

KENTUCKY-AMERICAN WATER COMPANY
CASE NO. 2015-00418
COMMISSION STAFF'S FIRST REQUEST FOR INFORMATION

Witness: Kevin N. Rogers / Donald J. Petry

- 18.**
- a. Identify the amounts of incentive pay that are included in base year and forecasted labor. Describe the incentive pay plans and explain why such a plan is necessary and reasonable.
 - b. List each Kentucky-American employee who is eligible to participate in the incentive pay program.
 - c. State the level of incentive pay awarded to all individuals participating in the program for the previous five calendar years compared to the level of incentive pay available to each participant in the forecasted period.
 - d. For the previous five calendar years, provide a comparison of the incentive pay that was budgeted to the actual amounts paid in each year. Include detailed explanations for any variance between the budgeted and actual payments.

Response:

- a. The amounts of incentive pay in the base year and performance pay in the forecasted year are \$339,017 and \$318,405, respectively.

To promote meeting company objectives, the Company offers compensation based on individual and company performance to eligible employees under American Water's Annual Performance Plan (APP) and Long Term Performance Plan (LTPP).

The Company's performance compensation plans contain tangible goals that are designed to do several things. First, they measure and reward employees for performance based on delivering clean, safe, reliable and affordable water service and providing good customer service when doing so. The operational components measure performance that can most directly influence customer satisfaction, health and safety, environmental performance, and operational efficiency. Customers derive a direct benefit from our focus on these key measures in the plan. Further, well-grounded financial measures keep the organization focused on improved performance at all levels of the organization, particularly in increasing efficiency, decreasing waste, and boosting overall productivity. The Company's compensation is not only a means of focusing its employees on the organization's goals, but also a means of measuring attainment of those goals.

A financially healthy utility focused on efficiency and customer satisfaction is able to attract the capital investments necessary to provide safe and reliable service and to maintain the technological expertise necessary to operate the company and comply with increasing water quality standards. A financially healthy utility is very much in the interest of KAWC's customers, as it helps ensure KAWC the ability to provide safe and reliable service at the lowest reasonable cost.

Most important, the evidence in this case demonstrates that, even with performance payments, our overall non-bargaining unit compensation is below the 50th percentile ranking. Consequently, all of our performance plans are necessary to attract and retain employees. Furthermore, the LTPP component is vital to retain employees who might otherwise seek higher compensation elsewhere but who are provided an incentive to remain with the Company. The retention of a highly trained and demonstrably effective and productive workforce is, without question, in the best interest of our customers.

Please see the attached 2015 annual incentive plan brochure. The Company will supplement this response with the 2016 annual performance plan brochure once it is completed.

- b. Please refer to Workpaper 3-1.
- c. Please see the attached confidential information regarding individual compensation for KAW employees by title. KAW is requesting Confidential Treatment of the individual information with these responses. The Company will provide copies of the information to all parties in this case upon execution of an appropriate confidentiality agreement.
- d. Please see the attached schedules.

Supplemental Response 4-15-16

- a. See the attached 2016 Annual Performance Plan brochure.



AMERICAN WATER

my Value Plan

2016 Annual Performance Plan

This booklet is intended to provide a summary of our Annual Performance Plan (APP) and the award you are eligible for under the Plan. All awards are subject to the terms and conditions of the American Water Works Company, Inc. Annual Performance Plan (the "Plan"). In the event of any conflict between the terms of the Plan and this booklet, the terms of the Plan will govern.

The company's policies, procedures and benefits, including (without limitation) those covered in this booklet, as well as wages and all other terms and conditions of employment, are subject to change, revision or deletion by the Company at any time.

American Water reserves the right to change or terminate the Plan at any time for any reason. Participation in the Plan does not give anyone the right to continued employment with American Water.

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This booklet provides an overview of the 2016 short term incentive award that is offered to eligible employees under the American Water Works Company, Inc. **Annual Performance Plan** (the “Plan”). The short-term incentive plan – a key component of your American Water compensation package and **myValue Plan (mVP)** – promotes the achievement of the company’s short-term, strategic business goals and your individual goals.

An Award Based on American Water’s Success

At American Water, our goal is to attract, motivate and retain a highly engaged workforce by creating an environment where every employee can excel, and by providing employees the opportunity to further benefit when the company meets or exceeds performance goals. One way we do this is through the implementation and management of competitive reward offerings.

We rely on our employee’s knowledge and skills to help the company achieve its business objectives. Since performance is key to our success we structure our performance based reward programs to truly “pay for performance”. We do this to ensure we reward our employees accordingly for their contributions to the business.

Let’s work together to make a great company even better.

What has changed from last year?

- **The name** – we have changed the name of the plan from Annual Incentive Plan to Annual Performance Plan (APP) to reflect our pay for performance philosophy.
- **Broader Eligibility** – non-exempt, non-union employees are now eligible.
- **Company Performance Goals** – Company performance goals have been reduced and redefined in order to more closely align with our strategy.
- **External Benchmarking** – Customer Satisfaction and our OSHA ORIR rate will now be benchmarked against external competitors.
- **Financial Company Performance Goal** - Earnings Per Share (EPS) will be weighted at 50%. EPS is a key growth metric and the basis for our 7 – 10% growth rate.
- **Individual alignment to company and/or business performance** – employees will be aligned more closely to the performance of the area of the business they support as well as the performance of the overall company. Please see chart on page 4 for details.

Determination of eligibility and target award amounts

Eligibility is based upon start date and the number of days you work during the plan year. Your start date must be on or before September 30, 2016 in order to be eligible to receive an award.

If you are an exempt employee, your target award is expressed as a percentage of your 12/31 salary and is dependent upon job/grade level within the organization. If you are a non-exempt (hourly), non-union employee you are assigned to a target that is equal to 5% of annual earnings. Employees who transfer to or from positions in salary grades 60 and above will receive prorated awards based on days worked at each salary grade. Please see Attachment A in the Appendix for details.

You must be active on the day APP awards are distributed (early 2017) in order to receive an award. However, you (or your beneficiary) may be eligible for a pro rata award in the event of divestiture, disability, retirement, death or involuntary termination (not for cause) on or after July 1, 2016. Please see your HR representative for details.

Determination of Company Performance

Each year, senior management establishes the financial and non-financial performance goals that are aligned with our corporate strategy. APP award pool funding is determined by the results under each performance category.

STRATEGY	GOAL	WEIGHT	TARGET
 SAFETY & PEOPLE	OSHA Recordable Incident Rate	7.50%	2.75
	Ratio of the # of Near Miss Reports to OSHA Recordable Injuries	7.50%	9 to 1
 CUSTOMER	Customer Satisfaction Survey	15%	First Quartile in Industry Benchmarking
 TECHNOLOGY & OPERATIONAL EFFICIENCY	Environmental Leadership/Drinking Water Quality Standards	10%	18x Industry Average
	Operational Efficiency Improvement	10%	35.4%
 GROWTH	Financial/Earnings Per Share	50%	\$2.75-\$2.85

*Customer Strategy – Our goal is first quartile performance; however target attainment is achieved if results are between the 2nd and 3rd quartiles.

Within each company performance category there are defined thresholds (minimums), targets and maximums. Thresholds indicate the minimum level of performance possible to receive credit for any particular company performance category. Targets represent target performance and maximums represent the highest level of performance that impacts awards. Please see Attachment B in Appendix for details.

Safety and People

OSHA is the abbreviation for the federal Occupational Safety & Health Administration. We measure our incidence rate, or ORIR, against published Bureau of Labor Statistics utility industry safety benchmarks in order to drive American Water safety performance improvement.

Near Miss Reporting metrics continuously raise safety awareness through identification and correction of unsafe conditions and behaviors through increased reporting. By identifying near misses, we can expect to reduce injuries.

Customer Satisfaction

We use a competitive assessment by an independent third party to determine how American Water compares to the top customer service providers in the water utility industry. Goal attainment is based upon the quartile achieved.

Technology and Operational Efficiency

We are committed to protecting the environment and to maintaining our consistent history of complying with, and in many cases surpassing, minimum standards required by applicable laws and regulations. This target was established based upon our goals to lead the water industry in environmental compliance and outperform the U.S. EPA published industry average.

In addition, achievement of this goal will allow us to improve our overall cost structure and culture of continuous improvement, while creating headroom for continued investment.

Diluted Earnings Per Share (EPS)

Strong EPS performance enhances our capacity to raise the financing necessary to make prudent capital improvements in our water and wastewater systems as well as provide greater total return to our stockholders. Diluted EPS (as defined in the 10k) will be used for calculation purposes.

Individual Alignment to Business Specific Performance

Business performance impacts individual APP award amounts. We believe that every individual should be measured upon the performance of the business they most closely support, as well as overall company performance because every employee makes a difference in the performance of the company as a whole.

The chart on the next page illustrates the alignment of employee performance in the businesses they support and the performance of the company overall (AWK).

Employee Group	Business Performance Weighting(s)
AWK Reg Ops State/Division Employees	75% State/Division, 25% AWK
AWK Service Company Employees Fully Dedicated to One State/Division	75% State/Division, 25% AWK
AWK Service Company Employees Dedicated to Multiple States/Divisions	100% AWK
AWE Line of Business Employees	75% Line of Business, 25% AWK
AWE Functional Employees Dedicated to One Line of Business	75% Line of Business, 25% AWK
AWE Functional Employees Dedicated to Multiple Lines of Business	75% AWE, 25% AWK

In instances where individual State, Division, or Line of Business performance metrics are not available, overall company performance metrics will be used.

APP goal attainment scorecards are posted on mySource quarterly.

Impact of Individual Performance

Your individual performance plays a large role in determining the amount of your award. If you exceed the individual performance targets you and your manager have set, you could receive higher award amounts. Conversely, if you underperform and do not meet your performance goals you could receive lower award amounts or no award at all. Individual performance is assessed by your manager and is measured against your individual performance goals. See Attachment C in Appendix for more information on performance ratings.

If company, business, or individual performance is above target, it is possible for you to earn an award that is worth up to 200% of target as illustrated below.

APP Target	% of Target Achieved (based upon individual performance)	Final APP Award Amount
\$2,500	125%	(\$2,500 * 125%) \$3,125

Note – Company and/or Business performance directly impacts the pool of funds available for distribution.

Payment and Taxation of Awards

2016 APP awards will be paid in the first quarter of 2017. Your APP will be treated as taxable income in the year it is paid. It is recommended you consult a personal tax or financial advisor for guidance on the tax treatment of your APP award.

Payment will be issued in the same manner as your normal paycheck (direct deposit or advice).

For more information

If you have questions about the American Water APP, contact the compensation team:

Natasha Graham (856) 782-3651

Kevin Coogan (856) 782-2309

“American Water recognizes and rewards our employees when we work together to reach our goals. The success of our business depends on our ability to continually meet the commitments we make to our customers and shareholders each year. The APP plan is one part of our overall commitment in providing a great place to work for our employees,” **BJ Holdnak, senior vice president, Human Resources.**

APPENDIX
Attachment A

Target APP Award Percentages

Non- Exempt Positions

All full time, non-union employees have a 5% target. Targets are based upon regular and overtime earnings.

GRADE	APP%
All Grades	5%

Exempt Positions

GRADE	APP%
L06/N06	20%
L07/N07	15%
L08 – L09/N08 – N09	10%
L10 – L11/N10 – N11	5%

APPENDIX
Attachment B

Company Performance Thresholds, Targets and Maximums

ORIR	
Threshold	3.15
Target	2.75
Maximum	2.55

Near Miss Reports: Recordable Injuries	
Threshold	8.1 : 1
Target	9.0 : 1
Maximum	10.0 : 1

Customer Satisfaction Survey Performance	
Threshold	4th Quartile when compared to peers
Target	Between 2nd & 3rd Quartile when compared to peers
Maximum	1st Quartile when compared to peers

Environmental Compliance with Drinking Water Standards	
Threshold	13x above industry average
Target	18x above industry average
Maximum	26x above industry average

Operational Efficiency	
Threshold	35.80%
Target	35.40%
Maximum	34.90%

EPS	
Threshold	\$2.63
Target	\$2.81
Maximum	\$2.88

APPENDIX

Attachment C

Performance Ratings

Each year, you and your manager identify performance goals, which align with American Water’s overall objectives for 2016, and directly impact the company’s success. These performance targets should be specific, measurable, and aligned with the company’s performance goals. During your year-end performance review, you and your manager will discuss how well you performed against the established targets, while demonstrating American Water’s values. Your manager will provide your overall performance rating using the following ratings:

Performance Goal and Overall Rating Scale	Values Rating Scale
<p>Significantly Exceeded - Performance significantly exceeded expectations due to exceptionally high quality of work performed in all <i>essential</i> areas of responsibility, resulting in an overall quality of work that was superior and made an exceptional or unique contribution in support of business unit, functional, or organizational objectives.</p>	<p>Role Model - Always or frequently demonstrates this behavior; is recognized as exemplary and frequently teaches others how to do it well.</p>
<p>Achieved - Performance consistently met expectations in all <i>essential</i> areas of responsibility, at times possibly exceeding expectations, and the quality of work overall was very good.</p>	<p>Demonstrated - Demonstrates most aspects of this behavior most of the time.</p>
<p>Underperformed - Performance was consistently below expectations in most <i>essential</i> areas of responsibility, and/or reasonable progress toward critical goals was not made.</p>	<p>Not Demonstrated - Rarely or never demonstrates this behavior.</p>
<p><i>The ratings for performance goals (based on goal weight) accounts for 50% of the overall rating.</i></p>	<p><i>The ratings for values accounts for 50% of the overall rating.</i></p>

* *Underperformed* definition as an Overall Rating is expanded to include the following: **A performance enhancement plan must be established, including timelines, and monitored to measure progress.**

APPENDIX Attachment D

Frequently Asked Questions

What is the plan year for APP?

The “Plan Year” for 2016 APP is January 1, 2016 through December 31, 2016.

When will my 2016 APP award be paid?

APP payments will be paid through your payroll no later than March 15, 2017.

How will my 2016 APP award be paid?

You will receive payment in accordance with how you receive your normal paycheck, i.e. direct deposit or advice. Payments are subject to tax withholding.

What happens if I change job positions within American Water during the plan year?

Your APP award will be based on your target level percentage as of December 31, 2015.

What happens if I am on a leave of absence when APP is paid?

If you are eligible to receive an award, it will be paid during the same time frame all other employees receive their APP pay.

What happens if I leave American Water before I receive my award payment?

To receive the award payment, you must be actively employed with American Water on the date the payment is made.

What is the minimum and maximum that could be paid under the plan (as a percent of target)?

APP award amounts can range from zero, to a maximum of 200%.

Will I receive an award if I meet my individual performance goals but the company does not achieve minimum (threshold) performance?

No. A pre-determined financial threshold for company performance must be met in order for funding and any award to be provided under the APP.