earlier. The average bonus as a percentage of salary or wages is shown to be very modest in some sectors, such as not-for-profit organizations. It is our belief that bonuses as little as 2.5% to 3% of wages can draw employees' attention and begin to encourage work-related behavior changes. At the other end of the reward spectrum, we do not believe it is necessary to award more than 7% to 8.5% of wages to achieve full employee involvement in the program. It is also essential that incentive payouts have noticeable volatility, including zero to avoid establishing an entitlement attitude among participants. With the population we have defined as eligible for the broad-based employee bonus plan, 3% of compensation is about \$1.07 billion and 7% is nearly \$2.5 billion.⁴

What level of productivity improvement or revenue generation is necessary to fund these payouts? Revenues achieved through postal rate increases must be removed from the bonus calculations. Further, revenues are a suboptimal measure since it is not clear how employees in the group we are addressing can drive demand, other than the practice of effective customer relations by those who have public contact.

The true leverage in the plan concept is to process the same or greater level of production with fewer resources. If mail volume declines, the human capital content must decrease more rapidly. All this must be accomplished either through improved individual productivity or advances in technology. Many employees we spoke with in the focus groups believe individual productivity can be improved.

⁴ However, since the payroll includes overtime, these figures are likely overstated for a bonus plan that would be calculated based on straight-time salary or wages



President's Commission on the United States Postal Service

Compensation and Incentive System Design Study

f) Study Findings and Recommendations

Static examples of productivity improvements necessary to fund bonus pools are calculated in the following table. Although we recommend that the unit of measurement be at a Performance Cluster or district level, until those figures are analyzed, we present calculations on a system-wide basis.

A. Expected improvement in PPE at annualized 1.6% (2002: 273,000 PPE × 1.016 = 2003 Minimum PPE)	277,400
B. Human capital reduction to achieve 2003 Minimum PPE [2002 Employees minus (2002 Pieces ÷ Minimum PPE)]	12,000 employees
C. 2003 Pieces to achieve Minimum PPE (2002 Employees × 2003 Minimum PPE)	206.4 billion
D. Cost to fund 3% bonus pool (i.e., Threshold Bonus)	\$1.07 billion
E. Total human capital reductions to fund 3% pool [(\$1.07 B ÷ \$62,200 cost per field employee) + 12,000]	29,200 employees
F. Threshold <i>quarterly</i> bonus for \$40,000 employee @ 3%	\$300
G. Cost to fund 7% bonus pool (i.e., Superior Bonus)	\$2.5 billion
H. Total human capital reductions to fund 7% pool [(\$2.5 B ÷ \$62,200) + 12,000]	52,200 employees
I. Superior <i>quarterly</i> bonus for \$40,000 employee @ 7%	\$700

In the above example, presented for illustrative purposes only, a dynamic model would include a combination of mail volume volatility as well as human capital efficiencies. With static mail volume assumed in the illustration, the number of employees becomes dynamic. Clearly, headcount reductions cannot continue indefinitely at the USPS. Therefore, at some future point efficiency gains based on this incentive plan will stagnate and the incentive plan may need to be recalibrated. We would advise the Postal Service to carefully evaluate these issues annually.

In Line B above, the cost avoidance of \$62,200 for each of 12,000 employees is about \$750 million, approximately three-quarters of our estimate of the total increase in compensation and benefits for 2003. In Line C, an increase of 3.6 billion pieces, at an average rate of \$0.33 per piece (based on 2002 volume and revenues) would generate



President's Commission on the United States Postal Service
Compensation and Incentive System Design Study

f) Study Findings and Recommendations

about \$1.2 billion of additional revenue. It is the cost avoidance or cost reductions above these levels that are expected to fund the employee incentive pool. In addition, depending on USPS's human resources strategies regarding increases in wages, it may be possible to divert these wage costs from fixed to variable expenses and assist in incentive pool funding.

It is expected that declines in service quality will severely affect the funding of the incentive pool. From an achievement of mission point of view, we believe it is prudent to set Performance Cluster/district on-time delivery levels as the threshold for plan payment. To the extent current levels cannot be maintained, the plan would not make incentive payments. This incentive plan design element will clearly communicate to employees the critical organizational objective of customer service and satisfaction.

What are the organizational and operational considerations for a successful incentive compensation plan?

Setting performance targets is a crucial exercise in the operation of any incentive plan. If the probability of achieving some payment from the plan is seen as too low, it will not motivate participants to change behaviors. Indeed, it could have a damaging effect on employee morale and their attitudes toward Postal Service management. On the other hand, goals that are set too low provide inadequate returns to the organization and an entitlement expectation among employees, which may not be reversible without damage to morale. The definition of precise performance targets, triggers, performance periods and other administrative design elements requires data analysis and modeling with actual performance information.

Performance measurement periods need to be tied closely to process periods and the nature of the jobs covered by the plan(s). As a broad generalization, craft employees' individual and group performance should be measured and communicated frequently (daily, weekly, and monthly), whereas executive and management performance should be measured and communicated on a somewhat longer time horizon (monthly, quarterly, and annually). While the performance cycle for the employee group we are addressing should have a short time horizon, it must be long enough to gauge productivity properly. Until we know more about the measurement process and other ingredients of productivity in the Postal Service, we believe quarterly cycles balance these issues.



President’s Commission on the United States Postal Service
Compensation and Incentive System Design Study

g) Appendix

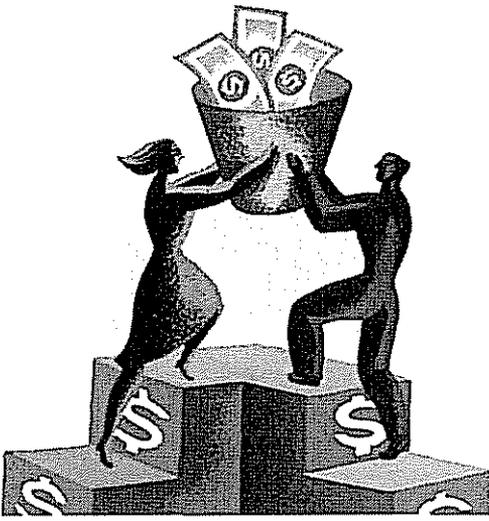
Exhibit 1 – Union Leaders Participating in Study

Mr. William Burrus, President	American Postal Workers Union, AFL-CIO
Mr. Gus Baffa, President	National Rural Letter Carriers’ Association
Mr. William Young, President	National Association of Letter Carriers, AFL-CIO
Mr. Steve LeNoir, President	National League of Postmasters of the United States
Mr. Vincent Palladino, President	National Association of Postal Supervisors
Mr. Bruce Lerner, General Counsel	National Postal Mail Handlers Union

Exhibit 2 – Employee Focus Group Questions

- | |
|---|
| <ol style="list-style-type: none"> 1. If you were to tell me that the USPS had a great year last year, what measures would you point to as proof? 2. Are employees as productive as they can be? If not, what are the obstacles? 3. Please provide your thoughts and ideas on measuring your work. 4. Why is customer service important? How do you know when you have met customer service expectations? 5. Would you like an incentive compensation plan? Why? |
|---|





Annual Cash Incentives for Managerial and Professional Employees



Dow Scott, Ph.D.
Loyola University Chicago



Thomas D. McMullen
Hay Group



Marc Wallace
Hay Group



Dennis Morajda, MSIR
Performance Development
International Inc.

Since the early 80's, there has been a substantial increase in the use of variable pay as a percentage of total pay that managers and professionals receive. In recent years, management's mantra has been to increase the "leverage" of variable pay to better align managers and professionals with the business, to encourage outstanding performance, to share the risk of business success and to more fairly reward those employees who make the largest contributions. With the exception of executive compensation, few research studies have attempted to link annual cash incentive pay programs to organizational effectiveness. Lack of empirical evidence, however, has not prevented compensation managers, academicians and consultants from suggesting that organizations can gain a competitive advantage by using variable pay to increase performance. Since annual cash incentives are widely used with managerial and professional employees, it would be in management's best interests to learn which designs of annual cash variable pay programs are most effective. Consequently, this study attempts to identify the most common design features of annual cash variable pay programs and determine if certain design features are more effective than others in driving organizational performance.

Research Methods

Identifying the Research Population

The first phase of the study focused on identifying the common features of annual variable pay programs in use today by reviewing the literature and discussing this issue informally with academics, consultants and practitioners. Differences in terminology and program definitions used in the compensation field created a significant challenge to the research. To meet this challenge, the team tried to find the most common or universally used terminology and definitions for policies or programs to minimize confusion for respondents.

The research team also recognized that there are variations in variable pay programs across different organizational levels and occupations within the same organization. For example, outside sales incentive programs are designed very differently than incentive programs for managers in a manufacturing operation. Consequently, research focused on managerial and professional employees for four reasons. First, most organizations tend to have a uniform set of policies and practices for this group. Incentive plans associated with the senior executive team or sales professionals were excluded from the study because incentive programs are often customized for these groups and even for individuals within these groups. Second, compensation managers will likely have substantial knowledge of the variable pay policies and programs for professional and managerial employees since they are typically accountable for program administration and are probably included in this group for pay purposes. Third, this employee group tends to have a significant impact on total organizational performance, making this a critical group to understand in terms of pay policies and programs and organizational effectiveness. Finally, the focus of the study provided continuity since managers and professionals were the focus of our previous study that examined the linkages between base-pay policies and practices and organizational effectiveness.

The focus of the study provided continuity since managers and professionals were the focus of our previous study that examined the linkages between base-pay policies and practices and organizational effectiveness.

Developing the Survey Instrument

In phase two, the team constructed a data collection instrument with statements and response categories that generated a set of standardized responses for use in quantitative analysis of the data. To enhance the richness of the findings, open-ended questions were also included to ensure that nonstandardized responses were captured. There were three cycles of pilot tests with compensation managers, consultants and academics before the survey instrument was finalized.

The final version of the survey instrument asked participants to describe and evaluate the annual variable pay program for which their managerial and professional employees were eligible as it related to:

During a two-week period, a total of 958 members responded.

This represents variable pay programs covering approximately 2.8 million management and professional plan participants from a cross section of industries.

- ▶ Design features of the annual cash incentive pay program
- ▶ Identification of those involved in program design
- ▶ Administration and implementation
- ▶ Evaluation of program effectiveness

The study did not examine equity pay programs because a long-drawn-out survey might have discouraged compensation managers from responding.

Defining "Successful"

We used three measures to determine the effectiveness of the annual variable compensation program. First, the team compared the pay policies and programs between companies included in *Fortune* magazine's 2003 "America's Most Admired Companies" list for their industry sector and those that did not receive the designation. *Fortune's* "Most Admired Companies" is a

highly regarded annual survey of corporate reputations, conducted by Hay Group, of more than 10,000 executives, directors and analysts. The survey invites them to rate companies overall and within industry groupings on eight criteria ranging from financial soundness and use of corporate assets to quality of management, products and services.

Second, the team collected 2003 total shareholder return (TSR) information for the publicly traded companies that responded to this survey. TSR is defined as the monthly percentage growth in stock price and dividends paid over a five-year period. The team divided the TSR data into quartiles and compared survey responses for the highest TSR quartile (i.e., the top 25 percent of companies) with data from companies in the lowest or bottom quartile of TSR (i.e., the lowest 25 percent of the companies).

Finally, survey respondents were asked to make a personal assessment of the effectiveness of their compensation policies and practices. Although this measure may be subjective, we believe that the education and experience of most compensation managers provides a relatively valid indicator of program success.

Response Rate

A representative sample of more than 9,000 WorldatWork members was sent a Web link to the electronic survey instrument in late November 2003. The membership sample targeted the highest-level compensation manager for each company. Virtually all responses were from compensation professionals or HR managers who had significant responsibility for compensation decisions. During a two-week period, a total of 958 members responded. This represents variable pay programs covering approximately 2.8 million management and professional plan participants from a cross section of industries including manufacturing (26 percent), financial and insurance (22 percent), information (seven percent), health care

and social assistance (seven percent), utilities (seven percent) and professional, scientific and technical services (five percent).

Key descriptive findings are highlighted in the following section. Additional relevant descriptive statistics are provided in this report's appendix. All percentages are rounded up from .5 and therefore may not equal 100 percent.

More than 99 percent of respondents completed the entire survey and were included in the analysis. Figures 1, 2 and 3 show how the sample represented virtually all industries and organization sizes. The analyses reported here are descriptive statistics and t-tests comparing responses between "Most Admired" and other companies, and comparing companies with the highest TSR (i.e., top quartile) and the lowest TSR (i.e., bottom quartile).

Research Findings

Program Features

Over the past two decades, the prevalence of variable pay programs has increased substantially and today a significant majority of organizations offer these programs. Seventy percent of respondents believed that variable pay was "important to very important" to the success of their organizations' competitive strategies.

Type of Variable Pay Program	% of Managers and Professionals Eligible	% Responded Strongly to Moderately Effective
Individual-based Performance Programs	79%	89%
Team-based Performance Programs	48%	83%
Gain-sharing Programs	19%	72%
Profit or Revenue Sharing Programs	46%	69%
Equity Programs	59%	68%
Spot/Other Cash-based Recognition Programs	75%	70%

Annual (or short-term) Variable Pay	% Used
Individual measures only	25%
Group measures	75%

Individual measures only	25%
Corporate measures only	31%
Business unit, team, department measures only	16%
Combination of corporate, business unit and individual measures	15%
Other combinations	13%

Primary Objectives of Variable Pay Program (Respondents asked to select three most important)	Percentage
Improve organization or team financial performance	65%
Create a more competitive total compensation market position	58%
Improve individual performance or productivity	47%
Improve overall productivity	32%
Better recognize employee contributions	32%
Promote a sense of ownership	22%
Use variable pay to better manage compensation costs	17%
Improve employee involvement	12%
Support culture change	8%
Reduce employee turnover	7%

Furthermore, 36 percent believed that it is "moderately important" for "most" employee groups and 44 percent believed that variable pay is "important" for "all" employee groups

Data shown in Figure 1 excludes organizations that do not offer variable pay eligibility to both managers and professionals. However, 14 percent of this sample grants eligibility to "managers only" (not including the senior executive team), while less than one percent grants "only to professional" employees. Specifically, Figure 1 details the types of variable pay programs for which managers and professionals are eligible and rates the effectiveness of those programs

Figure 2 indicates the types of measures used to determine performance. A majority of organizations in the survey (75 percent) utilize some form of group measure in variable pay plan design and 25 percent of organizations rely on individual performance measures alone to determine payouts. Of the organizations using group measures, a significant subset uses corporate performance measures only (31 percent)

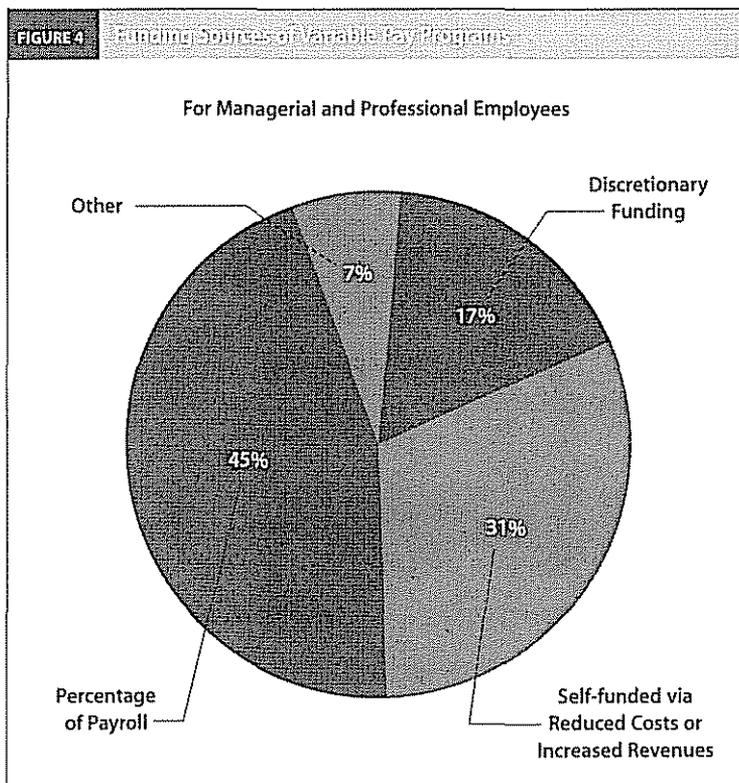
When asked their view regarding leverage (i.e., variable pay as percentage of base pay), 73 percent of compensation managers believed that their managerial and professional employees were "moderately to aggressively leveraged" as compared to other companies in the labor market. As might be expected, higher-paid professionals and managerial employees are more highly leveraged than those who are paid less. The range of reported variable pay (as a percentage of base) is provided below:

- ▶ Paid less than \$50,000 are leveraged zero to nine percent
- ▶ \$50,000 to \$99,000 are leveraged 10 to 24 percent
- ▶ \$100,000 to \$149,000 are leveraged 10 to 39 percent

- ▶ \$150,000 to \$199,000 are leveraged 10 to 59 percent
- ▶ \$200,000 to \$299,000 are leveraged 40 to 79 percent.

Survey participants reported diverse reasons for providing variable pay programs to managerial and professional employees. Figure 3 indicates the number of respondents who said a particular objective was one of their top three objectives for the variable pay programs. "Improve organization or team financial performance," "create a more competitive compensation market position" and "improve individual performance" are the most frequently mentioned variable pay objectives. Improved overall productivity and employee recognition are in the second tier of objectives.

Three primary funding sources for the managerial and professional annual or short-term variable plans were identified, as shown in Figure 4, (i.e., discretionary, percentage of payroll and self-funded). Discretionary is defined as a means of funding in which, near the end



of the performance period, the senior managers simply determine what the bonus pool will be and establish some method for dividing up the pool (i.e. the amount paid out is at the management's discretion). It was interesting that almost half (45 percent) of the managerial and professional annual incentives were simply budgeted as labor costs as opposed to self-funded plans (31 percent).

Organizations tend to provide corporate safeguards in the design of variable pay programs. The survey indicated that 82 percent of variable pay programs have a hurdle or trigger that can cancel a payout and 87 percent of programs have pre-established performance levels. Likewise, most organizations have a maximum cap on earning opportunities in the variable pay program. Approximately 80 percent of those surveyed utilize a performance cap on potential variable pay earnings. Figure 5 shows that most caps are between 1.5 and 2 times the target.

It should be noted that nearly one quarter of plans have a maximum that is between 100 and 124 percent of the target. Our experience tells us that these are likely to be plans based on a hurdle. In other words, there is a specific objective to achieve and once the objective is achieved, there is a payout. Conversely, there is no payout if the objective is not achieved and there is no increased payout if results beyond the objective were achieved.

FIGURE 5: Performance Targets	
If Plan Contains a Cap, the Maximum % of the Target	Percentage
100 – 124%	24%
125 – 149%	12%
150 – 199%	27%
200 – 249%	25%
250 – 300%	3%
Over 300%	1%
Not applicable	8%

Figure 6 shows that the vast majority of variable pay programs for managerial and professional employees are paid annually.

Program Communications and Implementation

The survey indicates that 81 percent of the variable pay programs have been revised in the "last five years" with 47 percent revised during the "last two years." The primary designer of the variable pay plan for 66 percent of the respondents was "Human Resources," often with input from senior management. It is interesting to note that 23 percent of responding organizations "seldom involved eligible employees" in the design of the program.

Sixty-seven percent of compensation managers believe that "most to all eligible employees" understand the variable pay program.

Ninety-three percent of respondents indicated that they provided some variable pay communication. The findings report in Figure 7 on page 12 indicates that variable pay plans are communicated in diverse ways. "One-on-one discussions with supervisors" and "written materials outlining the plan" were listed as the primary means to communicate changes in the plan to employees. This indicated to us that executives use traditional, reliable and perhaps the most effective forms of communication.

FIGURE 6: When Programs are Paid Out	
Primary Variable Pay Program Designed to Pay Out:	Percentage Responses
Annually	81%
Semi-annually	5%
Quarterly	7%
Monthly	1%
Achievement of objectives/milestones	2%

FIGURE 7 Communication Methods	
Details and Updates are Communicated Through:	Percentage Responses
One-on-one discussions with supervisor	55%
Written materials outlining plan	52%
Information posted in a public place or on the intranet	31%
Employee meetings	34%
Variable pay information in NOT communicated	7%

Variable Pay Program Effectiveness

Compensation managers were asked to rate the effectiveness of their variable pay program for managers and professional employees on several dimensions. Figure 8 shows the percentage of managers that said that the variable pay plan was effective or very effective for the stated dimension. Figure 8 indicates that approximately two thirds of compensation managers are satisfied with the overall effectiveness of their variable pay programs. However, this still indicates that a significant minority (one in three) is not satisfied. The items that scored higher on perceived effectiveness tend to be design-related attributes such as frequency of payouts, funding mechanism and appropriateness of measures. The relationship between payouts and organization performance also scored high, but the relationship of payouts to individual performance and team/group performance scored lower. The motivational value of the program also scored relatively low. We could imply that since a high percentage of plans are based on corporate measures only, the motivational impact at the individual level is diluted.

The criteria used to judge the effectiveness of managerial and professional annual or short-term variable pay programs are shown in Figure 9.

FIGURE 8 Effectiveness of Programs	
Variable Pay Program Dimension	Percent Responded Effective to Very Effective
Frequency of payouts	79%
Funding mechanism	77%
Relationship between variable pay program payouts to organizational performance	72%
Appropriateness of the variable pay plan measures	68%
Overall effectiveness	64%
Administrative ease	64%
Appropriate return on investment	62%
Employee understanding the program	61%
Motivational value of the program	55%
Relationship between variable pay program payouts to individual performance	53%
Responsiveness to change	50%
Relationship between variable pay program payouts to group or team performance	43%

FIGURE 9 Criteria Used to Judge Effectiveness	
Criteria Management Uses to Judge Effectiveness of Their Programs (Respondents asked to select all that apply)	Percent Response
Business operating results	73%
Informal opinion gathering from senior leadership	35%
Employee satisfaction survey measures	30%
Employee productivity metrics	28%
Employee turnover or retention	27%
Informal opinion gathering from employees	23%
Management does not evaluate variable pay plan success	16%
Labor costs are controlled or lowered	9%

Respondents indicated that “business operating results” are the primary criteria, with “informal opinion gathering from senior leadership” a distant second choice. This same question was asked in last year’s survey regarding base pay practices. For base pay, respondents overwhelmingly chose employee retention as the primary effectiveness criterion. This shows that HR professionals are taking a balanced approach to compensation and using different compensation vehicles to meet different objectives. Base pay tends to be used to attract and retain talent and variable pay is typically used to reward performance.

Interviews with compensation managers supported these trends. Companies that were successful with variable pay attributed it to line of sight and communication. Mark Premock, general director of compensation at Burlington Northern Santa Fe, said during a personal interview on April 29, 2004, “We take extra time to get performance communication approved by the entire senior leadership team. That way, no matter how employees receive their information, it is always a consistent message.”

Compensation managers indicate that improving the “line-of-sight” and the linkage between payout and performance are the most important ways to improve the variable pay programs (See Figure 10). Despite these findings, a majority of organizations do not involve employees in the design of the variable pay program. This seems to be an obvious area for improvement. In focusing on line-of-sight issues, organizations are suggesting that they must do a better job of ensuring that their employees understand what they are being asked to do to earn their rewards, and that their individual goals are based on a realistic view of the future and connected to what the organization needs to succeed in the future.

Employees are typically motivated to provide additional discretionary effort in their jobs when they feel connected to the bigger picture and understand

In focusing on line-of-sight issues, organizations are suggesting that they must do a better job of ensuring that their employees understand what they are being asked to do to earn their rewards, and that their individual goals are based on a realistic view of the future and connected to what the organization needs to succeed in the future.

FIGURE 10 Areas for Improvement

How Variable Pay Programs Can Be Improved (Respondents asked to select three most important)	Percent Response
Improve plan “line of sight” to individual or team efforts	60%
Improve linkage between payout and performance	57%
Improve communication of plan objectives	48%
Increase understanding of the variable pay plan	33%
Improve ease of administration	23%
Increase payout opportunities	23%
Ensure goals are viewed as more attainable	22%
Reduce conflicting goals	9%

There were not many differentiating features in terms of plan design, but programs differ widely in terms of how they are executed — especially in the areas of communication, building line of sight and providing management with an important role in the design and implementation of these programs.

how their actions contribute. This is both a variable pay issue as well as a communication issue. Goals and measures will have little value if employees are unaware of how they are progressing toward the goal until they have either met or missed it.

Conclusions

In this research, we have seen that the prevalence and eligibility levels of variable pay programs are substantial and that compensation professionals view variable pay programs as instrumental in their reward strategy. The primary objectives of these programs tend to be squarely focused on improving organizational and

individual performance and improving the overall market competitiveness of pay. The majority of plans consist of group measures, but there is renewed focus on individual measures.

This study indicates that variable compensation for most managerial and professional employees is still administered under fairly traditional, time-tested methods such as individual bonuses, profit sharing, gain sharing and equity programs. Compensation professionals believe that these methods are generally effective, as is evident by their widespread use and positive responses regarding the perceived effectiveness of these programs. Designs for short-term or annual cash variable pay programs are generally given high ratings for effectiveness by the survey respondents, but program implementation is not viewed as favorably. Relatively low marks are given for the effectiveness of the compensation programs' motivational value and communication to employees. Although individual variable pay plans are rated highly, most plans have a group variable pay component. We have found in this research that there were not many differentiating features in terms of plan design, but that programs differ widely in terms of how they are executed — especially in the areas of communication, building line of sight and providing management with an important role in the design and implementation of these programs.

Compared to our previous study that examined base-pay issues, we found fewer connections between program design features and two measures of organizational effectiveness, i.e., TSR and designation as a Most Admired Company (according to *Fortune* magazine). We did find that the most admired companies were more likely to involve program eligible employees in the design of the variable pay program. Involvement not only builds commitment to the program, it may also improve program design and help employees better understand how the program works.

Compensation managers from most admired companies perceived their annual cash variable pay program as being more effective, especially as it related to the motivational value of the program and the relationship of variable compensation payouts to individual employee performance. Respondents from most admired companies also had more confidence that employees understood the program, which is consistent with their willingness to involve employees in the design of the program. The authors did not find any significant differences between variable pay program design features and TSR.

Thus, we conclude that annual bonuses for managerial and professional employees will continue to be an important component of their pay. However, program effectiveness is less an issue of having the "right" program features and more dependent on program implementation and communication. Therefore, companies that want to improve the effectiveness of their annual incentive programs should focus on helping employees understand the program and how their actions contribute to business results, and on building commitment for the program. 

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Authors

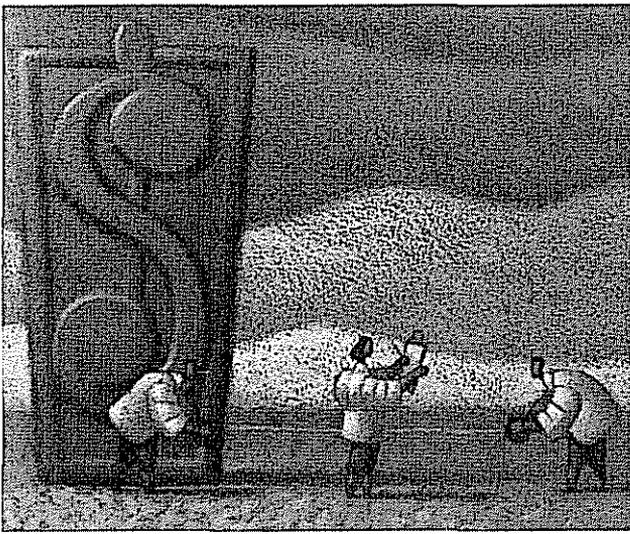
Dow Scott, Ph.D. (dscott@wpo.it.luc.edu) is a professor of HR in the School of Business Administration at Loyola University Chicago. His practical approaches to teaching, research and consulting focus on helping business leaders create more productive and satisfying work environments. He has been published in more than 100 journals, books and conference proceedings, and received national recognition for team/productivity improvement and HR research. Scott's research and consulting has focused on employee retention, creation of effective teams, performance improvement strategies, pay and incentive systems, evaluation of HR programs and the development of high-performance organizations.

Dennis Morajda, MSIR (dmorajd@earthlink.net) is vice president of Performance Development International, Inc., an HR consulting firm that specializes in working with organizations to build more satisfying and productive work environments. He has worked with clients in a variety of industries toward reducing employee turnover and absenteeism, assessing employee attitudes on pay, and improving organizational and safety cultures. He has extensive experience in designing employee attitude surveys, continuous improvement and performance evaluation systems.

Marc Wallace (marc_wallace@haygroup.com) is an experienced consultant in performance management and compensation. He has presented for several regional organizations as well as at the WorldatWork annual conference on multiple occasions and at national conferences on variable pay. As a consultant at Hay Group, Wallace works with organizations to develop strong rewards and performance management systems. Wallace holds a master's degree in international management from Thunderbird and a bachelor's degree in economics from the University of Wisconsin at Madison.

Thomas D. McMullen (tom_mcmullen@haygroup.com) is a senior consultant and Midwest Rewards practice leader in the Chicago office of Hay Management Consultants. He has over 20 years of combined HR practitioner and consulting experience. His work focuses primarily on total rewards and performance program design, including rewards strategy development, incentive plan design, employee pay and job evaluation.

Prior to joining Hay, McMullen was in senior compensation roles with Kentucky Fried Chicken Corp. and Humana Inc. He holds a master's degree in business administration and a bachelor's degree in mathematics from the University of Louisville.



Evaluating Pay Program Effectiveness: A National Survey of Compensation Professionals



Dow Scott, Ph.D.
Loyola University Chicago



Thomas D. McMullen
Hay Group



Richard S. Sperling
Hay Group

This paper is the second in a two-part examination of pay program evaluation. The first paper, "Evaluating Pay Program Effectiveness" (published last quarter in the *WorldatWork Journal*), suggested that using return on investment (ROI) to determine the value of pay programs has significant limitations. The authors proposed that comprehensive pay program evaluation should not only assess ROI but should also:

- ▶ Provide necessary feedback for improving pay program effectiveness, given the constant changes in the work and business environment
- ▶ Identify problems early in the pay program's rollout
- ▶ Build employee and management commitment to the pay program by engaging them in the evaluation and improvement process
- ▶ Hold management responsible for implementing the program as designed, and
- ▶ Communicate pay values, policies and programs to employees and managers

To accomplish these goals, a comprehensive two-dimensional framework for evaluating pay programs was proposed (adapted from the work of Donald Kirkpatrick 1998). The first dimension focuses on four evaluation perspectives that should be considered in the evaluation process:

- ▶ employee perception of the pay program
- ▶ their understanding of the pay program
- ▶ employee behaviors driven by the program and
- ▶ the impact the pay program has on results

Researchers widely use the second dimension in the process to collect and analyze data:

- 1 Setting goals or objectives
- 2 Identifying evaluation criteria
- 3 Selecting an evaluation methodology
- 4 Collecting and analyzing data
- 5 Interpreting findings and
- 6 Developing and implementing program improvement strategies.

This process ensures the information collected is of sufficient rigor to provide accurate insights on pay program value. This framework is explained in considerable detail in Part 1 of this series, published in the Second Quarter 2006 edition of the *WorldatWork Journal*.

This paper, Part 2 of the series, presents the findings from a national survey of compensation, human resources and finance professionals who identify current practices of how pay programs are evaluated within their organizations. To understand if a systematic and comprehensive evaluation process is used within organizations, the authors structured the survey to address the following questions:

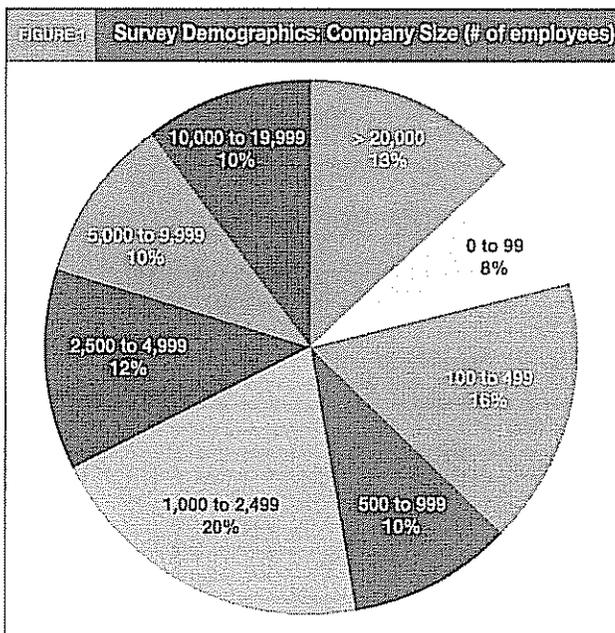
- ▶ To what extent do organizations evaluate pay program effectiveness?
- ▶ How is pay program effectiveness evaluated?
- ▶ Does pay program evaluation tend to be quantitative or qualitative, formal or informal?
- ▶ To what degree does pay program evaluation focus on financial versus human resources measures (e.g., turnover, absenteeism, attracting talent or motivation)?
- ▶ What impact, if any, does pay program evaluation have on organizational effectiveness?

Data Collection Methods and Respondent Characteristics

WorldatWork, Chicago Compensation Association members and registered Hay Group (a management consulting firm) Web site users were invited to participate in the research initiative in January 2006. The survey was open for a 30-day period, and the database was closed in February 2006. The survey required approximately 15 to 20 minutes to complete.

Of the more than 600 respondents participating in the study, 55 percent were compensation professionals, 27 percent were human resources managers and 18 percent held other managerial positions (e.g., primarily business-unit executives and finance professionals). Participating organizations were fairly evenly distributed by size. Approximately one-third of organizations had fewer than 1,000 employees, one-third had between 1,000 and 5,000 employees and one-third had greater than 5,000 employees (See Figure 1 on page 48). Only 8 percent of the sample reported representing organizations with fewer than 100 employees.

Figure 2 on page 49 shows the sample included respondents from a diverse range of industries. The



Because of rounding, this figure totals 99 percent.

FIGURE 2 Survey Demographics: Industry Sector	
INDUSTRY SECTOR	%
Manufacturing	16
Finance and Insurance	15
Health Care, Social Assistance	11
Professional, Scientific, Technical Services	8
Public Administration	6
Educational Services	6
Retail Trade	4
Utilities	3
Information (Publishing, Electronic, Print, IT)	3
Transport and Warehousing	3
Wholesale Trade	2
Other Services (Except Public Administration)	2
Real Estate and Construction	2
Other	20

Due to rounding, this figure totals more than 100 percent

largest representation were from manufacturing (16 percent); finance and insurance (15 percent); health care and social assistance (11 percent); and professional, scientific and technical services (8 percent)

While the Most Admired analysis uses a balanced set of rating attributes covering both financial and nonfinancial criteria, it is important to note that Most Admired Companies outperform the market as a whole.

Respondents were excluded from the analysis if more than one manager responded for a single organization (the highest-ranking manager was retained) or if the organization reported it had fewer than 10 employees.

To examine the impact pay program evaluation may have on organizational effectiveness, companies identified by *Fortune* magazine as a “Most Admired Company” were compared to respondents with the same range in employee size. The *Fortune* “Most Admired Companies” survey is a highly regarded annual analysis of corporate reputations. The Hay Group conducts the survey for *Fortune*. More than 10,000 executives, directors and industry analysts are involved in developing these overall rankings. The survey invites these respondents to rate companies, overall and within industry groupings, on nine criteria ranging from financial soundness and use of corporate assets to quality of management and quality of products and services. While the Most Admired analysis uses a balanced set of rating attributes covering both financial and nonfinancial criteria, it is important to note that Most Admired Companies outperform the market as a whole. In 2006, the top 10 Most Admired Companies delivered a five-year average total shareholder return of 11.1 percent, compared to -2.7 percent for the S&P 500.

Research Findings

In response to the question “Does your company evaluate the effectiveness of its pay program?” 66 percent responded “yes” for base pay programs and 53 percent responded “yes” for variable pay programs. From the total sample, 47 percent of the companies evaluate their base and variable pay programs. However, there was a significant difference in evaluation prevalence for the Most Admired Companies, with 81 percent of these organizations evaluating base and variable pay program effectiveness as compared to 51 percent of comparably sized companies (5,000 employees or more) that did not receive this designation.

The information reported in Figure 3 through Figure 8 (pages 50-52) is only for those organizations that reported they evaluated their pay programs. Figure 3 shows the level at which pay programs are evaluated and the importance associated with that information, collected for evaluation purposes. For base and variable pay programs, overall company or organization level was the most common point where pay program evaluation occurred; 87 percent and 76 percent for base pay and variable pay programs, respectively. Evaluation at either the department, work unit or team level was less prevalent for both base and variable pay. Although individual scores were not significantly different, companies with the "Most Admired" designation indicated that overall, they were more likely to evaluate base and variable pay programs at the organization and business-unit levels.

For those organizations where pay programs are evaluated, this paper's findings showed considerable variations in the depth and rigor of the analysis (See Figure 4). Few organizations report that they seldom, if ever, evaluate their pay programs after the programs are implemented for base and variable pay (10 percent and 7 percent, respectively). Whereas at the other extreme, 27 percent of respondents indicated that their organizations evaluate base pay and 38 percent said they evaluate their variable pay programs by

calculating both the cost and their bottom-line impacts. The most common practice for organizations is to calculate the costs associated with the compensation program and to informally discuss the impacts on bottom-line performance.

Companies were more likely to calculate the cost and at least discuss the bottom-line impact on variable pay programs than for base pay programs. This finding is consistent with the authors' beliefs that variable pay programs, by their very nature, are easier to evaluate.

Figure 5 on page 51 summarizes the criteria used to evaluate both base and variable pay programs. The most often used criteria for base pay programs are "attracting new employees or time to fill open positions" and "impact on employee retention or turnover." Whereas, the most widely used criteria for variable pay are "impact on revenues, profits and net worth" and "impact on productivity or cost savings." Given the significantly different nature and objectives of the base and variable pay programs, it is not surprising that different criteria are used to evaluate these programs.

Figure 6 reports the perspective used to evaluate base and variable pay programs. For all participants, informal feedback from both employees and managers are heavily used information sources. Formal employee feedback is relied upon for more than one-half of the

FIGURE 3 Pay Program Evaluation Levels				
	Prevalence		Importance	
	Base Pay	Variable Pay	Base Pay	Variable Pay
Company or Organization Level	87%	76%	60%	56%
Business Unit or Division Level	45%	50%	23%	31%
Department Level	33%	27%	11%	9%
Work Unit or Team Level	16%	14%	6%	4%

FIGURE 4 Depth of Pay Program Evaluation		
	Base Pay	Variable Pay
Seldom, if ever, evaluate after implementation	10%	7%
Calculate costs, but do not try to determine value/contribution	24%	12%
Calculate costs and discuss their impact on bottom line	39%	43%
Calculate costs and bottom-line impacts	27%	38%

respondents for both base and variable pay. More than two-thirds of the respondents indicated that results or outcomes attributed to base pay, were used to evaluate base pay and 88 percent said the same was used for variable pay programs. These data indicated that 80 percent calculated the ROI for variable pay programs, whereas a lower percentage of organizations (34 percent) calculate the ROI for base pay programs. Companies designated as "Most Admired" were more likely to engage in a comprehensive evaluation approach that included employee understanding, behavior change and results to evaluate pay programs, especially for base pay programs.

Figure 7 shows that the evaluation processes

(i.e., research methodology) used by most organizations are weak and largely informal. The most-powerful evaluation methods are seldom used. Less than one-third of the organizations even attempt to evaluate pay programs, and less than one-sixth compare pay program effectiveness with a nonparticipating employee group. However, as one might expect, "Most Admired" companies are more likely to use rigorous methods for evaluating pay programs.

Figure 8 on page 52 indicates that respondents strongly agree that more needs to be done to develop methods that accurately assess the contribution pay makes to the bottom line and to calculate ROI. Ninety

FIGURE 6: Criteria Used to Evaluate Pay Programs		
	Base Pay	Variable Pay
Impact on revenues, profits, net worth	80%	90%
Impact on productivity or cost savings	72%	83%
Impact on quality waste or rework time	53%	61%
Impact on employee retention or turnover	84%	79%
Impact on employee satisfaction/engagement	78%	82%
Attracting new employees or time to fill open positions	86%	66%
Impact on overtime or other labor expenses	54%	41%
Qualification of recruits or applicant pool	74%	40%
Other qualitative measures (e.g., capability, competency)	67%	68%

FIGURE 8: Pay Program Evaluation Perspective				
	All Participants		Most Admireds	
	Base Pay	Variable Pay	Base Pay	Variable Pay
Informal feedback from participating employees	39%	55%	60%	53%
Informal feedback from supervisors or managers	64%	71%	70%	50%
Formal feedback from participating employees	55%	79%	73%	79%
Level of employee understanding of program	47%	79%	69%	80%
Behavior change of participating employees	55%	N/A	84%	N/A
Results or outcomes attributed to pay program	67%	88%	93%	100%
ROI	34%	80%	70%	80%

FIGURE 7: Pay Program Evaluation Method				
	All Participants		Most Admireds	
	Base Pay	Variable Pay	Base Pay	Variable Pay
Informally evaluate the pay program (no quantitative information is used)	52%	49%	70%	70%
Compare pay program criteria before and after program implementation	35%	47%	45%	75%
Compare pay program effectiveness with a nonparticipating employee group	16%	14%	15%	15%
Examine pay effectiveness measures over time	29%	30%	40%	50%

FIGURE 3 Pay Program Evaluation Improvement		
	Base Pay	Variable Pay
Nothing needs to be done	20%	21%
Develop systems to provide capability to evaluate pay effectiveness	92%	93%
Develop better qualitative measures (e.g., capability, competency)	80%	73%
More accurately assess the cost of pay	73%	77%
Develop methods to accurately assess contribution pay makes to bottom line	80%	93%
Develop methods to accurately assess cost and contribution of pay effectiveness	93%	91%
Calculate ROI of pay programs	88%	92%
Engage management to realize importance of base pay evaluation	91%	90%

percent of respondents said that they need to help management realize the importance of pay program evaluation

Conclusions and Recommendations

Most organizations evaluate their pay program using a variety of methodologies, however, informal processes are still the most common approach. "Most Admired" companies are more likely to evaluate pay programs and to use more objective and formal methods for doing so. Much remains to be done if the reader accepts the thesis that information from comprehensively designed pay program evaluation can substantially improve the quality and effectiveness of pay programs. The majority of organizations do not evaluate their base and variable pay programs, and only about one-third of organizations calculate the cost and bottom line impact of their pay programs. Less than one-half of the companies attempt to evaluate their pay programs pre- and post-implementation. Even fewer attempt more rigorous comparative or time-series analysis.

One important "qualitative" insight is the divide in thinking of human resources and compensation professionals about pay program evaluation. On one side of the divide are those who tend to view pay programs as a cost of doing business. Professionals holding this belief tend to have an orientation on focusing their evaluation efforts on cost control and benchmarking. On the other side are compensation and human resources professionals who view pay programs

as an *investment* and are concerned about optimizing the return on this investment. As a result, they are more likely to be proactive in determining how employees, especially high performers, perceive their pay program. Furthermore, those that see pay programs as an investment want to ensure their employees understand the pay program's purpose and design, and they are interested in how the pay program shapes employee behavior.

To obtain senior management legitimacy and to enhance the impact of the pay program, the authors recommend that an organization follow a systematic and comprehensive process for evaluating pay programs, as suggested in "Evaluating Pay Program Effectiveness." Given the substantial investment made in pay programs and the program's impact on organizational effectiveness, comprehensive pay program evaluation only makes good business sense. When management desires to know why the pay program did not meet expectations, compensation professionals must be prepared with answers and, more importantly, must be able to make suggestions as to how these pay programs can be improved. More specifically, pay program evaluation must use multiple perspectives and rigorous analytical methods including the following:

- ▶ Use formal employee opinion surveys or focus groups to determine how eligible employees and the managers to whom they report feel about the pay program (e.g., fair, equitable and competently administered)
- ▶ Test eligible employees' and manager understanding of the pay program

- ▶ Monitor the influence of the pay program on employee behavior since changes in behavior drive expected performance and pay.
- ▶ Assess the results that the pay program is expected to impact (e.g., retention and performance).
- ▶ Calculate the ROI; program costs and value added.
- ▶ Use rigorous research methods to analyze data from each perspective.

Although evaluation methods and use of multiple perspectives may be new for many compensation professionals, human resources development and training professionals have considerable expertise in this area. Furthermore, most HR development professionals routinely develop e-learning programs that can be used to effectively communicate the intent and substance of pay programs. Thus, pay program evaluation provides an excellent opportunity to begin working with human resources development to educate employees about compensation and evaluate the impact of these programs. The earlier paper in this series provides specific strategies as to how to comprehensively evaluate pay programs. 

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Authors

Dow Scott, Ph.D., is a professor of human resources at Loyola University, Chicago, and president of Performance Development International Inc. Scott is a nationally recognized compensation and human resources program evaluation expert, with more than 100 publications. His teaching, research and consulting have focused on the creation of effective teams, employee opinion surveys, performance improvement strategies, pay and incentive systems and the development of high-performance organizations.

Thomas D. McMullen is the U.S. Reward Practice leader for Hay Group based in Chicago. He has more than 20 years of combined HR practitioner and compensation consulting experience. His work focuses primarily on total rewards and performance program design, including rewards strategy development and incentive plan design. Prior to joining Hay Group, McMullen worked for Humana Inc. and Kentucky Fried Chicken Corp. in senior compensation analyst roles. He earned bachelor of science and master of business administration degrees from the University of Louisville. (He can be reached at tom_mcmullen@haygroup.com).

Richard S. Sperling, CCP, is a senior consultant in the Chicago office of Hay Group. He works with clients to design and value jobs, build effective organization structures, and develop and implement reward systems. He has designed leading-edge approaches to analyzing, understanding, designing and valuing work in clients' increasingly complex and varied organizational settings. Sperling can be reached at richard_sperling@haygroup.com.

Prior to joining Hay Group in 1981, Sperling worked for Ford Motor Co. in a variety of human resources positions. He earned a bachelor of science degree from Yale University and a master of management degree from Northwestern University.

The authors would like to thank Dennis Morajda, Performance Development International Inc., for his help in structuring the survey and analyzing the data.

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KENTUCKY-AMERICAN WATER COMPANY
CASE NO. 2007-00143
COMMISSION STAFF'S THIRD
SET OF INFORMATION REQUESTS
Item 4 of 54

Witness: Michael A. Miller

4. State whether Kentucky-American capitalized any portion of its incentive pay plan. Explain.

Response:

No.

For electronic version, refer to KAW_R_PSCDR3#4_071607.pdf

**KENTUCKY-AMERICAN WATER COMPANY
CASE NO. 2007-00143**

**COMMISSION STAFF'S THIRD
SET OF INFORMATION REQUESTS
Item 5 of 54**

Witness: Sheila Miller

5. Describe how Kentucky-American determines its forecast capitalization rate. If an historical rate is used, describe how Kentucky-American determines the historical rate.

Response:

The forecasted labor in the rate filing was used to calculate the forecast capitalization rate. The forecasted capital labor of \$1,353,403 was divided by total labor of \$7,349,916 to arrive at a capitalization rate of 18.41% (see revised filing).

For electronic version, refer to KAW_R_PSCDR3#5_071607.pdf

KENTUCKY-AMERICAN WATER COMPANY
CASE NO. 2007-00143
COMMISSION STAFF'S THIRD
SET OF INFORMATION REQUESTS
Item 6 of 54

Witness: Nick Rowe/Michael Miller/Sheila Miller

6. Refer to Kentucky-American's Response to Commission Staff's Second Set of Information Requests, Item 9.
- a. Provide the basis for the 3.5 percent pay increase to union and non-union employees.
 - b. State when the pay rates effective for the forecasted period will be approved.
 - c. Provide a comparison of projected pay rates used in Kentucky-American's budgeting process to those actually awarded to union and non-union employees over the previous 10 years.

Response:

- a. The basis for the 3.5% pay increase for union and non-union employees is management's judgment considering current economic conditions and recent historical pay increases.
- b. For non-union employees, the new pay rates should be approved in March 2008 to be effective April 1, 2008. Both union contracts are open for renegotiation in 2007. The current inside union contract is a 3-year contract with the most recent wage increase effective 12/17/06. New pay rates under this contract and subject to this filing should be effective 12/17/07. The current outside union contract is a 3-year contract with the most recent wage increase effective 11/1/06. New pay rates under this contract and subject to this filing will be effective 11/1/07 and 11/1/08.
- c.

Year	Non-union		Inside union		Outside union	
	Actual	Budget	Actual	Budget	Actual	Budget
1997	3.6%/3.0%**	3.00%	2.50%	2.50%	2.50%	2.50%
1998	4.50%	3.00%	2.50%	2.50%	2.50%	2.50%
1999	4.50%	4.00%	2.50%	2.50%	2.50%	2.50%
2000	4.50%	4.00%	2.50%	2.50%	2.50%	2.50%
2001	3.68%	4.50%	3.00%	2.50%	3.00%	2.50%
2002	3.80%	3.50%	3.00%	3.00%	3.00%	3.00%
2003	3.53%	3.0%/3.5%***	3.00%	3.50%	2.50%	3.50%
2004	2.88%	3.00%	3.00%	3.00%	3.00%	3.00%
2005	3.50%	3.00%	3.00%	3.00%	4.00%*	4.00%
2006	3.50%	4.2%/3.5%****	3.00%	3.00%	4.00%*	4.00%

*3% plus 25 cent wage adjustment

** 3.6% for salaried employees/3.0% for non-union employees

***3.0% for salaried employees/3.5% for non-union employees

****4.2% for salaried employees/3.5% for non-union employees

KENTUCKY-AMERICAN WATER COMPANY
CASE NO. 2007-00143
COMMISSION STAFF'S THIRD
SET OF INFORMATION REQUESTS
Item 7 of 54

Witness: Linda Bridwell/Sheila Miller

7. Refer to Kentucky-American's Response to Commission Staff's Second Set of Information Requests, Item 14(a).
 - a. Describe how the replacement intake pumps were "factored into the higher kwh/mg values in the 2008 budget for KRS."
 - b. Define "higher kwh/mg values" as used in the Response.
 - c. Relate the historic five-year information to the forecasted KWH/MG included at W/P 3, pages 45 through 52, showing the effect of the replacement pumps separately.

Response:

- a. This applies only to the Kentucky River Station. The six old intake pumps at the Kentucky River Station would produce about 11 MGD each. The six new intake pumps at the Kentucky River Station are rated at 14.4 MGD, or an increase of about 30%. However, the motors driving these pumps are staying the same. In order to drive the new pumps, these motors will have to work harder requiring more electricity. The annual average KWH/MG was increased by 5.5% in the 2008 budget over the 2006 historical average KWH/MG.
- b. "Higher kwh/mg values" refers to the increase of 5.5% noted above.
- c. As shown in the exhibit, the kwh/mg can vary up or down based upon the system demand, weather, pump usage and maintenance considerations. The budgeted kwh/mg is taken from looking at the historical data and using our best operational knowledge of any known and measurable changes to arrive at the appropriate kwh/mg values to budget. This modest increase was put in place to capture the cost increases from the installation of these pumps.

For electronic version, please refer to KAW_R_PSCDR3#7_071607.pdf

**KENTUCKY-AMERICAN WATER COMPANY
CASE NO. 2007-00143**

**COMMISSION STAFF'S THIRD
SET OF INFORMATION REQUESTS
Item 8 of 54**

Witness: Sheila Miller

8. Refer to Kentucky-American's Response to Commission Staff's Second Set of Information Requests, Item 16. State whether any of the listed Owen Electric Cooperative, Inc. or Kentucky Utilities Company accounts involve the purchase of electricity for any of Owenton's wastewater facilities.

Response:

No.

For electronic version, refer to KAW_R_PSCDR3#8_071607.pdf

KENTUCKY-AMERICAN WATER COMPANY
CASE NO. 2007-00143
COMMISSION STAFF'S THIRD
SET OF INFORMATION REQUESTS
Item 9 of 54

Witness: Sheila Miller

9. Refer to Kentucky-American's Response to Commission Staff's First Set of Information Requests, Item 1(a), W/P 3, pages 56 through 63 of 118.
- a. State whether Kentucky-American incurs any chemical expenses for the operations of the Owenton Sewer Facility.
 - b. If yes, explain why no separate entry for the Owenton Sewer Facility's chemical expenses appears on these pages, while a separate entry is made for the Boonesboro Sewer Facility.¹
 - c. State whether pages 56 through 63 contain any entries related to chemical expenses for the Owenton Sewer Facility.

Response:

- a. Yes.
- b. The Owenton Sewer chemical expenses were inadvertently omitted. However, the Company is not seeking any recovery of sewer expenses in the rate filing.
- c. No.

For electronic version, refer to KAW_R_PSCDR3#9_071607.pdf

¹ See W/P 3, page 63 of 118 ("Boonesboro Sewer").

KENTUCKY-AMERICAN WATER COMPANY
CASE NO. 2007-00143
COMMISSION STAFF'S THIRD
SET OF INFORMATION REQUESTS
Item 10 of 54

Witness: Linda C. Bridwell/Sheila Miller

10. Refer to Kentucky-American's Response to Commission Staff's Second Set of Information Requests, Item 20.
- a. Kentucky-American includes in its forecasted operations the second year of the two-year amortization of the Kentucky River Station sludge lagoon cleaning, which it performed in December 2006. Considering that the prior cleaning was performed in November 2001, explain why a two-year amortization period for the 2006 cleaning costs is more appropriate than a five-year amortization period.
 - b. State whether the unamortized balance of the Kentucky River sludge lagoon cleaning is included in the forecasted 13-month average balance of deferred maintenance included in Kentucky-American's proposed rate base.
 - c. Explain why Kentucky-American does not amortize the cost of cleaning the Richmond Road Station's Lake Ellerslie and sedimentation basins.
 - d. State the date when the Richmond Road Station's Lake Ellerslie and sedimentation basins will be cleaned next.

Response:

- a. The response to Item 20 omitted a 2004 cleaning of the Kentucky River Station lagoons for \$178,065, amortized over two years and a 2004 cleaning of the Lake Ellerslie for \$75,769, which was not amortized. The KRS sludge lagoons require cleaning every two years.
- b. No it was not included.
- c. Kentucky-American had planned for annual cleaning due to the significant amount of build up expected, but annual cleaning has not occurred. Kentucky-American is now accruing for this cleaning and will true the accrual up to actual when the cleaning occurs.
- d. September 2007.

For electronic version, refer to KAW_R_PSCDR3#10_071607

KENTUCKY-AMERICAN WATER COMPANY
CASE NO. 2007-00143
COMMISSION STAFF'S THIRD
SET OF INFORMATION REQUESTS
Item 11 of 54

Witness: Linda C. Bridwell

11. Refer to Kentucky-American's Response to Commission Staff's First Set of Information Requests, Item 1(a), W/P 3, page 66 of 118. Provide the basis for:
- a. The 2007 Cleaning Richmond Road Station costs of \$55,000.
 - b. Kentucky River Station Waste Disposal Current.
 - c. Richmond Road Station Waste Disposal Current.

Response:

- a. For the Lake Ellerslie (Richmond Road Station), the Company is now accruing expenses according to a new company policy and has \$158,000 accrued toward a September 2007 cleaning. The last cleaning was in 2004. We are continuing to accrue for the next cleaning at approximately the same rate.
- b. Historical averages of chemical, power and labor costs increased for known increases in price.
- c. Historical averages of chemical, power and labor costs increased for known increases in price.

For electronic version, refer to KAW_R_PSCDR3#11_071607.pdf

KENTUCKY-AMERICAN WATER COMPANY
CASE NO. 2007-00143
COMMISSION STAFF'S THIRD
SET OF INFORMATION REQUESTS
Item 12 of 54

Witness: Michael Miller

12. In its Response to Commission Staff's Second Set of Information Requests, Item 22(c), Kentucky-American states that business development costs of \$79,365 are included in requested forecasted management fees. In Case No. 2004-00103, the Commission denied management fee business development costs of \$117,525 because Kentucky-American could not "appropriately document and separate forecasted management fees between those that are directly assignable and those that are allocated."¹
- a. List and describe the forecasted management fees that are directly assignable to Kentucky-American. Provide supporting invoices for these fees.
 - b. Explain why, if Kentucky-American cannot document and separate forecasted management fees between those that are directly assignable and those that are allocated, it is reasonable and appropriate to include these fees in Kentucky-American's rates.

Response:

- a. See the attached schedules for a breakdown of the forecasted test-year Business Development costs. In the response to PSCDR2#22(c) referenced above, the forecasted test-year level was determined on a overall percentage basis using the 2006 ratio charged to Kentucky American Water. The attached schedule utilizes the 2006 hours by department and the result is within \$441.34 of the original calculation. No invoices are available for the budgeted numbers, but the schedules indicate labor, employee benefits and general overheads that make up the plan numbers.
- b. The attached schedule provides the breakdown between allocated and direct costs.

For electronic version, refer to KAW_R_PSCDR3#12_071607.pdf.

¹ Case No. 2004-00103, Order of February 28, 2005 at 52-53.

Kentucky American Water
Business Development Costs Forecasted Test Year

Business Unit	Description	Type of Allocation	Hr Rate	Hours	dollars	labor benefit	burdened total	general benefit rate	grand burden total	Total	
January	035020	SE-Business Development	Regional Allocation	\$39.51	4.60	\$181.76	26.38%	\$229.70	28.35%	\$233.28	
	035020	SE-Business Development	Regional Allocation	\$57.47	3.68	\$211.49	26.38%	\$267.29	28.35%	\$271.45	
	035020	SE-Business Development	Regional Allocation	\$55.08	3.45	\$190.02	26.38%	\$240.14	28.35%	\$243.89	
	035020	SE-Business Development	Regional Allocation	\$20.82	11.04	\$229.84	26.38%	\$290.47	28.35%	\$295.00	
	035020	SE-Business Development	Direct Charge	\$50.05	8.00	\$400.38	26.38%	\$506.00	28.35%	\$513.89	
	035020	SE-Business Development	Regional Allocation	\$50.05	7.22	\$361.44	26.38%	\$466.79	28.35%	\$463.91	
	035020	SE-Business Development	Regional Allocation	\$43.10	3.68	\$158.62	26.38%	\$200.47	28.35%	\$203.59	
	035020	SE-Business Development	Regional Allocation	\$39.51	4.05	\$159.95	26.38%	\$202.14	28.35%	\$205.29	
	035020	SE-Business Development	Regional Allocation	\$71.84	11.04	\$793.10	26.38%	\$1,002.32	28.35%	\$1,017.94	
	035020	SE-Business Development	Direct Charge	\$59.87	1.00	\$59.87	26.38%	\$75.66	28.35%	\$76.84	
	035020	SE-Business Development	Regional Allocation	\$59.87	3.96	\$236.83	26.38%	\$299.31	28.35%	\$303.97	
	035020	SE-Business Development	Regional Allocation	\$59.87	4.78	\$286.40	26.38%	\$361.95	28.35%	\$367.59	
	035020	SE-Business Development	Regional Allocation	\$52.68	7.36	\$387.74	26.38%	\$490.03	28.35%	\$497.67	
	035020	SE-Business Development	Regional Allocation	\$17.79	7.36	\$130.92	26.38%	\$165.45	28.35%	\$168.03	
	036520	NE-Business Development	Regional Allocation	\$47.52	0.46	\$21.86	26.38%	\$27.63	28.35%	\$28.06	
	February	035020	SE-Business Development	Regional Allocation	\$45.50	0.92	\$41.86	48.03%	\$61.86	40.41%	\$68.77
035020		SE-Business Development	Regional Allocation	\$57.47	0.37	\$21.15	48.03%	\$31.31	40.41%	\$29.70	
035020		SE-Business Development	Regional Allocation	\$55.08	0.18	\$10.13	48.03%	\$15.00	40.41%	\$14.23	
035020		SE-Business Development	Regional Allocation	\$20.82	7.36	\$153.23	48.03%	\$226.82	40.41%	\$215.14	
035020		SE-Business Development	Direct Charge	\$50.05	8.00	\$400.38	48.03%	\$592.68	40.41%	\$562.17	
035020		SE-Business Development	Regional Allocation	\$50.05	1.93	\$96.69	48.03%	\$143.13	40.41%	\$135.77	
035020		SE-Business Development	Regional Allocation	\$43.10	2.58	\$111.04	48.03%	\$164.37	40.41%	\$155.90	
035020		SE-Business Development	Regional Allocation	\$71.84	6.72	\$482.47	48.03%	\$714.20	40.41%	\$677.43	
035020		SE-Business Development	Regional Allocation	\$59.87	1.56	\$93.63	48.03%	\$138.60	40.41%	\$131.47	
035020		SE-Business Development	Regional Allocation	\$59.87	10.24	\$613.15	48.03%	\$907.64	40.41%	\$860.92	
035020		SE-Business Development	Regional Allocation	\$52.68	0.74	\$36.77	48.03%	\$57.40	40.41%	\$54.44	
035020		SE-Business Development	Regional Allocation	\$17.79	3.68	\$65.46	48.03%	\$96.90	40.41%	\$91.91	
035020		SE-Business Development	Regional Allocation	\$47.52	0.60	\$28.42	48.03%	\$42.07	40.41%	\$39.90	
March		035020	SE-Business Development	Regional Allocation	\$45.50	1.70	\$77.44	39.68%	\$108.17	28.52%	\$99.52
		035020	SE-Business Development	Regional Allocation	\$20.82	7.36	\$153.23	39.68%	\$214.03	28.52%	\$196.93
		035020	SE-Business Development	Regional Allocation	\$50.05	0.64	\$32.23	39.68%	\$45.02	28.52%	\$41.42
	035020	SE-Business Development	Regional Allocation	\$39.51	0.74	\$29.08	39.68%	\$40.62	28.52%	\$37.38	
	035020	SE-Business Development	Regional Allocation	\$71.84	5.03	\$361.49	39.68%	\$504.94	28.52%	\$464.59	
	035020	SE-Business Development	Direct Charge	\$59.87	10.00	\$598.66	39.68%	\$836.21	28.52%	\$769.40	
	035020	SE-Business Development	Regional Allocation	\$59.87	1.66	\$99.14	39.68%	\$138.48	28.52%	\$127.41	
	035020	SE-Business Development	Regional Allocation	\$59.87	0.55	\$33.05	39.68%	\$46.16	28.52%	\$42.47	
	036520	NE-Business Development	Regional Allocation	\$47.52	0.25	\$12.02	39.68%	\$16.79	28.52%	\$15.45	
	April	032096	CORP-Chief Growth Officer	National Allocation	\$55.08	1.39	\$76.67	39.27%	\$106.78	34.35%	\$103.00
		032096	CORP-Chief Growth Officer	National Allocation	\$57.79	1.39	\$80.44	39.27%	\$112.03	34.35%	\$108.07
		035020	SE-Business Development	Regional Allocation	\$45.67	0.37	\$16.81	39.27%	\$23.41	34.35%	\$22.58
		035020	SE-Business Development	Regional Allocation	\$60.58	0.37	\$22.29	39.27%	\$31.05	34.35%	\$29.95
		035020	SE-Business Development	Regional Allocation	\$57.47	0.74	\$42.30	39.27%	\$68.91	34.35%	\$66.83
		035020	SE-Business Development	Regional Allocation	\$20.82	3.68	\$76.61	39.27%	\$106.70	34.35%	\$102.93
		035020	SE-Business Development	Regional Allocation	\$21.84	3.68	\$80.36	39.27%	\$111.92	34.35%	\$107.97
035020		SE-Business Development	Regional Allocation	\$55.26	0.09	\$5.08	39.27%	\$7.08	34.35%	\$6.83	
035020		SE-Business Development	Regional Allocation	\$50.05	0.78	\$39.14	39.27%	\$54.51	34.35%	\$52.58	
035020		SE-Business Development	Regional Allocation	\$41.44	0.37	\$15.25	39.27%	\$21.24	34.35%	\$20.49	

Kentucky American Water
Business Development Costs Forecasted Test Year

Business Unit	Description	Type of Allocation	Hr Rate	Hours	dollars	labor benefit	burdened total	general benefit rate	grand burden total	Total
035020	SE-Business Development	Regional Allocation	\$71.84	2.94	\$211.49	39.27%	\$294.55	34.35%	\$284.14	\$299.50
035020	SE-Business Development	Regional Allocation	\$75.72	2.94	\$222.92	39.27%	\$310.47	34.35%	\$299.50	\$310.47
035020	SE-Business Development	Regional Allocation	\$60.70	1.01	\$61.43	39.27%	\$85.55	34.35%	\$62.53	\$85.55
035020	SE-Business Development	Regional Allocation	\$59.87	0.60	\$35.80	39.27%	\$49.86	34.35%	\$48.10	\$49.86
035020	SE-Business Development	Regional Allocation	\$61.61	1.47	\$90.69	39.27%	\$126.31	34.35%	\$121.84	\$126.31
035020	SE-Business Development	Regional Allocation	\$52.68	0.74	\$38.77	39.27%	\$54.00	34.35%	\$52.09	\$54.00
036520	NE-Business Development	Regional Allocation	\$47.70	0.09	\$4.39	39.27%	\$6.11	34.35%	\$5.90	\$6.11
036520	NE-Business Development	Regional Allocation	\$47.52	0.37	\$17.49	39.27%	\$24.35	34.35%	\$23.49	\$24.35
032096	CORP-Chief Growth Officer	National Allocation	\$57.79	8.35	\$482.64	59.29%	\$768.80	59.77%	\$771.12	\$768.80
035020	SE-Business Development	Regional Allocation	\$45.67	0.92	\$42.02	59.29%	\$66.93	59.77%	\$67.13	\$66.93
035020	SE-Business Development	Regional Allocation	\$60.58	0.37	\$22.29	59.29%	\$35.51	59.77%	\$35.62	\$35.51
035020	SE-Business Development	Regional Allocation	\$21.84	11.04	\$241.09	59.29%	\$384.03	59.77%	\$385.18	\$384.03
035020	SE-Business Development	Regional Allocation	\$55.26	3.13	\$172.86	59.29%	\$275.36	59.77%	\$276.19	\$275.36
035020	SE-Business Development	Regional Allocation	\$41.44	0.55	\$22.88	59.29%	\$36.44	59.77%	\$36.55	\$36.44
035020	SE-Business Development	Regional Allocation	\$75.72	9.94	\$752.37	59.29%	\$1,198.44	59.77%	\$1,202.05	\$1,198.44
035020	SE-Business Development	Regional Allocation	\$60.70	2.25	\$136.81	59.29%	\$217.93	59.77%	\$218.58	\$217.93
035020	SE-Business Development	Regional Allocation	\$61.61	1.66	\$102.03	59.29%	\$162.52	59.77%	\$163.01	\$162.52
036520	NE-Business Development	Regional Allocation	\$47.70	0.60	\$28.53	59.29%	\$45.44	59.77%	\$45.58	\$45.44
036520	NE-Business Development	Regional Allocation	\$47.70	1.33	\$63.64	59.29%	\$101.36	59.77%	\$101.67	\$101.36
035020	SE-Business Development	Regional Allocation	\$45.67	1.79	\$81.94	14.17%	\$93.55	24.71%	\$102.18	\$93.55
035020	SE-Business Development	Regional Allocation	\$60.58	0.86	\$52.10	14.17%	\$69.48	24.71%	\$64.97	\$69.48
035020	SE-Business Development	Regional Allocation	\$21.84	7.36	\$160.72	14.17%	\$183.50	24.71%	\$200.44	\$183.50
035020	SE-Business Development	Direct Charge	\$55.26	1.00	\$55.26	14.17%	\$63.09	24.71%	\$68.91	\$63.09
035020	SE-Business Development	Regional Allocation	\$55.26	0.92	\$50.84	14.17%	\$58.05	24.71%	\$63.41	\$58.05
035020	SE-Business Development	Regional Allocation	\$41.44	2.99	\$123.91	14.17%	\$141.47	24.71%	\$154.53	\$141.47
035020	SE-Business Development	Regional Allocation	\$75.72	7.18	\$543.38	14.17%	\$620.37	24.71%	\$677.64	\$620.37
035020	SE-Business Development	Regional Allocation	\$60.70	1.47	\$89.33	14.17%	\$102.01	24.71%	\$111.42	\$102.01
035020	SE-Business Development	Regional Allocation	\$61.61	0.37	\$22.67	14.17%	\$25.89	24.71%	\$28.28	\$25.89
035020	SE-Business Development	Regional Allocation	\$52.89	2.58	\$136.23	14.17%	\$155.54	24.71%	\$169.89	\$155.54
036520	NE-Business Development	Regional Allocation	\$47.70	3.01	\$143.73	14.17%	\$164.09	24.71%	\$179.24	\$164.09
035020	SE-Business Development	Regional Allocation	\$45.67	1.56	\$71.43	39.33%	\$99.53	49.53%	\$106.81	\$99.53
035020	SE-Business Development	Regional Allocation	\$60.58	3.31	\$200.63	39.33%	\$279.54	49.53%	\$300.01	\$279.54
035020	SE-Business Development	Regional Allocation	\$21.84	7.36	\$160.72	39.33%	\$223.94	49.53%	\$240.33	\$223.94
035020	SE-Business Development	Direct Charge	\$55.26	2.00	\$110.52	39.33%	\$153.99	49.53%	\$165.26	\$153.99
035020	SE-Business Development	Regional Allocation	\$55.26	3.40	\$188.12	39.33%	\$262.10	49.53%	\$281.29	\$262.10
035020	SE-Business Development	Regional Allocation	\$41.44	1.10	\$45.75	39.33%	\$63.75	49.53%	\$68.41	\$63.75
035020	SE-Business Development	Regional Allocation	\$75.72	6.62	\$501.58	39.33%	\$698.85	49.53%	\$750.01	\$698.85
035020	SE-Business Development	Direct Charge	\$60.70	1.00	\$60.70	39.33%	\$84.57	49.53%	\$90.76	\$84.57
035020	SE-Business Development	Regional Allocation	\$60.70	2.16	\$131.23	39.33%	\$182.84	49.53%	\$196.22	\$182.84
035020	SE-Business Development	Regional Allocation	\$61.61	2.94	\$181.38	39.33%	\$252.72	49.53%	\$271.22	\$252.72
035020	SE-Business Development	Regional Allocation	\$52.89	3.86	\$204.35	39.33%	\$284.72	49.53%	\$305.56	\$284.72
036520	NE-Business Development	Regional Allocation	\$62.59	0.78	\$48.95	39.33%	\$68.20	49.53%	\$73.19	\$68.20
036520	NE-Business Development	Regional Allocation	\$59.93	1.10	\$66.16	39.33%	\$92.18	49.53%	\$98.93	\$92.18
036520	NE-Business Development	Regional Allocation	\$47.70	2.71	\$129.46	39.33%	\$180.38	49.53%	\$193.59	\$180.38
036520	NE-Business Development	Regional Allocation	\$52.89	2.85	\$150.83	39.33%	\$210.15	49.53%	\$225.53	\$210.15
035020	SE-Business Development	Regional Allocation	\$45.67	2.67	\$121.85	36.58%	\$166.43	36.40%	\$166.21	\$166.43

Kentucky American Water
Business Development Costs Forecasted Test Year

Business Unit	Description	Type of Allocation	Hr Rate	Hours	dollars	labor benefit	burdened total	general benefit rate	grand burden total	Total
035020	SE-Business Development	Regional Allocation	\$60.58	1.47	\$89.17	36.58%	\$121.79	36.40%	\$121.63	\$121.63
035020	SE-Business Development	Regional Allocation	\$21.84	7.36	\$160.72	36.58%	\$219.52	36.40%	\$219.23	\$219.23
035020	SE-Business Development	Direct Charge	\$55.26	17.00	\$939.48	36.58%	\$1,283.14	36.40%	\$1,281.45	\$1,281.45
035020	SE-Business Development	Regional Allocation	\$55.26	0.55	\$30.51	36.58%	\$41.66	36.40%	\$41.61	\$41.61
035020	SE-Business Development	Regional Allocation	\$41.44	3.59	\$148.70	36.58%	\$203.09	36.40%	\$202.82	\$202.82
035020	SE-Business Development	Regional Allocation	\$75.72	6.99	\$529.44	36.58%	\$723.11	36.40%	\$722.16	\$722.16
035020	SE-Business Development	Regional Allocation	\$60.70	2.25	\$136.81	36.58%	\$186.86	36.40%	\$186.61	\$186.61
035020	SE-Business Development	Regional Allocation	\$61.61	0.74	\$45.35	36.58%	\$61.93	36.40%	\$61.85	\$61.85
035020	SE-Business Development	Regional Allocation	\$32.89	0.37	\$19.46	36.58%	\$26.58	36.40%	\$26.55	\$26.55
036520	NE-Business Development	Regional Allocation	\$62.91	0.41	\$25.91	36.58%	\$35.39	36.40%	\$35.34	\$35.34
036520	NE-Business Development	Regional Allocation	\$59.93	0.37	\$22.05	36.58%	\$30.12	36.40%	\$30.08	\$30.08
036520	NE-Business Development	Regional Allocation	\$47.70	3.31	\$157.99	36.58%	\$215.78	36.40%	\$215.50	\$215.50
036520	NE-Business Development	Regional Allocation	\$52.89	1.27	\$66.90	36.58%	\$91.37	36.40%	\$91.25	\$91.25
035020	SE-Business Development	Regional Allocation	\$45.67	1.01	\$46.22	33.51%	\$61.71	45.40%	\$67.21	\$67.21
035020	SE-Business Development	Regional Allocation	\$60.58	1.96	\$118.97	33.51%	\$158.84	45.40%	\$172.99	\$172.99
035020	SE-Business Development	Regional Allocation	\$21.84	11.04	\$241.09	33.51%	\$321.87	45.40%	\$350.54	\$350.54
035020	SE-Business Development	Direct Charge	\$55.26	2.00	\$110.52	33.51%	\$147.56	45.40%	\$160.70	\$160.70
035020	SE-Business Development	Regional Allocation	\$55.26	2.02	\$111.85	33.51%	\$149.34	45.40%	\$162.64	\$162.64
035020	SE-Business Development	Regional Allocation	\$41.44	0.97	\$40.03	33.51%	\$53.45	45.40%	\$58.21	\$58.21
035020	SE-Business Development	Regional Allocation	\$75.72	8.74	\$661.80	33.51%	\$883.57	45.40%	\$962.26	\$962.26
035020	SE-Business Development	Direct Charge	\$60.70	22.00	\$1,335.34	33.51%	\$1,782.81	45.40%	\$1,941.58	\$1,941.58
035020	SE-Business Development	Regional Allocation	\$60.70	2.58	\$156.36	33.51%	\$208.75	45.40%	\$227.34	\$227.34
035020	SE-Business Development	Regional Allocation	\$52.89	1.10	\$58.39	33.51%	\$77.95	45.40%	\$84.89	\$84.89
036520	NE-Business Development	Regional Allocation	\$47.70	4.97	\$236.99	33.51%	\$316.40	45.40%	\$344.58	\$344.58
032020	CORP-Corporate Bus Development	Direct Charge	\$50.48	4.34	\$218.93	38.39%	\$302.98	41.25%	\$309.24	\$309.24
035020	SE-Business Development	Regional Allocation	\$45.67	2.02	\$92.44	38.39%	\$127.93	41.25%	\$130.57	\$130.57
035020	SE-Business Development	Regional Allocation	\$21.84	7.36	\$160.72	38.39%	\$222.43	41.25%	\$227.02	\$227.02
035020	SE-Business Development	Direct Charge	\$55.26	16.00	\$884.22	38.39%	\$1,223.67	41.25%	\$1,248.96	\$1,248.96
035020	SE-Business Development	Regional Allocation	\$55.26	2.62	\$144.90	38.39%	\$200.53	41.25%	\$204.67	\$204.67
035020	SE-Business Development	Regional Allocation	\$63.36	0.37	\$23.32	38.39%	\$32.27	41.25%	\$32.93	\$32.93
035020	SE-Business Development	Regional Allocation	\$41.44	2.02	\$83.86	38.39%	\$116.08	41.25%	\$118.48	\$118.48
035020	SE-Business Development	Regional Allocation	\$75.72	6.44	\$487.64	38.39%	\$674.85	41.25%	\$688.80	\$688.80
035020	SE-Business Development	Direct Charge	\$60.70	7.00	\$424.90	38.39%	\$588.02	41.25%	\$600.17	\$600.17
035020	SE-Business Development	Regional Allocation	\$60.70	2.58	\$156.36	38.39%	\$216.38	41.25%	\$220.85	\$220.85
035020	SE-Business Development	Regional Allocation	\$52.89	3.68	\$194.62	38.39%	\$269.33	41.25%	\$274.90	\$274.90
036520	NE-Business Development	Regional Allocation	\$47.70	3.68	\$175.55	38.39%	\$242.94	41.25%	\$247.96	\$247.96
032020	CORP-Corporate Bus Development	Direct Charge	\$50.48	-1.54	-\$77.69	31.08%	-\$101.83	28.82%	-\$100.08	-\$100.08
035020	SE-Business Development	Regional Allocation	\$45.67	1.47	\$67.23	31.08%	\$85.12	28.82%	\$86.61	\$86.61
035020	SE-Business Development	Regional Allocation	\$60.58	0.74	\$44.59	31.08%	\$58.44	28.82%	\$57.43	\$57.43
035020	SE-Business Development	Regional Allocation	\$21.84	7.36	\$160.72	31.08%	\$210.68	28.82%	\$207.04	\$207.04
035020	SE-Business Development	Direct Charge	\$55.26	6.00	\$331.58	31.08%	\$434.64	28.82%	\$427.14	\$427.14
035020	SE-Business Development	Regional Allocation	\$55.26	1.84	\$101.69	31.08%	\$133.29	28.82%	\$130.99	\$130.99
035020	SE-Business Development	Regional Allocation	\$63.36	4.78	\$303.10	31.08%	\$397.30	28.82%	\$390.45	\$390.45
035020	SE-Business Development	Regional Allocation	\$41.44	1.47	\$61.00	31.08%	\$79.96	28.82%	\$78.58	\$78.58
035020	SE-Business Development	Regional Allocation	\$75.72	6.39	\$484.16	31.08%	\$634.64	28.82%	\$623.69	\$623.69
035020	SE-Business Development	Direct Charge	\$60.70	5.00	\$303.49	31.08%	\$397.81	28.82%	\$390.96	\$390.96
035020	SE-Business Development	Regional Allocation	\$60.70	2.90	\$175.90	31.08%	\$230.57	28.82%	\$226.59	\$226.59

September

October

November

Kentucky American Water
Business Development Costs Forecasted Test Year

Business Unit	Description	Type of Allocation	Hr Rate	Hours	dollars	labor benefit	burdened total	general benefit rate	grand burden total	Total
035020	SE-Business Development	Regional Allocation	\$52.89	2.94	\$155.69	31.08%	\$204.98	28.82%	\$200.56	
036520	NE-Business Development	Regional Allocation	\$47.70	3.29	\$156.99	31.08%	\$205.66	28.82%	\$202.11	
032020	CORP-Corporate Bus Development	National Allocation	\$78.77	4.86	\$383.13	38.42%	\$530.32	41.63%	\$542.62	
035020	SE-Business Development	Regional Allocation	\$45.67	1.96	\$89.29	38.42%	\$123.59	41.63%	\$126.46	
035020	SE-Business Development	Regional Allocation	\$60.58	1.47	\$89.17	38.42%	\$123.43	41.63%	\$126.29	
035020	SE-Business Development	Regional Allocation	\$21.84	7.36	\$160.72	38.42%	\$222.47	41.63%	\$227.63	
035020	SE-Business Development	Direct Charge	\$55.26	2.00	\$110.52	38.42%	\$152.98	41.63%	\$156.53	
035020	SE-Business Development	Regional Allocation	\$55.26	2.53	\$139.82	38.42%	\$193.54	41.63%	\$198.02	
035020	SE-Business Development	Regional Allocation	\$63.36	3.50	\$221.49	38.42%	\$278.78	41.63%	\$283.70	
035020	SE-Business Development	Regional Allocation	\$41.44	0.92	\$38.13	38.42%	\$64.25	41.63%	\$66.12	
035020	SE-Business Development	Regional Allocation	\$75.72	6.12	\$463.26	38.42%	\$680.35	41.63%	\$701.45	
035020	SE-Business Development	Direct Charge	\$60.70	20.00	\$1,213.95	38.42%	\$1,680.35	41.63%	\$1,719.32	
035020	SE-Business Development	Regional Allocation	\$60.70	2.58	\$156.36	38.42%	\$216.43	41.63%	\$221.45	
035020	SE-Business Development	Regional Allocation	\$52.89	3.82	\$201.92	38.42%	\$279.49	41.63%	\$285.97	
036520	NE-Business Development	Regional Allocation	\$47.70	3.59	\$171.16	38.42%	\$236.92	41.63%	\$242.41	
				558.17	\$28,646.59		\$39,159.87		\$39,764.62	\$78,924.49
	National Allocation			16.00	\$ 1,022.87		\$ 1,517.93		\$ 1,524.81	3,042.74
	Regional Allocation			411.38	\$20,142.70		\$27,437.61		\$27,856.61	55,294.22
	Direct Charge			130.80	\$ 7,481.01		\$10,204.33		\$10,383.20	20,587.53
	Total Business Development Costs			558.17	\$28,646.59		\$39,159.87		\$78,924.49	78,924.49

KENTUCKY-AMERICAN WATER COMPANY
CASE NO. 2007-00143
COMMISSION STAFF'S THIRD
SET OF INFORMATION REQUESTS
Item 13 of 54

Witness: Michael Miller

13. Refer to Kentucky-American's Response to Commission Staff's Second Set of Information Requests, Item 22, page 3 of 4.
- a. Management Fees in the current filing are stated as \$6,246,717. Note 1 references Exhibit MAM-7 where, at page 1 of 2, Management Fees are stated as \$4,064,421. Reconcile these differences and explain why the \$6,246,717 should not replace the \$4,064,421 on Exhibit MAM-7, which results in a negative savings or cost of \$1,343,504 (\$9,296,847 + \$6,246,717 - \$14,200,060).
 - b. Note 2 explains that a portion of the increase in Management Fees requested in this case over the amount allowed by the Commission in Case No. 2004-00103 is attributable to 4 percent pay raises, medical cost increases of 8 to 10 percent, and pension cost increases of up to 150 percent.
 - (1) Quantify the increase in management fees that is attributable to each factor stated in Note 2.
 - (2) Quantify the increase in management fees requested in this case over those allowed in Case No. 2004-00103 that is attributable to the increased work-hours of Service Company personnel assigned or allocated to Kentucky-American. This response shall include the number of work-hours allocated or assigned to Kentucky-American by each Service Company in the forecast period of this case as compared to that of the forecast in Case No. 2004-00103, with explanations of all increases.
 - c. List all duties that the Service Companies will perform on Kentucky-American's behalf in the forecasted period of this case for which the proposed management fees will be charged that Kentucky-American employees performed during the forecasted period of Case No. 2004-00103.
 - d. At Exhibit MAM-7, page 1 of 2, of his written testimony, Mr. Miller refers to \$1,321,183 of management fees approved in Case No. 2000-00120. In Case No. 2000-00120,¹ Kentucky-American requested service company fees of \$1,021,021 and the Commission allowed a recovery of only \$988,522. State how Mr. Miller determined the allowed level to be \$1,321,183.

Response:

- a. The 4,064,421 shown on Exhibit MAM-7 is incorrect. Attached to this response is a revised Exhibit MAM-7 which includes the correction to reflect forecasted test-year AWWSC charges of \$6,246,717. Mr. Miller will be providing a correction to his Direct Testimony to reflect the changes made to the Exhibit. The revised

¹ Case No. 2000-00120, Application of Kentucky-American Water Company to Increase Its Rates (Ky. PSC Nov. 28, 2000) at 49.

Exhibit also corrects several cell calculations that were discovered in reviewing the Exhibit. The original Exhibit MAM-7 used a blended inflation factor for AWWSC charges of 4.5%. Based on the information requested in part b. below regarding the actual increases for AWWSC pensions, OPEB's and group insurance, the 2001 AWWSC charges have been separated into those components and have been inflated to reflect the cost increase for those components. The footnote added to the Exhibit explains the calculations and the basis for the calculations, and page 2 of the Revised Exhibit provides the calculations of those cost increase factors. The Revised Exhibit also includes adjustments necessary to make a meaningful comparison of 2001 to forecasted test-year costs along with explanations of those necessary adjustments.

- b. (1) Please see the attached schedule and the information added to Page 2 of the Revised Exhibit MAM-7 referenced in part a. above.
- (2) Please see the attached schedule.
- c. Please see the schedule attached to part b (2) above. As identified on that schedule the following functions are included in the AWWSC charges for this filing that were included in the duties of KAWC employees in the previous rate case:
 - Employee Benefit Administration
 - Customer Accounting Services (Service Order Scheduling & Completion)
 - Engineering Management
 - Human Resource Management
 - Operations Management
 - Risk Management
 - Water Quality Management
- d. As stated in the title to column on page 1 of Exhibit MAM-7, the \$1,321,183 was the actual AWWSC charges for 2001. The AWWSC charges authorized for the forecasted test-year in Case No. 2000-00120 were not reflective of the actual charges for 2001.

For electronic version, refer to KAW_R_PSCDR2#13_071607.pdf

Kentucky American Water Labor & Management Fee Analysis That Demonstrates the Shift From Fully Loaded Company Labor to Management Fees

Exhibit MAM-7
Page 1 of 2

	Labor Cost As Approved in KAWC Case No. 2000-00120 Attrition Yr. 11/30/2001 plus actual 2001 overhead costs & Man. Fees	Add emp. cost for 6 emp. EL, TV	2001 Base Cost	2002 Labor Cost	2003 Labor Cost	2004 Labor Cost	Add emp. cost for 8 emp. Owenton	2005 Labor Cost	2006 Labor Cost	2007 Labor Cost	2008 Labor Cost	Attrition Year Request by Company	Current Case Net Savings Variance Column 8 to Column 9
			(1)	(2)	(3)	(4)		(5)	(6)	(7)	(8)	(9)	(10)
							Note 5		Note 3&4				
KAWC Costs:													
Labor (Adj. 3.5% Avg. Pay Incr. 02-03 & 4% for 04-08)	6,004,634	250,193	6,254,827	6,514,837	6,742,856	7,012,571	473,103	7,766,176	8,284,074	8,743,248	9,092,978	6,318,580	(2,774,398)
Group Insurance	1,303,786	54,324	1,358,110	1,559,146	1,857,663	2,000,138	134,939	2,215,083	2,206,524	2,057,109	2,150,322	1,887,912	(262,410)
Pensions	356,713	14,863	371,576	451,264	940,976	915,419	61,759	1,013,794	946,558	650,433	585,941	503,733	(82,208)
Payroll Taxes	443,276	18,470	461,746	468,378	504,644	495,797	33,449	549,078	568,161	685,271	712,685	487,918	(224,767)
401(K)	95,232	3,551	98,783	98,733	96,842	92,530	6,243	102,473	114,001	116,069	118,549	98,704	(19,845)
Fully Loaded Labor Cost	8,193,641	341,402	8,535,043	9,092,359	10,142,982	10,516,454	709,493	11,646,605	12,119,317	12,252,131	12,660,475	9,296,847	(3,363,628)
AWWSC costs:													
Labor	871,980		871,980	906,859	943,134	980,859		1,020,093	1,060,897	1,103,333	1,147,466	3,240,763	2,093,287
Pensions	0		0	18,708	26,145	12,067		31,407	104,379	141,519	127,500	356,548	229,048
OPEB's	35,671		35,671	44,401	57,092	60,605		70,719	72,379	72,379	72,379	376,891	304,512
Group Insurance	63,053		63,053	69,949	75,854	78,193		85,382	90,618	100,743	112,832	591,908	479,076
Other Expenses	350,479		350,479	359,241	368,222	377,428		390,638	400,403	410,414	420,674	1,680,616	1,259,942
Management Fees (Adjusted for 4.5% inflation)	1,321,183	0	1,321,183	1,399,158	1,470,447	1,509,150	0	1,598,238	1,728,676	1,828,387	1,880,851	6,246,716	4,365,865
Total Labor & Management Fees	9,514,824	341,402	9,856,226	10,491,517	11,613,429	12,025,605	709,493	13,244,843	13,847,993	14,080,519	14,541,327	15,543,563	1,002,236

Adjustments: 1. Initiation of Procurement Center in 2003 which has resulted in savings to KAWC as demonstrated on the synergy statements filed at the PSC as part of the conditions in case no. 2002-00018
 2. Customer Growth at KAWC handled by the CCC & SCC is not accounted for in the analysis above. In 2001 KAWC had 22 employees serving 103,172 customers or 4,489 customer per employee. Based on the forecasted test-year customer base of 120,065 would have had to add 4.74 FTE's or 9,859 hours @ an average cost of \$19.23 per hour * OH at 1.40 =
 3. The analysis above does not account for the significant increase in ERISA pension contributions. KAWC's current rates were established in December 2004 based on AWWSC pension expense of \$27,234. AWWSC pension expenses charged to KAWC were 2005-81,108; 2006-304,691; 2007-395,751. To properly compare the impact the analysis should reflect this adjustment.

Unexplained variance (comprised of items not easily identifiable such as: changes in allocation factors, additional services, changes in operations, additional regulation, etc.)

FOOTNOTES RELATED TO KAWC COSTS:

- Note 1:** The calculation of inflation factors used to determining the pro-forma 2008 costs shown in column 8 above are included on page 2 of this Exhibit.
- Note 2:** Added one meter reader in 2002 to handle increases in customers due to growth
- Note 3:** Added 4 utility field employees to handle additional hydrant and valve maintenance work related to customer growth and one Administrative employee to handle sewer billing in 2006
- Note 4:** Added 1 utility person and one Admin to handle additional requirements for cross connections and 1 production tech for additional water treatment processes
- Note 5:** Added 8 employees from Owenton acquisition

FOOTNOTES RELATED TO AWWSC COSTS:

Footnote 1: Labor is inflated 4% per year; Other Expenses are inflated at 2.5% per year; and pensions, OPEB's, and group insurance are inflated by the factors on page 2 of this Exhibit.

Exhibit MAM-7
Page 2 of 2

KAWC Actual Loaded Labor Costs

	2001	2002	2003	2004	2005	2006	Budget 2007	Budget 2008
AVG. # Employees	145	143.25	129.42	118.58	117.92	124.75	137.00	137.00
Group Insurance	1,303,786	1,468,185	1,580,403	1,559,089	1,608,346	1,644,303	1,653,852	1,728,792
Pensions	356,713	424,938	800,534	713,561	782,335	748,274	554,137	499,193
Payroll Taxes	443,276	441,053	429,325	386,469	379,691	403,803	525,874	546,911
401(K)	85,232	92,973	82,388	72,126	78,071	109,606	94,990	99,928
Fully Loaded Cost	2,103,920	1,893,123	2,380,937	2,272,650	2,390,681	2,392,577	2,207,989	2,227,985

Cost per Employee

	2001	2002	2003	2004	2005	2006	Budget 2007	Budget 2008
Group Insurance	8,987	10,249	12,211	13,148	13,639	13,181	12,072	12,619
Pensions	2,459	2,966	6,186	6,018	6,634	5,998	4,045	3,644
Payroll Taxes	3,055	3,079	3,317	3,259	3,220	3,237	3,838	3,992
401(K)	587	649	637	608	662	879	693	729
Fully Loaded Cost per employee	14,501	16,294	21,714	22,425	23,494	22,416	19,955	20,255

	% Increase							
Group Insurance	1.140	1.191	1.077	1.037	1.037	0.966	0.916	1.045
Pensions	1.206	2.085	0.973	1.103	1.103	0.904	0.674	0.901
Payroll Taxes	1.008	1.077	0.982	0.988	0.988	1.005	1.186	1.040
401(K)	1.105	0.981	0.955	1.088	1.088	1.327	0.789	1.052
Fully Loaded Cost per customer	1.124	1.333	1.033	1.048	1.048	0.954	0.890	1.015

AWWC Costs:

	2001	2002	2003	2004	2005	2006	Budget 2007	Budget 2008
AVG. # Employees	9.17	16.36	22.12	37.10	42.25	47.75	45.75	45.75
Pension	0	18,708	35,350	27,364	81,108	304,651	395,751	356,548
OPEB's	35,671	79,215	137,719	245,194	325,832	376,891	361,107	361,107
Group Insurance	63,053	124,794	182,977	316,352	393,390	471,866	502,615	562,929

Cost per Employee

	2001	2002	2003	2004	2005	2006	Budget 2007	Budget 2008
Pension	0	1,144	1,598	738	1,920	6,380	8,650	7,793
OPEB's	3,890	4,842	6,226	6,609	7,712	7,893	7,893	7,893
Group Insurance	6,876	7,628	8,272	8,527	9,311	9,882	10,986	12,304

	% Increase							
Pensions	#DIV/0!	1.398	0.462	2.603	2.603	3.323	1.356	0.901
OPEB's	1.245	1.286	1.062	1.167	1.167	1.023	1.000	1.000
Group Insurance	1.109	1.084	1.031	1.092	1.092	1.061	1.112	1.120

**Kentucky American Water
Response to PSCDR3#13 b (1)**

	<u>2001</u>	<u>2002</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>Budget 2007</u>	<u>Fore. Test-yr. 2008</u>
Labor	871,980	1,638,096	2,091,188	2,787,120	2,732,410	2,996,259	3,116,109	3,240,753
Pension	0	18,708	35,350	27,364	81,108	304,651	395,751	356,548
OPEB's	35,671	79,215	137,719	245,194	325,832	376,891	361,107	361,107
Group Insurance	63,053	124,794	182,977	316,352	393,390	471,866	502,615	562,929
Other Expense	<u>350,479</u>	<u>1,325,492</u>	<u>674,451</u>	<u>2,401,475</u>	<u>2,361,694</u>	<u>2,462,748</u>	<u>2,094,374</u>	<u>1,725,380</u>
Total AWWWS Charges to KAWC	1,321,183	3,186,305	3,121,685	5,777,505	5,894,434	6,612,415	6,469,956	6,246,717
AWWSC Charges Recognized for Rates	932,968				3,800,677			6,246,717 Note 1
<u>Cost per Employee</u>								
Pension	0	1,144	1,598	738	1,920	6,380	8,650	7,793
OPEB's	3,890	4,842	6,226	6,609	7,712	7,893	7,893	7,893
Group Insurance	6,876	7,628	8,272	8,527	9,311	9,882	10,986	12,304
<u>Cost Increase factors:</u>								
Pensions		#DIV/0!	1.398	0.462	2.603	3.323	1.356	0.901
OPEB's		1.245	1.286	1.062	1.167	1.023	1.000	1.000
Group Insurance		1.109	1.084	1.031	1.092	1.061	1.112	1.120
Total AWWSC Hours Charged	19,067.01	34,026.40	46,017.33	81,619.23	92,942.34	105,060.13	100,900.00	100,900.00
	9.17	16.36	22.12	37.10	42.25	47.75	45.75	45.75

Note 1: 2008 level requested in current case

**Kentucky American Water Company
Response to PSCDR3#13 b (2)**

Org	Department	Provider	Case Number 2004-00103 Hours	Case Number 07-00143 Hours	Variance	Explanation
Belleville Lab	Water Quality/Laboratory	Professional Engineer	2,713	2,618	(95)	Staffing for add'l testing, offset by shift of R&D to corporate administration
Call Center	Information Systems/Billing	Customer Acct Svcs	29,547	47,604	18,057	04 rate case was based on partial year history (understated) +add'l emp. to meet service level targets and transfer of functions from IT
Corporate	Accounting	Certified Public Accountant	955	2,216	1,261	Add'l functions transferred from SSC
Corporate	Administration	Management Consultant	725	484	(241)	Functions transferred to corp. operations
Corporate	Audit	Certified Public Accountant	334	576	242	Vacancies in 04 not included in prior case
Corporate	Communications	Management Consultant	212	236	24	Difference in allocations
Corporate	Corporate Secretary	Attorney	72	299	227	Increase FTE's
Corporate	Finance	Certified Public Accountant	611	1,571	960	Vacancies in 04 not included in prior case
Corporate	Human Resources	Management Consultant	900	1,606	706	Added national benefits administration, offset at subsidiaries
Corporate	Operations	Professional Engineer	1,119	1,482	363	Included in Admin. in prior case
Corporate	Water Quality/Corporate	Professional Engineer	250	676	426	Transfer of R&D from Belleville Lab
Corporate	Risk Management	Management Consultant	-	351	351	Included in Admin. in prior case
Subtotal Corporate			5,178	9,496	4,318	
Information Technology	ITS Audit	Certified Public Accountant	44	410	366	Increase FTE's
Information Technology	IT	Certified Public Accountant	10,320	9,203	(1,117)	IT functions transferred to SSC, CCC
Subtotal ITS			10,364	9,613	(751)	
Shared Services	Accounting	Certified Public Accountant	6,682	7,922	1,240	IT functions transferred to SSCin.
Shared Services	Administration	Management Consultant	1,723	325	(1,398)	Shift of time to Corp. Acct.
Shared Services	Finance	Certified Public Accountant	1,475	1,676	201	Increase in FTE's
Subtotal SSE			9,880	9,923	43	
Regional Offices	Administration	Management Consultant	5,175	911	(4,264)	
Regional Offices	Communications	Management Consultant	-	2,171	2,171	Functions added to Reg. Ser. Co.
Regional Offices	Customer Service	Customer Acct Svcs	-	4,042	4,042	Functions added to Reg. Ser. Co., offset at reg. subsidiaries
Regional Offices	Corporate Secretary	Attorney	51	1,743	1,692	Shift from Admin (Herb Miller classified as Admin. In 04 case
Regional Offices	Engineering	Professional Engineer	317	539	222	Functions added to Reg. Ser. Co., offset at reg. subsidiaries
Regional Offices	Finance	Certified Public Accountant	2,599	3,136	537	Less FTE's
Regional Offices	Human Resources	Management Consultant	891	1,864	973	Functions added to Reg. Ser. Co., offset at reg. subsidiaries
Regional Offices	Operations	Professional Engineer	-	4,605	4,605	Functions added to Reg. Ser. Co., offset at reg. subsidiaries
Regional Offices	Risk Management	Management Consultant	-	1,646	1,646	Functions added to Reg. Ser. Co., offset at reg. subsidiaries
Regional Offices	Water Quality	Professional Engineer	-	990	990	Functions added to Reg. Ser. Co., offset at reg. subsidiaries
Subtotal Regional Office			9,033	21,647	12,614	
	Total		66,715	100,900	34,185	
	Average hourly rate per hour for AWWSC charge in 2008 forecasted test-year					\$32.11
	(\$3,240,753/100,900 Hrs.)					
	Increase in AWWSC Labor charges from prior case due to increased hours.					\$1,097,674
	Increase in AWWSC Pension Expense (\$7,793-737*45.75)					\$322,766
	Increase in AWWSC OPEB Expense (\$7893.05-6224*45.75)					\$76,357
	Increase in AWWSC Group Insurance Costs (\$12304-8270)*45.75)					\$184,556
	Increase in AWWSC charges directly related to increased hours charged to KAWC.					\$1,681,353
	This does not include the other expenses allocated thru the general overhead.					

KENTUCKY-AMERICAN WATER COMPANY
CASE NO. 2007-00143
COMMISSION STAFF'S THIRD
SET OF INFORMATION REQUESTS
Item 14 of 54

Witness: Michael Miller/Patrick Baryenbruch

14. Refer to the Direct Testimony of Patrick Baryenbruch, PLB-1, Schedule 3.
- a. Using the same format as used in Schedule 3, provide a chart of the hours that the Service Company assigned or allocated to Kentucky-American for the forecasted test period in Case No. 2004-00103 and for the forecasted test period in the present case. Explain any significant increases in hours allocated or assigned between these two cases.
 - b. Restate PLB-1, Schedule 3, to include hours for Customer Account Services.
 - c. Using the same format as used in Schedule 3, provide a chart of the hours that the Service Company assigned or allocated to Kentucky-American for the forecasted test period in Case No. 2004-00103 and for the forecasted test period in the present case but include hours assigned or allocated for Customer Account Services.

Response:

- a. Please see the attached.
- b. Please see the attached.
- c. Please see the schedule attached for part a. above.

For electronic version, refer to KAW_R_PSCDR3#14_071607.pdf

**Kentucky American Water Company
Response to PSCDR3#14 a**

Org	Department	Provider	Case Number 2004-00103 Hours	Case Number 07-00143 Hours	Variance	Explanation
Belleville Lab	Water Quality/Laboratory	Professional Engineer	2,713	2,618	(95)	Staffing for add'l testing, offset by shift of R&D to corporate administration
Call Center	Information Systems/Billing	Customer Acct Svcs	29,547	47,604	18,057	04 rate case was based on partial year history (understated) +add'l emp. to meet service level targets and transfer of functions from IT
Corporate	Accounting	Certified Public Accountant	955	2,216	1,261	Add'l functions transferred from SSC
Corporate	Administration	Management Consultant	725	484	(241)	Functions transferred to corp. operations
Corporate	Audit	Certified Public Accountant	334	576	242	Vacancies in 04 not included in prior case
Corporate	Communications	Management Consultant	212	236	24	Difference in allocations
Corporate	Corporate Secretary	Attorney	72	299	227	Increase FTE's
Corporate	Finance	Certified Public Accountant	611	1,571	960	Vacancies in 04 not included in prior case
Corporate	Human Resources	Management Consultant	900	1,606	706	Added national benefits administration, offset at subsidiaries
Corporate	Operations	Professional Engineer	1,119	1,482	363	Included in Admin. in prior case
Corporate	Water Quality/Corporate	Professional Engineer	250	676	426	Transfer of R&D from Belleville Lab
Corporate	Risk Management	Management Consultant	-	351	351	Included in Admin. In prior case
Subtotal Corporate			5,178	9,496	4,318	
Information Technology	ITS Audit	Certified Public Accountant	44	410	366	Increase FTE's
Information Technology	IT	Certified Public Accountant	10,320	9,203	(1,117)	IT functions transferred to SSC, CCC
Subtotal ITS			10,364	9,613	(751)	
Shared Services	Accounting	Certified Public Accountant	6,682	7,922	1,240	IT functions transferred to SSCin.
Shared Services	Administration	Management Consultant	1,723	325	(1,398)	Shift of time to Corp. Acct.
Shared Services	Finance	Certified Public Accountant	1,475	1,676	201	Increase in FTE's
Subtotal SSE			9,880	9,923	43	
Regional Offices	Administration	Management Consultant	5,175	911	(4,264)	Functions added to Reg. Ser. Co.
Regional Offices	Communications	Management Consultant	-	2,171	2,171	Functions added to Reg. Ser. Co., offset at reg. subsidiaries
Regional Offices	Customer Service	Customer Acct Svcs	-	4,042	4,042	Functions added to Reg. Ser. Co., offset at reg. subsidiaries
Regional Offices	Corporate Secretary	Attorney	51	1,743	1,692	Shift from Admin (Herb Miller classified as Admin. In 04 case
Regional Offices	Engineering	Professional Engineer	317	539	222	Functions added to Reg. Ser. Co., offset at reg. subsidiaries
Regional Offices	Finance	Certified Public Accountant	2,599	3,136	537	Less FTE's
Regional Offices	Human Resources	Management Consultant	891	1,864	973	Functions added to Reg. Ser. Co., offset at reg. subsidiaries
Regional Offices	Operations	Professional Engineer	-	4,605	4,605	Functions added to Reg. Ser. Co., offset at reg. subsidiaries
Regional Offices	Risk Management	Management Consultant	-	1,646	1,646	Functions added to Reg. Ser. Co., offset at reg. subsidiaries
Regional Offices	Water Quality	Professional Engineer	-	990	990	Functions added to Reg. Ser. Co., offset at reg. subsidiaries
Subtotal Regional Office			9,033	21,647	12,614	
Total			66,715	100,900	34,185	

Kentucky American Water Company
2003 Service Company Hours
Company Witness: Patrick Baryenbruch

Org	Function	Department	Year	Provider	Hours
Belleville Lab	Belleville Lab	Water Quality/Laboratory	2003	Professional Engineer	2,713
Call Center	Call Center	Information Systems/Billing	2003	Customer Acct Svcs	6,547
Corporate	Corporate	Accounting	2003	Certified Public Accountant	955
Corporate	Corporate	Administration	2003	Management Consultant	725
Corporate	Corporate	Audit	2003	Certified Public Accountant	334
Corporate	Corporate	Communications	2003	Management Consultant	212
Corporate	Corporate	Corporate Secretary	2003	Attorney	72
Corporate	Corporate	Engineering	2003	Professional Engineer	841
Corporate	Corporate	Finance	2003	Certified Public Accountant	611
Corporate	Corporate	Human Resources	2003	Management Consultant	900
Corporate	Corporate	Information Systems/Billing	2003	Customer Acct Svcs	4
Corporate	Corporate	Operations	2003	Professional Engineer	278
Corporate	Corporate	Water Quality/Corporate	2003	Professional Engineer	250
Indiana	Regional Offices	Corporate Secretary	2003	Attorney	24
Information Technology	Information Technology	Administration	2003	Management Consultant	40
Information Technology	Information Technology	Information Systems/Billing	2003	Customer Acct Svcs	125
Information Technology	Information Technology	Information Systems/Financial	2003	Certified Public Accountant	11,195
Shared Services	Shared Services	Accounting	2003	Certified Public Accountant	6,682
Shared Services	Shared Services	Administration	2003	Management Consultant	1,647
Shared Services	Shared Services	Finance	2003	Certified Public Accountant	1,475
Shared Services	Shared Services	Human Resources	2003	Certified Public Accountant	76
Southeast Region	Regional Offices	Administration	2003	Management Consultant	5,171
Southeast Region	Regional Offices	Corporate Secretary	2003	Attorney	27
Southeast Region	Regional Offices	Engineering	2003	Professional Engineer	317
Southeast Region	Regional Offices	Finance	2003	Certified Public Accountant	2,100
Southeast Region	Regional Offices	Human Resources	2003	Management Consultant	1,191
Southeast Region	Regional Offices	Rates and Revenues	2003	Certified Public Accountant	1,499
Western Region	Regional Offices	Risk Management	2003	Management Consultant	4
				Total	46,015

**Kentucky American Water Company
2006 Service Company Hours
Company Witness: Patrick Baryenbruch**

Function	Department	Year	Provider	Hours
Belleville Lab	Water Quality	2006	Professional Engineer	2617.57
Call Center	Customer Service	2006	Customer Account Services	43767.74
Call Center	Human Resources	2006	Management Consultant	472.36
Corporate	Accounting	2006	Certified Public Accountant	1549.68
Corporate	Administration	2006	Management Consultant	127.9
Corporate	Audit	2006	Certified Public Accountant	574.7
Corporate	Communications	2006	Management Consultant	226.95
Corporate	Finance	2006	Certified Public Accountant	1462.73
Corporate	Human Resources	2006	Management Consultant	1594.77
Corporate	Legal	2006	Attorney	298.91
Corporate	Operations	2006	Professional Engineer	507.08
Corporate	Rates & Revenue	2006	Certified Public Accountant	327.31
Corporate	Risk Management	2006	Management Consultant	350.56
Corporate	Water Quality	2006	Professional Engineer	571.52
Regional Offices	Accounting	2006	Certified Public Accountant	349.42
Regional Offices	Administration	2006	Management Consultant	909.46
Regional Offices	Communications	2006	Management Consultant	4241.98
Regional Offices	Customer Service	2006	Customer Account Services	6136.02
Regional Offices	Engineering	2006	Professional Engineer	341.28
Regional Offices	Finance	2006	Certified Public Accountant	2604.28
Regional Offices	Human Resources	2006	Management Consultant	1939.77
Regional Offices	Legal	2006	Attorney	1741.9
Regional Offices	Operations	2006	Professional Engineer	4481.73
Regional Offices	Risk Management	2006	Management Consultant	1646.77
Regional Offices	Water Quality	2006	Professional Engineer	991.05
Information Technology	Information Technology	2006	Certified Public Accountant	335.62
Information Technology	Accounting	2006	Certified Public Accountant	8415.06
Shared Services	Administration	2006	Certified Public Accountant	7979.31
Shared Services	Finance	2006	Management Consultant	275.14
Shared Services	Rates & Revenue	2006	Certified Public Accountant	1382.87
Shared Services		2006	Certified Public Accountant	277.46
			Total	98,499

KENTUCKY-AMERICAN WATER COMPANY
CASE NO. 2007-00143
COMMISSION STAFF'S THIRD
SET OF INFORMATION REQUESTS
Item 15 of 54

Witness: Sheila Miller

15. Refer to Kentucky-American's Response to Commission Staff's First Set of Information Requests, Item 1(a), W/P 3, pages 71 through 118. Explain how the billing department coverage is estimated.

Response:

Life Basic – non bargaining (salary x 1.5)	\$2,786,492 x 1.5 = 4,179,738
Life Basic – bargaining (salary)	\$4,563,424 = 4,563,424
AD & D – no. of hourly employees x 10,000	93 x 10,000 = 930,000
AD & D – no. of salary employees x 10,000	44 x 100000 = 440,000
Long term disability – non bargaining salary / 12	\$2,786,492/12 = 232,208

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KENTUCKY-AMERICAN WATER COMPANY
CASE NO. 2007-00143
COMMISSION STAFF'S THIRD
SET OF INFORMATION REQUESTS
Item 16 of 54

Witness: Michael A. Miller/Sheila Miller

16. Refer to Kentucky-American's Response to Commission Staff's Second Set of Information Requests, Item 30.
- a. Provide a comparison of estimated and actual rate case expenses for the previous 10 rate cases that Kentucky-American has filed with the Commission.
 - b. For each rate case listed in response to Item 16(a), state the case number, the type of test-period (e.g., historic, future) used, and the number of customers served or estimated to be served during the test-year.

Response:

Information is only available for the prior five rate filings and the current rate case.

Case No.	Type of TY	# Customers	Estimated Rate Case Expense	Actual Rate Case Expense
94-197	forecasted	83,959	381,000	250,434
95-554	forecasted	87,912	366,000	389,982
97-034	forecasted	90,296	397,100	326,414
2000-120	forecasted	101,740	310,420	459,817
2004-103	forecasted	113,726	622,409	1,081,715
2007-143	forecasted	120,065	700,000	

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**KENTUCKY-AMERICAN WATER COMPANY
CASE NO. 2007-00143**

**COMMISSION STAFF'S THIRD
SET OF INFORMATION REQUESTS
Item 17 of 54**

Witness: Michael Miller

17. For each American Water Company (“AWWC”) subsidiary that a state utility regulatory commission regulates, state its name, the level of rate case expense that its state regulatory commission permitted in the most recently completed general rate proceeding, the number of customers (actual or projected) that it served during the during the test period year, and the allowed rate case expense per customer.

Response:

See the table below.

	<u>Total Rate Case Expense from Last Rate Case</u>	<u>Total Customers</u>	<u>Cost Per Customer</u>
<u>Western Division:</u>			
California	1,334,741	169,200	7.89
Arizona	201,794	12,991	15.53
New Mexico	276,194	16,600	16.64
Texas	33,426	4,335	7.71
<u>Central Division:</u>			
Missouri	1,090,749	464,365	2.35
Indiana	776,510	281,125	2.76
Illinois	591,032	304,072	1.94
Iowa	246,537	59,986	4.11
Ohio	400,000	57,811	6.92
Michigan	Not regulated		
<u>Southeast Region:</u>			
Virginia	325,000	54,233	5.99
Pennsylvania	1,503,500	637,847	2.36
Maryland	66,000	4,778	13.81
West Virginia	650,000	165,639	3.92
Tennessee	400,000	72,841	5.49
Kentucky	622,409	113,726	5.47
<u>Northeast Region:</u>			
New Jersey	843,867	625,000	1.35
New York	400,000	74,000	5.41

KENTUCKY-AMERICAN WATER COMPANY
CASE NO. 2007-00143
COMMISSION STAFF'S THIRD
SET OF INFORMATION REQUESTS
Item 18 of 54

Witness: Michael Miller

18. Refer to Kentucky-American's Response to Commission Staff's Second Set of Information Requests, Item 32(a).
- a. Describe Kentucky-American's policy regarding the termination of water service for non-payment of bills.
 - b. State whether Kentucky-American requires customers to make a deposit to assure payment and retains that deposit for a significant period. Explain.
 - c. State whether Kentucky-American agrees that a uniform policy requiring customers to make a deposit will assist in minimizing "uncollectibles."
 - d. Describe each change in Kentucky-American's controls of customer accounts since January 1, 2005 and the effect of such change on Kentucky-American's uncollectibles.
 - e. Identify all measures that Kentucky-American intends to implement to reduce uncollectibles to the previously approved levels.

Response:

a.

	Days from bill date - previous	Days from bill date - current (effective May 6, 2007)
Due date and grace days	20	20
Reminder notice sent	21	n/a
Shut off notice sent	40	22
Shut off worked	61	34
 \$ Threshold	 >\$25	 >\$25
 Total days from bill to charge off	 154	 109
 Eligible to receive calls from a collection agency:		
\$ Threshold	>\$50	>\$50
Age in days	>31	>31

Note: Since we converted to monthly billing approximately 10 years ago, until recently, we did not take collection steps until the account had a balance over 30 days old. Effective May 6, 2007 this practice was eliminated to reduce uncollectibles.

- b. No.
- c. Kentucky American Water believes that a firm, but fair, policy for disconnection of service for nonpayment, consistently applied, will be more cost-effective than a policy requiring deposits.
- d. Since January 1, 2005, a significant change in controls of customer accounts to effect a change in uncollectibles was made effective May 6, 2007 as shown in the table above in response to item a. of this request.
- e. We will monitor the results of the recent changes for a period of time and depending on the success of these efforts, considering the impact of demographic and economic conditions, we may implement additional changes including the elimination of a dollar threshold and resumption of the collection of customer deposits.

For electronic version, please refer to [KAW_R_PSCDR3#18_071607.pdf](#)

KENTUCKY-AMERICAN WATER COMPANY
CASE NO. 2007-00143
COMMISSION STAFF'S THIRD
SET OF INFORMATION REQUESTS
Item 19 of 54

Witness: Michael Miller/Sheila Miller

19. Provide a schedule that shows for each of the last 10 years:
- a. Kentucky-American's uncollectibles expense.
 - b. Kentucky-American's total water sales.
 - c. Kentucky-American's uncollectibles expense as a percentage of water sales.

Response:

See below:

	Billed		% Uncoll
	Revenues	Net Charge-offs	Factor
1997	34,408,086	167,445	0.49%
1998	36,975,837	176,214	0.48%
1999	38,087,589	154,397	0.41%
2000	37,572,701	162,340	0.43%
2001	40,413,668	197,913	0.49%
2002	42,468,765	248,729	0.59%
2003	40,113,344	180,650	0.45%
2004	40,603,264	376,473	0.93%
2005	47,982,801	398,108	0.83%
2006	48,668,813	384,318	0.79%

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KENTUCKY-AMERICAN WATER COMPANY
CASE NO. 2007-00143
COMMISSION STAFF'S THIRD
SET OF INFORMATION REQUESTS
Item 20 of 54

Witness: Michael Miller/Sheila Miller

20. For each AWWC subsidiary that provides retail water service and is regulated by a state utility regulatory commission, describe the policy of its state utility regulatory commission towards uncollectibles for rate-making purposes.

Response:

Please see table below.

**Uncollectible
Rate Recovery
Commission Policy**

Western Division:

California	5 yr. avg.ratio applied to pro-forma revenues
Arizona	Historical test-year + % of add'l revenues
New Mexico	Historical test-year + % of add'l revenues
Texas	Historical test-year + % of add'l revenues

Central Division:

Missouri	3 yr. avg.ratio applied to pro-forma revenues
Indiana	3 yr. avg.ratio applied to pro-forma revenues
Illinois	Forecasted Test-year
Iowa	3 yr. avg.ratio applied to pro-forma revenues
Ohio	3 yr. avg.ratio applied to pro-forma revenues
Michigan	Not Regulated

Southeast Region:

Virginia	3 yr. avg.ratio applied to pro-forma revenues
Pennsylvania	3 yr. avg.ratio applied to pro-forma revenues
Maryland	3 yr. avg.ratio applied to pro-forma revenues
West Virginia	3 yr. avg.ratio applied to pro-forma revenues
Tennessee	3 yr. avg.ratio applied to pro-forma revenues
Kentucky	Forecasted Test-year

Northeast Region:

New Jersey	Projected Test-year
New York	Forecasted Test-year

For electronic version, refer to KAW_R_PSCDR3#20_071607.pdf

KENTUCKY-AMERICAN WATER COMPANY
CASE NO. 2007-00143
COMMISSION STAFF'S THIRD
SET OF INFORMATION REQUESTS
Item 21 of 54

Witness: John J. Spanos

21. Refer to Kentucky-American's Response to Commission Staff's Second Set of Information Requests, Item 42(b). Compare the information supplied in III-71 through III-101 to the Net Salvage percentages included on Exhibit JJS-1. For each account group where the net salvage percentages as stated on Exhibit JJS-1 are not identical to those calculated on III-71 through III-101, show the calculation of the net salvage values. The calculation should show how "estimates of other water companies within the industry" were used in the calculation as stated by Mr. Spanos and the source of the estimates.

Response:

An explanation of how the net salvage percentage for each account was determined is set forth on pages II-24 through II-26 of Exhibit JJS-1. The net salvage percent utilized in the depreciation calculation is an estimate that best represents the statistical data, future expectations and estimates of others. Therefore, the statistics on pages III-71 through III-101 are just a component of the final estimate.

I will use Account 331, Mains and Accessories, on pages III-86 and III-87 as an example. The statistical indications on pages III-86 for the period 1980-2006 set forth negative 13 percent net salvage. The most recent five-year period, 2002-2006, sets forth a negative 26 percent net salvage. Future expectations are comparable to the most recent seven or eight years and the industry range is negative 15 to negative 30 percent. Therefore, negative 20 was determined as the most appropriate estimate for mains. The other accounts were determined in a similar fashion.

For electronic version, refer to KAW_R_PSCDR3#21_071607.pdf

KENTUCKY-AMERICAN WATER COMPANY
CASE NO. 2007-00143
COMMISSION STAFF'S THIRD
SET OF INFORMATION REQUESTS
Item 22 of 54

Witness: John J. Spanos

22. Refer to Kentucky-American's Response to Commission Staff's Second Set of Information Requests, Item 43.
- a.
 - (1) State whether Mr. Spanos agrees that Kentucky-American intends to depreciate assets added to its system subsequent to the Commission's approval of the proposed depreciation study at a composite rate that corresponds with the life years cited at Item 43.
 - (2) If Mr. Spanos agrees, state whether Mr. Spanos also agrees that, for the assets listed in Item 43, the depreciation rates that he has calculated differ significantly from those included in Kentucky-American's last approved depreciation study.
 - b. For each account listed at Item 43, identify and explain why the net salvage and survivor curves that Mr. Spanos uses are more appropriate than those used in Kentucky-American's previously accepted depreciation study.

Response:

- a.
 - (1) The response to item 43 represents composite remaining lives of the existing or surviving assets as of December 31, 2006. These remaining lives change as time passes and plant vintages change. Therefore, the key component for new assets is the annual accrual rate. Thus, new assets will be depreciated at the composite annual accrual rate for each account as set forth on pages III-4 and III-5 column (8) of the depreciation study.
 - (2) Based on the response above that much has changed since the last approved depreciation study, I would expect to see quite a change from annual depreciation rates and the composite remaining lives shown on item 43.
- b. The net salvage percents and survivor curves set forth in Mr. Spanos' depreciation study are more appropriate than those currently in place for many reasons. First, the estimates include data through 2006, which is more current than estimates based on data prior to 1994. Second, current management plans and life expectancies of assets are reflected in the estimates proposed in this depreciation study. Third, current practices are incorporated in the 2006 study as compared to how things were done 12 years ago.

For electronic version, refer to KAW_R_PSCDR3#22_071607

KENTUCKY-AMERICAN WATER COMPANY
CASE NO. 2007-00143
COMMISSION STAFF'S THIRD
SET OF INFORMATION REQUESTS
Item 23 of 54

Witness: Michael Miller/John Spanos

23. Refer to Kentucky-American's Response to Attorney General's ("AG") First Set of Information Requests, Item 225. Explain why it is reasonable to permit recovery of removal costs if Kentucky-American has no "legal obligation" to remove the assets. The response should explain why removal of all asset groups included in the depreciation study with negative salvage is necessary and list and discuss all factors that indicate that Kentucky-American will actually incur the costs of removing those assets.

Response:

The Company interpreted the question AGDR1#225 to refer to the definition of a legal obligation contained in paragraph 2, page 1 of FAS 143 that says "a legal obligation that a party is required to settle as a result of an existing or enacted law, statute, ordinance, or written or oral contract or by legal construction of a contract under the doctrine of promissory estoppel." The company responded it had no asset retirement obligation that would be required by those terms.

The Company believes that the cost of removal to be incurred when its assets are retired in the normal course of its business meets the scope of FAS 143 and therefore it is required to comply with the provisions of FAS 143. The Company has an obligation to retire plant and property under NARUC accounting when it is no longer used and useful and record the costs of removing those assets (net of salvage) as cost of removal. Most regulatory commissions have recognized the future net negative salvage costs as a component of depreciation rates to be recovered over the average remaining service lives of the various utility plant accounts based on reasonable estimates of what those future net negative salvage costs will be. In fact the current depreciation rates of the Company were determined in this manner.

The Company has utilized an estimate of the net negative salvage included in its Commission approved depreciation rates to record the regulatory liability prescribed by FAS 143. The Company's books comply with U. S. GAAP (and FAS 143), but the Company believes its inclusion of the net negative salvage (ARO), shown as a regulatory liability on the financials but shown as accumulated depreciation for ratemaking purposes, is consistent and in compliance with the depreciation rates and methods historically approved by the Commission for the Company.

The Company is not certain what is meant by the second part of the question which asks for an explanation of why "removal of all asset groups included in the depreciation study

with net negative salvage is necessary.” The Company does not believe the asset group should be removed from the depreciation study because it has a net negative salvage component included in the depreciation rate calculation. The Company also does not believe that the net negative salvage component should be eliminated from the determination of the depreciation rates proposed in this case. The Company each year replaces utility plant that has reached the end of its useful life, or can no longer provide adequate service, and the Company has regular replacement programs for mains, meters, services, pumps and motors, etc. Please see the response to AGDR1#171 for the actual numbers for the last five years. In addition the depreciation study prepared by Mr. Spanos provides significant data on historical cost of removal and salvage. There is no doubt that removal costs for certain categories of assets will be incurred in the future when those assets are retired from service, and, as prescribed by NARUC accounting those removal costs will be recorded.

It is the practice of most regulatory commissions to provide for the future cost of removal associated with the retirement of those assets by allowing recovery in rates over the life of the asset. The reason that is the proper regulatory method is because it matches the return of that asset (including the cost to retire that asset) with the customer base utilizing that asset over its service life. If a reasonable estimate of the future cost of removal is not recovered over the life of the asset, then the removal cost of that asset will be borne by a group of customers who did not get the use of that asset. This is contrary to the matching principle and in the Company’s opinion would be poor regulatory policy.

For electronic version, refer to KAW_R_PSCDR3#23_071607.pdf

KENTUCKY-AMERICAN WATER COMPANY
CASE NO. 2007-00143
COMMISSION STAFF'S THIRD
SET OF INFORMATION REQUESTS
Item 24 of 54

Witness: Michael Miller

24.

- a. State the amounts accrued on the books of Kentucky-American for asset removal costs immediately prior to the implementation of Financial Accounting Standards Board ("FASB") Statement 143.
- b. Identify all accounts, on both sides of the balance sheet, to which the accrued amounts were recorded. State the amounts accrued to each account.
- c. Describe how the accrued amounts were determined. Show all calculations and state all assumptions used to determine the amounts.

Response:

- a. Prior to the implementation of FAS 143 there was no accrual of asset removal cost on the Company's books. The Company recorded depreciation expense (which includes the recovery of estimated cost of removal over the service life of its assets as approved by the Commission) with the offsetting credit to accumulated depreciation. The Company continues to report its depreciation expense and accumulated depreciation in this manner for ratemaking purposes as approved by the Commission. At the adoption of FAS 143 the Company reclassified accumulated depreciation of \$5,509,000 as of 12/31/03 to a regulatory liability-ARO/NNS in order to comply with U. S. GAAP and FAS 143.
- b. Account 108105 accumulated depreciation.
- c. Prior to adoption of FAS 143 there was no distinct calculation of the asset retirement obligation.

For electronic version, refer to KAW_R_PSCDR3#24_071607.pdf

KENTUCKY-AMERICAN WATER COMPANY
CASE NO. 2007-00143
COMMISSION STAFF'S THIRD
SET OF INFORMATION REQUESTS
Item 25 of 54

Witness: Michael Miller

25.

- a. State the amounts accrued on Kentucky-American's books to implement FASB Statement 143.
- b. Identify the accounts, on both sides of the balance sheet, to which the accrued amounts were recorded. State the amounts accrued to each account.
- c. Describe how the accrued amounts were determined. Show all calculations and state all assumptions used to determine the amounts.
- d. Explain what the accrued amounts represent.

Response:

- a. Please see the response to AGDR1#228, page 2 of 26. The first journal entry was the initial entry made to reclassify accumulated depreciation to Regulatory Liability-AR/NNS (account 256250) for U.S. GAAP financial statement presentation. This entry had no impact on the Company's earnings and is not presented in this manner for ratemaking purposes in compliance with the depreciation expense rates currently approved by the Commission.
- b. Please see the response above referencing the response to AGDR1#228, which provides the accounting entries to implement FAS143 and the balance sheet accounts impacted.
- c. Please see the response to AGDR1#228, which provides the calculations made to record the ARO/NNS through 2006 on the books of the Company and which also contains the worksheets used to arrive at those numbers.

For 2003, net negative salvage included in depreciation was calculated using each company's most recent depreciation study. That calculation was made using the percentage factor of net negative salvage as a percent of total gross utility plant in service and net salvage.

- d. The regulatory liability recorded for U.S. GAAP financial statement purposes represents the amount of Net Negative Salvage recovered in rates (less the net negative salvage actually spent) which the Company will be required to spend funds for at the future retirement date of its utility plant assets that remain in service.

For electronic version, refer to KAW_R_PSCDR3#25_071607.pdf

KENTUCKY-AMERICAN WATER COMPANY
CASE NO. 2007-00143
COMMISSION STAFF'S THIRD
SET OF INFORMATION REQUESTS
Item 26 of 54

Witness: Michael Miller

26. a. State the amount accrued on Kentucky-American's books related to asset removal costs as of December 31, 2006.
- b. Provide the general ledger pages that show the accrued amounts for all accounts on both sides of the balance sheet.
- c. Describe how the accrued amounts were determined. Show all calculations and state all assumptions used to determine the amounts.

Response:

- a. The Reg. Liability for Asset Removal Costs as of 12/31/06 is \$7,597,007.36.
- b. Please see attached documents.
- c. The Regulatory Liability is calculated by using the PSC approved Cost of Removal Rate multiplied by the amount of Depreciation recorded. This calculation is performed by Plant account. A/C 108-Accumulated Depreciation is Debited and the credit goes to the Reg. Liability for A/C 256-Asset Removal Costs.

Actual removal is actual charges (Invoices, Labor, Inventory, etc) for removing/retiring Plant. Actual Removal Costs are accumulated in A/C 185-RWIP and transferred to A/C 256 when the asset is retired.

Please see the response and attachments to AGDR1#228 for the detailed calculations and annual accumulations of the journal entries recorded.

For electronic version, refer to KAW_R_PSCDR3#26_071607.pdf

American Water Works Company
Account 256250 December Activity
NNS Reg Liability

Page Date - 7/13/07
From Date - 12/10/05
Thru Date - 12/31/06

G/L Account	Account Description	Do Document	G/L Date	Co.	Debit	Amounts	Credit	Current Balance	LT	P
120105.256250	Reg Liab-ARO/NN			00012						
	Balance Forward		12/31/06				6,560,981.16			P
	Net Negative Salvage	NS	12/31/06				1,028.30			P
	Net Negative Salvage	NS	12/31/06				2,223.77			P
	Net Negative Salvage	NS	12/31/06				2,199.35			P
	Net Negative Salvage	NS	12/31/06				15,174.95			P
	Net Negative Salvage	NS	12/31/06				3,655.55			P
	Net Negative Salvage	NS	12/31/06				31.07			P
	Net Negative Salvage	NS	12/31/06				75,886.35			P
	Net Negative Salvage	NS	12/31/06		1,936.95	5.28				P
	Net Negative Salvage	NS	12/31/06			70.56				P
	Net Negative Salvage	NS	12/31/06			72.87				P
	Net Negative Salvage	NS	12/31/06			696.30				P
	Net Negative Salvage	NS	12/31/06			30.42				P
	Net Negative Salvage	NS	12/31/06			4,799.65				P
	Net Negative Salvage	NS	12/31/06			1,732.60				P
	Net Negative Salvage	NS	12/31/06			569.27				P
	Net Negative Salvage	NS	12/31/06			1,486.70				P
	Dec 2006 Clear Remov	F7	12/28/06		12,937.40		244.29			P
	Clear Removal & Salv	F7	12/28/06							P
	Dec 2006 Clear Remov	F7	12/28/06		1,101.66					P
	Clear Removal & Salv	F7	12/28/06							P
	Dec 2006 Clear Remov	F7	12/28/06		3,722.01					P
	Clear Removal & Salv	F7	12/28/06							P
	Dec 2006 Clear Remov	F7	12/28/06		316.05					P
	Clear Removal & Salv	F7	12/28/06							P
	Dec 2006 Clear Remov	F7	12/28/06		675.00					P
	Clear Removal & Salv	F7	12/28/06							P
	Dec 2006 Clear Remov	F7	12/28/06		149.44					P
	Clear Removal & Salv	F7	12/28/06							P
	Dec 2006 Clear Remov	F7	12/28/06		769.00					P
	Clear Removal & Salv	F7	12/28/06							P
	Dec 2006 Clear Remov	F7	12/28/06		101.92					P
	Clear Removal & Salv	F7	12/28/06							P
	Dec 2006 Clear Remov	F7	12/28/06		2,700.00					P
	Clear Removal & Salv	F7	12/28/06							P
	Dec 2006 Clear Remov	F7	12/28/06		179.03					P
	Clear Removal & Salv	F7	12/28/06							P
	Dec 2006 Clear Remov	F7	12/28/06		97.63					P
	Clear Removal & Salv	F7	12/28/06							P
	Dec 2006 Clear Remov	F7	12/28/06		239.76					P
	Clear Removal & Salv	F7	12/28/06							P
	Dec 2006 Clear Remov	F7	12/28/06		480.55					P

American Water Works Company
Account 256250 December Activity
NNS Reg Liability

Page Date - 7/13/07
From Date - 12/10/05
Thru Date - 12/31/06

G/L Account	Account Description	Do Document	G/L Date	Co.	Debit	Amounts	Credit	Current Balance	LT	P
120105.256250	Reg Liab-ARO/NN			00012						
	Nov 2006 Clear Remov & Salv	F7 30733382	11/30/06		574.10				AA	P
	Nov 2006 Clear Remov & Salv	F7 30733382	11/30/06				848.00-		AA	P
	Nov 2006 Clear Remov & Salv	F7 30733382	11/30/06				598.00-		AA	P
	Nov 2006 Clear Remov & Salv	F7 30733382	11/30/06				1,098.00-		AA	P
	Nov 2006 Clear Remov & Salv	F7 30733382	11/30/06				798.00-		AA	P
	Nov 2006 Clear Remov & Salv	F7 30733382	11/30/06				1,998.00-		AA	P
	Nov 2006 Clear Remov & Salv	F7 30733382	11/30/06				1,098.00-		AA	P
	Nov 2006 Clear Remov & Salv	F7 30733382	11/30/06				1,198.00-		AA	P
	Nov 2006 Clear Remov & Salv	F7 30733382	11/30/06				2,298.00-		AA	P
	Nov 2006 Clear Remov & Salv	F7 30733382	11/30/06				1,898.00-		AA	P
	Period Totals				28,597.49		134,309.42-			
	Oct 2006 Clear Remov & S	F7 30710620	10/27/06		2,849.52				AA	P
	Oct 2006 Clear Remov & S	F7 30710620	10/27/06		1,911.78				AA	P
	Oct 2006 Clear Remov & S	F7 30710620	10/27/06		2,122.80				AA	P
	Oct 2006 Clear Remov & S	F7 30710620	10/27/06				25.00-		AA	P
	Oct 2006 Clear Remov & S	F7 30710620	10/27/06		1,048.04				AA	P
	Oct 2006 Clear Remov & S	F7 30710620	10/27/06				100.00-		AA	P
	Oct 2006 Clear Remov & S	F7 30710620	10/27/06		420.73				AA	P
	Net Negative Salvage	NS 30710934	10/27/06				838.78-		AA	P
	Net Negative Salvage	NS 30710934	10/27/06				1,170.02-		AA	P
	Net Negative Salvage	NS 30710934	10/27/06				223.77-		AA	P
	Net Negative Salvage	NS 30710934	10/27/06				2,194.05-		AA	P
	Net Negative Salvage	NS 30710934	10/27/06				136.36-		AA	P
	Net Negative Salvage	NS 30710934	10/27/06				14,165.75-		AA	P
	Net Negative Salvage	NS 30710934	10/27/06				1,715.69-		AA	P
	Net Negative Salvage	NS 30710934	10/27/06				5,570.21-		AA	P
	Net Negative Salvage	NS 30710934	10/27/06				75.33-		AA	P
	Net Negative Salvage	NS 30710934	10/27/06				31.34-		AA	P
	Net Negative Salvage	NS 30710934	10/27/06				74,867.41-		AA	P
	Net Negative Salvage	NS 30710934	10/27/06		1,708.54				AA	P
	Net Negative Salvage	NS 30710934	10/27/06				10,594.56-		AA	P

American Water Works Company
Account 256250 December Activity
NNS Reg Liability

Page Date - 7/13/07
From Date - 12/10/05
Thru Date - 12/31/06

G/L Account	Account Description	Do Document	G/L Date	Co.	Debit	Credit	Current Balance	LT	P
120105.256250	Reg Liab-ARO/NN			00012					
	Net Negative Salvage	NS 30710934	10/27/06		70.54	5,698.20		AA	P
	Net Negative Salvage	NS 30710934	10/27/06		49.83			AA	P
	Net Negative Salvage	NS 30710934	10/27/06		3,042.92			AA	P
	Net Negative Salvage	NS 30710934	10/27/06		694.47			AA	P
	Net Negative Salvage	NS 30710934	10/27/06		29.32			AA	P
	Net Negative Salvage	NS 30710934	10/27/06		1,738.33			AA	P
	Net Negative Salvage	NS 30710934	10/27/06		1,600.18			AA	P
	Net Negative Salvage	NS 30710934	10/27/06		1,513.96			AA	P
	Net Negative Salvage	NS 30710934	10/27/06		1,486.70	194.38		AA	P
	Period Totals				21,288.50	117,601.10			
	Net Negative Salvage	NS 30652930	09/25/06		833.98			AA	P
	Net Negative Salvage	NS 30652930	09/25/06		1,173.14			AA	P
	Net Negative Salvage	NS 30652930	09/25/06		2,194.39			AA	P
	Net Negative Salvage	NS 30652930	09/25/06		14,116.36			AA	P
	Net Negative Salvage	NS 30652930	09/25/06		1,715.69			AA	P
	Net Negative Salvage	NS 30652930	09/25/06		5,538.70			AA	P
	Net Negative Salvage	NS 30652930	09/25/06		75.33			AA	P
	Net Negative Salvage	NS 30652930	09/25/06		31.19			AA	P
	Net Negative Salvage	NS 30652930	09/25/06		74,424.02			AA	P
	Net Negative Salvage	NS 30652930	09/25/06		1.91			AA	P
	Net Negative Salvage	NS 30652930	09/25/06		1,702.55			AA	P
	Net Negative Salvage	NS 30652930	09/25/06		70.54			AA	P
	Net Negative Salvage	NS 30652930	09/25/06		49.83			AA	P
	Net Negative Salvage	NS 30652930	09/25/06		3,042.92			AA	P
	Net Negative Salvage	NS 30652930	09/25/06		694.47			AA	P
	Net Negative Salvage	NS 30652930	09/25/06		29.32			AA	P
	Net Negative Salvage	NS 30652930	09/25/06		1,738.33			AA	P
	Net Negative Salvage	NS 30652930	09/25/06		1,610.66			AA	P
	Net Negative Salvage	NS 30652930	09/25/06		1,513.96			AA	P
	Net Negative Salvage	NS 30652930	09/25/06		1,486.70	194.38		AA	P
	Net Negative Salvage	NS 30652930	09/25/06		674.18			AA	P
	Clear 2006 Removal &	F7 30655524	09/28/06		6,437.87			AA	P
	Clear 2006 Removal &	F7 30655524	09/28/06		5,881.89			AA	P
	Clear 2006 Removal &	F7 30655524	09/28/06		89.70			AA	P
	Clear 2006 Removal &	F7 30655524	09/28/06		13,682.00			AA	P
	Clear 2006 Removal &	F7 30655524	09/28/06		39,706.85	116,917.24			
	Period Totals								

G/L Account	Account Description	Do Document	G/L Date	Co.	Debit	Amounts	Credit	Current Balance	LT	P	C
120105.256250	Reg Liab-ARO/NN			00012							
	Net Negative Salvage	NS 30628419	08/25/06				781.83		AA	P	
	Net Negative Salvage	NS 30628419	08/25/06				1,172.35		AA	P	
	Net Negative Salvage	NS 30628419	08/25/06				2,233.77		AA	P	
	Net Negative Salvage	NS 30628419	08/25/06				2,134.34		AA	P	
	Net Negative Salvage	NS 30628419	08/25/06				14,115.69		AA	P	
	Net Negative Salvage	NS 30628419	08/25/06				1,683.48		AA	P	
	Net Negative Salvage	NS 30628419	08/25/06				5,514.16		AA	P	
	Net Negative Salvage	NS 30628419	08/25/06				31.05		AA	P	
	Net Negative Salvage	NS 30628419	08/25/06				73,496.11		AA	P	
	Net Negative Salvage	NS 30628419	08/25/06		1,675.13	2.43			AA	P	
	Net Negative Salvage	NS 30628419	08/25/06		70.54	49.83			AA	P	
	Net Negative Salvage	NS 30628419	08/25/06		3,042.02	694.25			AA	P	
	Net Negative Salvage	NS 30628419	08/25/06		229.34	238.33			AA	P	
	Net Negative Salvage	NS 30628419	08/25/06		1,613.96	513.96			AA	P	
	Net Negative Salvage	NS 30628419	08/25/06		1,486.53	250.91	158.56		AA	P	
	Clear Removal & S	F7 30624645	08/24/06		19,715.97				AA	P	
	Clear Removal & S	F7 30624645	08/24/06		2,860.66				AA	P	
	Clear Removal & S	F7 30624645	08/24/06		73.95				AA	P	
	Clear Removal & S	F7 30624645	08/24/06				788.00		AA	P	
	Clear Removal & S	F7 30624645	08/24/06		295.69				AA	P	
	Clear Removal & S	F7 30624645	08/24/06		295.69				AA	P	
	Period Totals				42,405.89		116,455.06				
	Net Negative Salvage	NS 30543047	07/28/06				781.83		AA	P	
	Net Negative Salvage	NS 30543047	07/28/06				1,169.35		AA	P	
	Net Negative Salvage	NS 30543047	07/28/06				2,233.77		AA	P	
	Net Negative Salvage	NS 30543047	07/28/06				2,134.34		AA	P	
	Net Negative Salvage	NS 30543047	07/28/06				14,115.69		AA	P	
	Net Negative Salvage	NS 30543047	07/28/06				1,683.48		AA	P	
	Net Negative Salvage	NS 30543047	07/28/06				5,504.02		AA	P	
	Net Negative Salvage	NS 30543047	07/28/06				75.33		AA	P	

Account Explanation	G/L Account	Do Document	G/L Date	Co.	Debit	Amounts	Credit	Current Balance	LT	P	C
120105:256250				00012							
Reg Liab - ARO/NN											
Net Negative Salvage		NS	305433047					31.05-	AA	P	
Net Negative Salvage		NS	305433047					19-	AA	P	
Net Negative Salvage		NS	305433047				72,932.68-		AA	P	
Net Negative Salvage		NS	305433047		1,672.92	3.18			AA	P	
Net Negative Salvage		NS	305433047				10,359.19-		AA	P	
Net Negative Salvage		NS	305433047				5,576.03-		AA	P	
Net Negative Salvage		NS	305433047		70.34				AA	P	
Net Negative Salvage		NS	305433047		49.83				AA	P	
Net Negative Salvage		NS	305433047		3,015.56				AA	P	
Net Negative Salvage		NS	305433047		694.25				AA	P	
Net Negative Salvage		NS	305433047		29.34				AA	P	
Net Negative Salvage		NS	305433047		3,738.33				AA	P	
Net Negative Salvage		NS	305433047		1,610.66				AA	P	
Net Negative Salvage		NS	305433047		513.96				AA	P	
Net Negative Salvage		NS	305433047		1,486.53		157.88-		AA	P	
Clear Removal & Salv		F7	305422340		1,108.07				AA	P	
Clear Removal & Salv		F7	305422340		994.40				AA	P	
Clear Removal & Salv		F7	305422340		3,669.56				AA	P	
Clear Removal & Salv		F7	305422340		591.33				AA	P	
Clear Removal & Salv		F7	305422340		221.81				AA	P	
Clear Removal & Salv		F7	305422340		1,478.40				AA	P	
Clear Removal & Salv		F7	305422340		73.91				AA	P	
Period Totals					21,022.48		114,968.10-				
June 2006 Removal & Clear		F7	30533409		2,984.91				AA	P	
June 2006 Removal & Clear		F7	30533409		6,167.26				AA	P	
June 2006 Removal & Clear		F7	30533409		3,926.43				AA	P	
June 2006 Removal & Clear		F7	30533409				24.60-		AA	P	
June 2006 Removal & Clear		F7	30533409		132.30				AA	P	
June 2006 Removal & Clear		F7	30533409		354.48				AA	P	
June 2006 Removal & Clear		F7	30533409				700.00-		AA	P	
June 2006 Removal & Clear		F7	30533409		3,600.00				AA	P	
June 2006 Removal & Clear		F7	30533409		721.12				AA	P	

Account Description	Do Document	G/L Date	Co.	Debit	Amounts	Credit	Current Balance	LT	P
Reg Liab-ARO/NN			00012						
June 2006 Removal & Clear	F7 30533409	06/30/06		1,318.00				AA	P
June 2006 Removal & Clear	F7 30533409	06/30/06		57,600.00				AA	P
June 2006 Removal & Clear	F7 30533409	06/30/06		631.61				AA	P
June 2006 Removal & Clear	F7 30533409	06/30/06				1,060.00		AA	P
June 2006 Removal & Clear	F7 30533409	06/30/06				781.83		AA	P
Net Negative Salvage	NS 30533672	06/30/06				1,149.96		AA	P
Net Negative Salvage	NS 30533672	06/30/06				2,223.77		AA	P
Net Negative Salvage	NS 30533672	06/30/06				14,165.69		AA	P
Net Negative Salvage	NS 30533672	06/30/06				1,683.01		AA	P
Net Negative Salvage	NS 30533672	06/30/06				31.05		AA	P
Net Negative Salvage	NS 30533672	06/30/06				72,570.19		AA	P
Net Negative Salvage	NS 30533672	06/30/06		1,642.06				AA	P
Net Negative Salvage	NS 30533672	06/30/06				10,299.82		AA	P
Net Negative Salvage	NS 30533672	06/30/06				5,516.89		AA	P
Net Negative Salvage	NS 30533672	06/30/06				70.34		AA	P
Net Negative Salvage	NS 30533672	06/30/06				49.83		AA	P
Net Negative Salvage	NS 30533672	06/30/06				1,015.66		AA	P
Net Negative Salvage	NS 30533672	06/30/06				694.25		AA	P
Net Negative Salvage	NS 30533672	06/30/06				29.34		AA	P
Net Negative Salvage	NS 30533672	06/30/06				1,738.33		AA	P
Net Negative Salvage	NS 30533672	06/30/06				1,610.66		AA	P
Net Negative Salvage	NS 30533672	06/30/06				157.88		AA	P
Net Negative Salvage	NS 30533672	06/30/06		1,480.49				AA	P
Period Totals				90,284.23		116,199.73			
Net Negative Salvage	NS 30266228	05/26/06				781.83		AA	P
Net Negative Salvage	NS 30266228	05/26/06				1,149.96		AA	P
Net Negative Salvage	NS 30266228	05/26/06				2,223.77		AA	P
Net Negative Salvage	NS 30266228	05/26/06				14,165.69		AA	P
Net Negative Salvage	NS 30266228	05/26/06				1,682.97		AA	P
Net Negative Salvage	NS 30266228	05/26/06				5,395.30		AA	P
Net Negative Salvage	NS 30266228	05/26/06				31.05		AA	P
Net Negative Salvage	NS 30266228	05/26/06				72,066.27		AA	P
Net Negative Salvage	NS 30266228	05/26/06				3.20		AA	P

G/L Account	Account Description	DO	Document	G/L	Co.	Debit	Credit	Current Balance	LT	P
120105.256250	Reg Liab ARO/NN	NS	302562228	05/25/06	00012	1,642.58			AA	P
	Net Negative Salvage	NS	302562228	05/25/06			10,232.14		AA	P
	Net Negative Salvage	NS	302562228	05/25/06			5,416.36		AA	P
	Net Negative Salvage	NS	302562228	05/25/06		70.34			AA	P
	Net Negative Salvage	NS	302562228	05/25/06		49.83			AA	P
	Net Negative Salvage	NS	302562228	05/25/06		3,015.66			AA	P
	Net Negative Salvage	NS	302562228	05/25/06		687.26			AA	P
	Net Negative Salvage	NS	302562228	05/25/06		29.34			AA	P
	Net Negative Salvage	NS	302562228	05/25/06		3,738.33			AA	P
	Net Negative Salvage	NS	302562228	05/25/06		1,610.66			AA	P
	Net Negative Salvage	NS	302562228	05/25/06		513.96			AA	P
	Net Negative Salvage	NS	302562228	05/25/06		1,480.49		155.69	AA	P
	Net Negative Salvage	NS	302562228	05/25/06		554.92			AA	P
	Clear Removal & S	F7	3025632	05/25/06		1,845.17			AA	P
	Clear Removal & S	F7	3025632	05/25/06		9,466.74			AA	P
	Clear Removal & S	F7	3025632	05/25/06		1,545.00			AA	P
	Clear Removal & S	F7	3025632	05/25/06		444.33			AA	P
	Clear Removal & S	F7	3025632	05/25/06		222.18			AA	P
	Clear Removal & S	F7	3025632	05/25/06			8,030.00		AA	P
	Clear Removal & S	F7	3025632	05/25/06		67.91			AA	P
	Clear Removal & S	F7	3025632	05/25/06					AA	P
	Period Totals					26,987.90	121,706.12			
	Net Negative Salvage	NS	30257947	04/11/06			781.83		AA	P
	Net Negative Salvage	NS	30257947	04/11/06			1,149.96		AA	P
	Net Negative Salvage	NS	30257947	04/11/06			223.77		AA	P
	Net Negative Salvage	NS	30257947	04/11/06			2,192.47		AA	P
	Net Negative Salvage	NS	30257947	04/11/06			113.02		AA	P
	Net Negative Salvage	NS	30257947	04/11/06			14,171.50		AA	P
	Net Negative Salvage	NS	30257947	04/11/06			1,626.46		AA	P
	Net Negative Salvage	NS	30257947	04/11/06			5,374.57		AA	P
	Net Negative Salvage	NS	30257947	04/11/06			75.33		AA	P
	Net Negative Salvage	NS	30257947	04/11/06			31.05		AA	P
	Net Negative Salvage	NS	30257947	04/11/06			19		AA	P
	Net Negative Salvage	NS	30257947	04/11/06			71,287.31		AA	P
	Net Negative Salvage	NS	30257947	04/11/06		3.20			AA	P
	Net Negative Salvage	NS	30257947	04/11/06		1,644.39			AA	P
	Net Negative Salvage	NS	30257947	04/11/06			10,159.68		AA	P
	Net Negative Salvage	NS	30257947	04/11/06			5,374.08		AA	P
	Net Negative Salvage	NS	30257947	04/11/06		70.34			AA	P
	Net Negative Salvage	NS	30257947	04/11/06		49.83			AA	P
	Net Negative Salvage	NS	30257947	04/11/06		3,008.34			AA	P
	Net Negative Salvage	NS	30257947	04/11/06		687.26			AA	P

09421

American Water Works Company
Account 256250 December Activity
NNS Reg Liability

Page Date - 7/13/07
From Date - 12/10/95
Thru Date - 12/31/06

G/L Account	Account Description	Do Document	G/L Date	Co.	Debit	Amounts	Credit	Current Balance	LT P	C
120105.256250	Reg Liab-ARO/NN			00012						
	Company Totals	- Posted			397,288.21		7,999,462.58	7,602,174.37		
		- Unposted								
	Total	- Posted			397,288.21		7,999,462.58	7,602,174.37		
		- Unposted								

+ entries on
next page

[09200] - Account Ledger Inquiry

Functions Options Tools Help

Account: 3201351253250 From Date/Period: 01/21/06
 Reg Liab-RAO/NHS Thru Date/Period: 02/17/06
 Ledger Type: RA
 Subledger: F

Skip to Doc/Type: _____
 Y-T-D Period End: 173,459 66-
 Cumul Period End: 6,734,440 82-

Additional Selections Exist

DT	Document	Date	Explanation	Debit	Credit	P
F7	30246943	02/03/06	FASTA - FINANCIAL	326 64		P
F7	30246943	02/03/06	FASTA - FINANCIAL	203 00		P
F7	30246943	02/03/06	FASTA - FINANCIAL	172 32		P
F7	30246943	02/03/06	FASTA - FINANCIAL	172 32		P
F7	30246943	02/03/06	FASTA - FINANCIAL	203 00		P
F7	30246943	02/03/06	FASTA - FINANCIAL	100 06		P
F7	30246943	02/03/06	FASTA - FINANCIAL	661 93		P
F7	30246943	02/03/06	FASTA - FINANCIAL	309 20		P
F7	30246943	02/03/06	FASTA - FINANCIAL	273 53		P
F7	30246943	02/03/06	FASTA - FINANCIAL	1,746 48		P
F7	30246943	02/03/06	FASTR - FINANCIAL	997 73		P
NS	30247106	02/06/06	Net Negative Salva	1,400 49		P
NS	30247106	02/06/06	Net Negative Salva		138 31-	P
NS	30247106	02/06/06	Net Negative Salva	513.96		P

5167.01

Opt: 1/2=Orig Entry 5=Details F17=Top F18=Totals F21=Prnt Ldg F24=More MW

G/L Account	Account Description	Do Document	G/L Date	Co.	Debit	Amounts	Credit	Current Balance	LT	P	C
120105.108105	AD UPIS-Acc Dep			00012							
	Net Negative Salvage	NS 30734129	12/01/06			204.35	1,600.18	1,600.18	AA	P	P
	Net Negative Salvage	NS 30734129	12/01/06				513.96	513.96	AA	P	P
	Net Negative Salvage	NS 30734129	12/01/06				1,486.70	1,486.70	AA	P	P
	Period Totals				118,042.91		12,942.07				
	Net Negative Salvage	NS 30710934	10/27/06		938.78				AA	P	P
	Net Negative Salvage	NS 30710934	10/27/06		1,170.02				AA	P	P
	Net Negative Salvage	NS 30710934	10/27/06		2,223.77				AA	P	P
	Net Negative Salvage	NS 30710934	10/27/06		2,194.05				AA	P	P
	Net Negative Salvage	NS 30710934	10/27/06		1,336.36				AA	P	P
	Net Negative Salvage	NS 30710934	10/27/06		14,165.75				AA	P	P
	Net Negative Salvage	NS 30710934	10/27/06		1,715.69				AA	P	P
	Net Negative Salvage	NS 30710934	10/27/06		5,570.21				AA	P	P
	Net Negative Salvage	NS 30710934	10/27/06		75.33				AA	P	P
	Net Negative Salvage	NS 30710934	10/27/06		31.34				AA	P	P
	Net Negative Salvage	NS 30710934	10/27/06		74,867.41				AA	P	P
	Net Negative Salvage	NS 30710934	10/27/06				1,708.84	1,708.84	AA	P	P
	Net Negative Salvage	NS 30710934	10/27/06		10,594.56				AA	P	P
	Net Negative Salvage	NS 30710934	10/27/06		5,698.20				AA	P	P
	Net Negative Salvage	NS 30710934	10/27/06				70.54	70.54	AA	P	P
	Net Negative Salvage	NS 30710934	10/27/06				49.83	49.83	AA	P	P
	Net Negative Salvage	NS 30710934	10/27/06				3,042.92	3,042.92	AA	P	P
	Net Negative Salvage	NS 30710934	10/27/06				694.47	694.47	AA	P	P
	Net Negative Salvage	NS 30710934	10/27/06				29.32	29.32	AA	P	P
	Net Negative Salvage	NS 30710934	10/27/06				3,738.33	3,738.33	AA	P	P
	Net Negative Salvage	NS 30710934	10/27/06				1,600.18	1,600.18	AA	P	P
	Net Negative Salvage	NS 30710934	10/27/06				513.96	513.96	AA	P	P
	Net Negative Salvage	NS 30710934	10/27/06		194.38				AA	P	P
	Period Totals				117,476.10		12,935.63				
	Net Negative Salvage	NS 30662930	09/29/06		833.98				AA	P	P
	Net Negative Salvage	NS 30662930	09/29/06		1,173.14				AA	P	P
	Net Negative Salvage	NS 30662930	09/29/06		2,223.77				AA	P	P
	Net Negative Salvage	NS 30662930	09/29/06		2,194.39				AA	P	P
	Net Negative Salvage	NS 30662930	09/29/06		1,336.36				AA	P	P
	Net Negative Salvage	NS 30662930	09/29/06		14,165.75				AA	P	P
	Net Negative Salvage	NS 30662930	09/29/06		1,715.69				AA	P	P
	Net Negative Salvage	NS 30662930	09/29/06		5,538.70				AA	P	P
	Net Negative Salvage	NS 30662930	09/29/06		75.33				AA	P	P
	Net Negative Salvage	NS 30662930	09/29/06		31.05				AA	P	P
	Net Negative Salvage	NS 30662930	09/29/06		74,424.02				AA	P	P
	Net Negative Salvage	NS 30662930	09/29/06				1.91	1.91	AA	P	P
	Net Negative Salvage	NS 30662930	09/29/06		10,549.87				AA	P	P
	Net Negative Salvage	NS 30662930	09/29/06		5,660.62				AA	P	P

American Water Works Company
Account 108105
December Activity
NNS Accum Depreciation

Page Date - 7/13/07
From Date - 12/10/05
Thru Date - 12/31/06

Account Description	DO	Document	G/L	Co.	Debit	Amounts	Credit	Current Balance	LT	P	C
AD UPIS-ACC Dep	NS	306663330	09/29/06	00012							
Net Negative Salvage	NS	306663330	09/29/06				70.54-		AA		P
Net Negative Salvage	NS	306663330	09/29/06				49.83-		AA		P
Net Negative Salvage	NS	306663330	09/29/06				3,042.32-		AA		P
Net Negative Salvage	NS	306663330	09/29/06				694.34-		AA		P
Net Negative Salvage	NS	306663330	09/29/06				2,738.33-		AA		P
Net Negative Salvage	NS	306663330	09/29/06				1,610.66-		AA		P
Net Negative Salvage	NS	306663330	09/29/06				513.96-		AA		P
Net Negative Salvage	NS	306663330	09/29/06		194.38			1,486.70-	AA		P
Period Totals					116,917.24		12,941.21-				
Net Negative Salvage	NS	3062284119	08/23/06		781.83				AA		P
Net Negative Salvage	NS	3062284119	08/23/06		223.77				AA		P
Net Negative Salvage	NS	3062284119	08/23/06		2,134.34				AA		P
Net Negative Salvage	NS	3062284119	08/23/06		14,183.48				AA		P
Net Negative Salvage	NS	3062284119	08/23/06		5,175.33				AA		P
Net Negative Salvage	NS	3062284119	08/23/06		31.05				AA		P
Net Negative Salvage	NS	3062284119	08/23/06		73,496.11				AA		P
Net Negative Salvage	NS	3062284119	08/23/06				1,675.13-		AA		P
Net Negative Salvage	NS	3062284119	08/23/06		10,447.64				AA		P
Net Negative Salvage	NS	3062284119	08/23/06		5,584.80				AA		P
Net Negative Salvage	NS	3062284119	08/23/06				70.54-		AA		P
Net Negative Salvage	NS	3062284119	08/23/06				49.83-		AA		P
Net Negative Salvage	NS	3062284119	08/23/06				3,042.02-		AA		P
Net Negative Salvage	NS	3062284119	08/23/06				694.34-		AA		P
Net Negative Salvage	NS	3062284119	08/23/06				2,738.33-		AA		P
Net Negative Salvage	NS	3062284119	08/23/06				1,610.66-		AA		P
Net Negative Salvage	NS	3062284119	08/23/06		158.56			1,486.53-	AA		P
Period Totals					115,667.06		12,913.02-				
Net Negative Salvage	NS	30543047	07/28/06		781.83				AA		P
Net Negative Salvage	NS	30543047	07/28/06		223.77				AA		P
Net Negative Salvage	NS	30543047	07/28/06		2,134.34				AA		P
Net Negative Salvage	NS	30543047	07/28/06		14,183.02				AA		P
Net Negative Salvage	NS	30543047	07/28/06		1,683.73				AA		P
Net Negative Salvage	NS	30543047	07/28/06		5,594.02				AA		P
Net Negative Salvage	NS	30543047	07/28/06		31.05				AA		P

American Water Works Company
Account 108105 December Activity
NNS Accum Depreciation

Page Date - 7/13/07
From Date - 12/10/05
Thru Date - 12/31/06

G/L Account	Account Description	DO Ty	Document	G/L Date	Co.	Debit	Amounts	Credit	Current Balance	LT	C
120105.108105	AD PPS-ACC Dep	NS	30543047	07/28/06	00012					AA	P
	Net Negative Salvage	NS	30543047	07/28/06		72,932.68				AA	P
	Net Negative Salvage	NS	30543047	07/28/06				1,672.92	3.18-	AA	P
	Net Negative Salvage	NS	30543047	07/28/06						AA	P
	Net Negative Salvage	NS	30543047	07/28/06		10,358.19				AA	P
	Net Negative Salvage	NS	30543047	07/28/06		5,576.03				AA	P
	Net Negative Salvage	NS	30543047	07/28/06				70.34-		AA	P
	Net Negative Salvage	NS	30543047	07/28/06				49.83-		AA	P
	Net Negative Salvage	NS	30543047	07/28/06				3,015.66-		AA	P
	Net Negative Salvage	NS	30543047	07/28/06				694.25-		AA	P
	Net Negative Salvage	NS	30543047	07/28/06				29.34-		AA	P
	Net Negative Salvage	NS	30543047	07/28/06				3,738.33-		AA	P
	Net Negative Salvage	NS	30543047	07/28/06				1,610.66-		AA	P
	Net Negative Salvage	NS	30543047	07/28/06		157.88				AA	P
	Net Negative Salvage	NS	30543047	07/28/06				1,486.53-		AA	P
	Period Totals					114,968.10		12,885.00-			
	Net Negative Salvage	NS	30533672	05/30/06						AA	P
	Net Negative Salvage	NS	30533672	06/30/06		1,193.96				AA	P
	Net Negative Salvage	NS	30533672	06/30/06		2,132.47				AA	P
	Net Negative Salvage	NS	30533672	06/30/06						AA	P
	Net Negative Salvage	NS	30533672	06/30/06		14,165.69				AA	P
	Net Negative Salvage	NS	30533672	06/30/06		1,633.93				AA	P
	Net Negative Salvage	NS	30533672	06/30/06		5,475.33				AA	P
	Net Negative Salvage	NS	30533672	06/30/06				31.05		AA	P
	Net Negative Salvage	NS	30533672	06/30/06		72,570.19				AA	P
	Net Negative Salvage	NS	30533672	06/30/06				3.20-		AA	P
	Net Negative Salvage	NS	30533672	06/30/06				1,642.06-		AA	P
	Net Negative Salvage	NS	30533672	06/30/06						AA	P
	Net Negative Salvage	NS	30533672	06/30/06		10,299.82				AA	P
	Net Negative Salvage	NS	30533672	06/30/06		5,516.89				AA	P
	Net Negative Salvage	NS	30533672	06/30/06				70.34-		AA	P
	Net Negative Salvage	NS	30533672	06/30/06				49.83-		AA	P
	Net Negative Salvage	NS	30533672	06/30/06				3,015.66-		AA	P
	Net Negative Salvage	NS	30533672	06/30/06				694.25-		AA	P
	Net Negative Salvage	NS	30533672	06/30/06				29.34-		AA	P
	Net Negative Salvage	NS	30533672	06/30/06				3,738.33-		AA	P
	Net Negative Salvage	NS	30533672	06/30/06				1,610.66-		AA	P
	Net Negative Salvage	NS	30533672	06/30/06		157.88				AA	P
	Net Negative Salvage	NS	30533672	06/30/06				1,480.49-		AA	P
	Period Totals					114,415.13		12,848.12-			
	Net Negative Salvage	NS	30266228	05/26/06						AA	P
	Net Negative Salvage	NS	30266228	05/26/06		1,193.96				AA	P
	Net Negative Salvage	NS	30266228	05/26/06		2,232.77				AA	P
	Net Negative Salvage	NS	30266228	05/26/06						AA	P
	Net Negative Salvage	NS	30266228	05/26/06		14,165.69				AA	P
	Net Negative Salvage	NS	30266228	05/26/06		1,633.93				AA	P
	Net Negative Salvage	NS	30266228	05/26/06		5,475.33				AA	P
	Net Negative Salvage	NS	30266228	05/26/06				31.05		AA	P
	Net Negative Salvage	NS	30266228	05/26/06		72,570.19				AA	P
	Net Negative Salvage	NS	30266228	05/26/06				3.20-		AA	P
	Net Negative Salvage	NS	30266228	05/26/06				1,642.06-		AA	P
	Net Negative Salvage	NS	30266228	05/26/06						AA	P
	Net Negative Salvage	NS	30266228	05/26/06		10,299.82				AA	P
	Net Negative Salvage	NS	30266228	05/26/06		5,516.89				AA	P
	Net Negative Salvage	NS	30266228	05/26/06				70.34-		AA	P
	Net Negative Salvage	NS	30266228	05/26/06				49.83-		AA	P
	Net Negative Salvage	NS	30266228	05/26/06				3,015.66-		AA	P
	Net Negative Salvage	NS	30266228	05/26/06				694.25-		AA	P
	Net Negative Salvage	NS	30266228	05/26/06				29.34-		AA	P
	Net Negative Salvage	NS	30266228	05/26/06				3,738.33-		AA	P
	Net Negative Salvage	NS	30266228	05/26/06				1,610.66-		AA	P
	Net Negative Salvage	NS	30266228	05/26/06		157.88				AA	P
	Net Negative Salvage	NS	30266228	05/26/06				1,480.49-		AA	P
	Period Totals					114,415.13		12,848.12-			

G/L Account	Account Description	Explanation	DO	Document	G/L Date	Co.	Debit	Amounts	Credit	Current Balance	LT	PC
120105.108105	AD UPIS-ACC Dep		NS		05/26/06	00012						
	Net Negative	Salvage	NS	302666228	05/26/06		12.02					AA
	Net Negative	Salvage	NS	302666228	05/26/06		14,183.97					AA
	Net Negative	Salvage	NS	302666228	05/26/06		1,682.77					AA
	Net Negative	Salvage	NS	302666228	05/26/06		5,395.30					AA
	Net Negative	Salvage	NS	302666228	05/26/06		75.33					AA
	Net Negative	Salvage	NS	302666228	05/26/06		31.05					AA
	Net Negative	Salvage	NS	302666228	05/26/06		72,066.12		3,20-			AA
	Net Negative	Salvage	NS	302666228	05/26/06				1,642.58-			AA
	Net Negative	Salvage	NS	302666228	05/26/06		10,232.14					AA
	Net Negative	Salvage	NS	302666228	05/26/06		5,410.36					AA
	Net Negative	Salvage	NS	302666228	05/26/06				70.34-			AA
	Net Negative	Salvage	NS	302666228	05/26/06				49.83-			AA
	Net Negative	Salvage	NS	302666228	05/26/06				3,015.96-			AA
	Net Negative	Salvage	NS	302666228	05/26/06				687.26-			AA
	Net Negative	Salvage	NS	302666228	05/26/06				29.34-			AA
	Net Negative	Salvage	NS	302666228	05/26/06				3,738.33-			AA
	Net Negative	Salvage	NS	302666228	05/26/06				1,610.66-			AA
	Net Negative	Salvage	NS	302666228	05/26/06		155.69					AA
	Net Negative	Salvage	NS	302666228	05/26/06				1,480.49-			AA
	Net Negative	Salvage	NS	302666228	05/26/06				12,841.65-			AA
	Period Totals						113,676.12					
	Net Negative	Salvage	NS	302575947	04/11/06		781.83					AA
	Net Negative	Salvage	NS	302575947	04/11/06		1,143.96					AA
	Net Negative	Salvage	NS	302575947	04/11/06		2,132.47					AA
	Net Negative	Salvage	NS	302575947	04/11/06		14,171.50					AA
	Net Negative	Salvage	NS	302575947	04/11/06		5,374.57					AA
	Net Negative	Salvage	NS	302575947	04/11/06		75.33					AA
	Net Negative	Salvage	NS	302575947	04/11/06		31.05					AA
	Net Negative	Salvage	NS	302575947	04/11/06		71,287.31					AA
	Net Negative	Salvage	NS	302575947	04/11/06				3,20-			AA
	Net Negative	Salvage	NS	302575947	04/11/06				1,644.39-			AA
	Net Negative	Salvage	NS	302575947	04/11/06		10,159.68					AA
	Net Negative	Salvage	NS	302575947	04/11/06		5,374.08					AA
	Net Negative	Salvage	NS	302575947	04/11/06				70.34-			AA
	Net Negative	Salvage	NS	302575947	04/11/06				49.83-			AA
	Net Negative	Salvage	NS	302575947	04/11/06				3,008.34-			AA
	Net Negative	Salvage	NS	302575947	04/11/06				687.26-			AA
	Net Negative	Salvage	NS	302575947	04/11/06				29.34-			AA
	Net Negative	Salvage	NS	302575947	04/11/06				3,738.33-			AA
	Net Negative	Salvage	NS	302575947	04/11/06				1,610.66-			AA
	Net Negative	Salvage	NS	302575947	04/11/06		155.69					AA
	Net Negative	Salvage	NS	302575947	04/11/06				1,480.49-			AA
	Net Negative	Salvage	NS	302575947	04/11/06				12,836.14-			AA
	Period Totals						112,716.91					

American Water Works Company
Account 108105 December Activity
NNS Accum Depreciation

Page Date - 7/13/07
From Date - 12/10/05
Thru Date - 12/31/06

G/L Account	Account Description Explanation	Do Ty	Document	G/L Date	Co.	Debit	Amounts	Credit	Current Balance	LT	PC
120105.108105	AD UPIS-Acc Dep	NS	302533433	03/14/06	00012	781.83				AA	P
	Net Negative Salvage	NS	302533433	03/14/06		1,149.98				AA	P
	Net Negative Salvage	NS	302533433	03/14/06		2,192.77				AA	P
	Net Negative Salvage	NS	302533433	03/14/06		113.02				AA	P
	Net Negative Salvage	NS	302533433	03/14/06		1,662.02				AA	P
	Net Negative Salvage	NS	302533433	03/14/06		5,325.84				AA	P
	Net Negative Salvage	NS	302533433	03/14/06		31.05				AA	P
	Net Negative Salvage	NS	302533433	03/14/06		70,966.82				AA	P
	Net Negative Salvage	NS	302533433	03/14/06			3.20-			AA	P
	Net Negative Salvage	NS	302533433	03/14/06		10,151.47		1,646.04-		AA	P
	Net Negative Salvage	NS	302533433	03/14/06		5,353.11				AA	P
	Net Negative Salvage	NS	302533433	03/14/06			70.34-			AA	P
	Net Negative Salvage	NS	302533433	03/14/06			49.83-			AA	P
	Net Negative Salvage	NS	302533433	03/14/06			3,008.34-			AA	P
	Net Negative Salvage	NS	302533433	03/14/06			687.26-			AA	P
	Net Negative Salvage	NS	302533433	03/14/06			29.34-			AA	P
	Net Negative Salvage	NS	302533433	03/14/06			3,738.33-			AA	P
	Net Negative Salvage	NS	302533433	03/14/06			1,610.66-			AA	P
	Net Negative Salvage	NS	302533433	03/14/06		138.31				AA	P
	Net Negative Salvage	NS	302533433	03/14/06			1,480.49-			AA	P
	Period Totals					112,340.70		12,837.79-		AA	P
	Net Negative Salvage	NS	30247106	02/06/06		781.83				AA	P
	Net Negative Salvage	NS	30247106	02/06/06		1,149.98				AA	P
	Net Negative Salvage	NS	30247106	02/06/06		2,192.77				AA	P
	Net Negative Salvage	NS	30247106	02/06/06		113.02				AA	P
	Net Negative Salvage	NS	30247106	02/06/06		1,662.02				AA	P
	Net Negative Salvage	NS	30247106	02/06/06		5,325.84				AA	P
	Net Negative Salvage	NS	30247106	02/06/06		31.05				AA	P
	Net Negative Salvage	NS	30247106	02/06/06		70,966.82				AA	P
	Net Negative Salvage	NS	30247106	02/06/06			3.20-			AA	P
	Net Negative Salvage	NS	30247106	02/06/06		10,058.58		1,601.77-		AA	P
	Net Negative Salvage	NS	30247106	02/06/06		5,323.25				AA	P
	Net Negative Salvage	NS	30247106	02/06/06			70.34-			AA	P
	Net Negative Salvage	NS	30247106	02/06/06			49.83-			AA	P
	Net Negative Salvage	NS	30247106	02/06/06			3,008.34-			AA	P
	Net Negative Salvage	NS	30247106	02/06/06			580.90-			AA	P
	Net Negative Salvage	NS	30247106	02/06/06			29.34-			AA	P
	Net Negative Salvage	NS	30247106	02/06/06			3,738.33-			AA	P
	Net Negative Salvage	NS	30247106	02/06/06			1,610.66-			AA	P

American Water Works Company
Account 108105 December Activity
NNS Accum Depreciation

Page Date - 7/13/07
From Date - 12/10/03
Thru Date - 12/31/06

Account Description Explanation	DO TY	Document	G/L Date	Co.	Debit	Amounts	Credit	Current Balance	LT C
AD UPIS-Acc Dep	NS	30247106	02/06/06	00012			513.96-		AA P
Net Negative Salvage	NS	30247106	02/06/06		138.31		1,480.49-		AA P
Net Negative Salvage	NS	30247106	02/06/06				12,687.16-		AA P
Period Totals					111,772.84				
Net Negative Salvage	NS	30247113	01/09/06		781.82				AA P
Net Negative Salvage	NS	30247113	01/09/06		1,449.98				AA P
Net Negative Salvage	NS	30247113	01/09/06		223.77				AA P
Net Negative Salvage	NS	30247113	01/09/06		2,132.47				AA P
Net Negative Salvage	NS	30247113	01/09/06		113.02				AA P
Net Negative Salvage	NS	30247113	01/09/06		14,166.84				AA P
Net Negative Salvage	NS	30247113	01/09/06		5,287.93				AA P
Net Negative Salvage	NS	30247113	01/09/06		72.43				AA P
Net Negative Salvage	NS	30247113	01/09/06		29.85				AA P
Net Negative Salvage	NS	30247113	01/09/06		70,553.61				AA P
Net Negative Salvage	NS	30247113	01/09/06			3.20-			AA P
Net Negative Salvage	NS	30247113	01/09/06		1,601.11				AA P
Net Negative Salvage	NS	30247113	01/09/06		10,047.81				AA P
Net Negative Salvage	NS	30247113	01/09/06		5,300.91				AA P
Net Negative Salvage	NS	30247113	01/09/06			70.21-			AA P
Net Negative Salvage	NS	30247113	01/09/06			49.83-			AA P
Net Negative Salvage	NS	30247113	01/09/06			3,008.34-			AA P
Net Negative Salvage	NS	30247113	01/09/06			579.86-			AA P
Net Negative Salvage	NS	30247113	01/09/06			29.34-			AA P
Net Negative Salvage	NS	30247113	01/09/06			2,738.33-			AA P
Net Negative Salvage	NS	30247113	01/09/06			1,610.66-			AA P
Net Negative Salvage	NS	30247113	01/09/06		138.31		1,480.49-		AA P
Period Totals					111,224.72		12,685.33-		AA P
Account Totals					8,722,404.95		155,814.32-	8,566,590.63	
Object 108105 Total					8,722,404.95		155,814.32-	8,566,590.63	
Company Totals - Posted					8,722,404.95		155,814.32-	8,566,590.63	
Total - Unposted					8,722,404.95		155,814.32-	8,566,590.63	