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Case No.: WR-2017-0285
SR-2017-0286
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MISSOURI PUBLIC SERVICE COMMISSION

**CASE NO. WR-2017-0285
CASE NO. SR-2017-0286**

DIRECT TESTIMONY

OF

ROBERT V. MUSTICH

ON BEHALF OF

MISSOURI-AMERICAN WATER COMPANY

Exhibit No. 26-P
Date 3/4/18 Reporter MR
File No. WR-2017-0285

Exhibit 26P
WR-2017-0285
Direct Testimony of Robert V.
Mustich - Public

**DIRECT TESTIMONY
ROBERT V. MUSTICH
MISSOURI-AMERICAN WATER COMPANY
CASE NO. WR-2017-0285
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BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

IN THE MATTER OF MISSOURI-AMERICAN)	
WATER COMPANY FOR AUTHORITY TO)	
FILE TARIFFS REFLECTING INCREASED)	CASE NO. WR-2017-0285
RATES FOR WATER AND SEWER)	CASE NO. SR-2017-0286
SERVICE)	

AFFIDAVIT OF ROBERT V. MUSTICH

Robert V. Mustich, being first duly sworn, deposes and says that he is the witness who sponsors the accompanying testimony entitled "Direct Testimony of Robert V. Mustich"; that said testimony and schedules were prepared by him and/or under his direction and supervision; that if inquiries were made as to the facts in said testimony and schedules, he would respond as therein set forth; and that the aforesaid testimony and schedules are true and correct to the best of his knowledge.


Robert V. Mustich

Commonwealth of Virginia
County of Arlington
SUBSCRIBED and sworn to
Before me this 7 day of June 2017.


Notary Public

My commission expires: April 30, 2021

ELAINE SUSAN WIGGINS
NOTARY PUBLIC
REGISTRATION # 7267311
COMMONWEALTH OF VIRGINIA
MY COMMISSION EXPIRES
APRIL 30, 2021

1 DIRECT TESTIMONY

2
3 ROBERT V. MUSTICH
4

5
6 I. INTRODUCTION

7 Q. Please provide your name, position and business address.

8 A. My name is Robert V. Mustich. I am Managing Director and the U.S. East Region
9 Line of Business Leader, Rewards for Willis Towers Watson. Willis Towers Watson
10 is a leading global professional services company which has 40,000 associates
11 throughout the world, and offers solutions in the areas of corporate risk and broking;
12 human capital and benefits; health care exchange solutions; and investment, risk, and
13 reinsurance. My business address is 901 North Glebe Road, Arlington, VA 22203.

14
15 Q. Please state your educational and professional background and experience.

16 A. I graduated from American University with a BS/BA in Human Resources
17 Management. I have over 25 years of industry and compensation consulting services
18 experience, have been with Willis Towers Watson for over 20 years, and have assisted
19 management and Boards of Directors at numerous companies in designing and
20 assessing total compensation programs. Since joining the firm in 1997, I have
21 consulted with numerous utilities and currently serve as U.S. East Region Line of
22 Business Leader, Rewards in addition to being a senior member of our utilities industry
23 practice. I have conducted competitive assessments of total compensation for
24 numerous public utilities throughout the U.S. Prior to joining Willis Towers Watson,
25 I was a senior compensation consultant for PricewaterhouseCoopers (formally Coopers

1 and Lybrand, LLP) performing similar compensation consulting services for clients.
2 Prior to that, I held corporate senior staff compensation and benefits positions.

3

4 **Q. Have Willis Towers Watson and you performed similar analyses in the past?**

5 A. Yes. Willis Towers Watson and I have conducted similar competitive compensation
6 studies for other utility clients.

7

8 **Q. Please explain Willis Towers Watson's experience in providing compensation and
9 benefits consulting services to organizations like Missouri-American Water
10 Company ("Missouri-American Water").**

11 A. Willis Towers Watson has extensive experience serving clients in the utility industry,
12 having served over 100 utilities in the U.S. within the last year. Because we invest so
13 heavily in our utility industry capabilities, we have rich competitive industry
14 compensation and benefits information that enables us to benchmark Missouri-
15 American Water against similar companies in the U.S. Given Willis Towers Watson's
16 breadth and depth of resources, we are frequently engaged by companies to evaluate
17 the competitiveness of their compensation philosophy, compensation and benefit
18 levels, at-risk compensation design and pay structures, and other consulting services.

19

II. DEFINITIONS

20 **Q. Can you please identify some of the key definitions that you will need to reference
21 as part of your testimony?**

22 A. Yes.

23

1 Q. More specifically, please define Target Total Cash Compensation.

2 A. Target Total Cash Compensation represents the sum of base salary plus target short-
3 term at-risk compensation.

4

5 Q. Please define Target Total Direct Compensation.

6 A. Target Total Direct Compensation represents the sum of base salary, plus target short-
7 term at-risk compensation, plus long-term at-risk compensation.

8

9

III. PURPOSE OF TESTIMONY

10 Q. What is the purpose of your testimony?

11 A. The purpose of my testimony is to demonstrate that the target total direct compensation
12 provided to Missouri-American Water at-risk compensation eligible employees, when
13 viewed against the markets for talent for employees in similar positions, is below the
14 competitive range of the market based on the company's stated compensation
15 philosophy. Willis Towers Watson specifically focused on the following aspects of
16 Missouri-American Water's program:

- 17
- Total compensation philosophy;
 - 18 • Competitive market positioning of target total direct compensation (base salary
19 plus short-term at-risk compensation plus long-term at-risk compensation)
 - 20 • Design of short-term at-risk compensation program; and
 - 21 • Design of long-term at-risk compensation program.

22

1 **IV. OVERVIEW OF TOTAL COMPENSATION PHILOSOPHY**

2 **Q. Does Missouri-American Water have a defined compensation philosophy?**

3 A. Yes, American Water Works Company, Inc. (“American Water”) has a defined
4 compensation philosophy which is applicable to Missouri-American Water.

5
6 **Q. How would you define the parent company’s compensation philosophy?**

7 A. American Water’s compensation philosophy is to generally pay salaries that are
8 competitive with those of comparable organizations for jobs of similar responsibility.
9 To carry out this philosophy, American Water’s objective is to target total direct
10 compensation (base, short-term at-risk compensation, and long-term at-risk
11 compensation) at the median (50th percentile) of the market with greater earning
12 opportunity for exceptional performance for fully qualified individuals.

13
14 **Q. How does this compensation philosophy compare with other utilities?**

15 A. Willis Towers Watson examined the proxy statements for two peer groups: (1) Large
16 Utility Peer Group, 15 publicly-traded utilities comparable in size to American Water
17 (revenues range from ½ to 2.5 times American Water’s 2016 revenues of \$3.3 billion),
18 as disclosed in the company’s March 27, 2017 proxy statement, and (2) Small Utility
19 Peer Group, 13 publicly-traded utilities comparable in size to Missouri-American
20 Water (revenues range from \$48-\$820M, compared to Missouri-American Water’s
21 2016 revenue of \$288M). Based on our review, we believe American Water’s
22 compensation philosophy is well-aligned with utility peers, as a majority of both Large
23 Utility Peer Group companies (14 of 15, 93%) and Small Utility Peer Group companies
24 (7 of 13, 54%) target the market median (50th percentile) for some or all pay elements.

1 Our consulting experience also suggests that American Water's median (50th
2 percentile) pay philosophy is comparable to typical market practice found in general
3 industry.

4
5 **V. SUMMARY OF WILLIS TOWERS WATSON'S TOTAL**
6 **COMPENSATION STUDY**

7 **Q. Did you conduct a compensation study of Missouri-American Water's**
8 **compensation program?**

9 A. Yes, and a copy of the Study is included as Schedule RVM-1 HIGHLY
10 CONFIDENTIAL to my testimony. Schedule RVM-1 HIGHLY CONFIDENTIAL
11 has been identified as Highly Confidential under terms of the Commission's
12 confidentiality rule because it contains employee specific personnel information.

13
14 **Q. Please describe how the study was conducted.**

15 A. Willis Towers Watson utilized three data sources to assess Missouri-American Water's
16 compensation program: (1) As we did in assessing American Water's total
17 compensation philosophy, we assessed the design of its short-term at-risk and long-
18 term at-risk compensation programs using proxy disclosures of groups of public
19 utilities referred to as the (1) Large Utility Peer Group and (2) Small Utility Peer Group,
20 and (3) competitive market positioning of Missouri-American Water's target total
21 direct compensation levels was compared to Willis Towers Watson published
22 compensation surveys.

23 **Q. How did you define "competitive" for the purposes of your compensation study?**

1 A. Willis Towers Watson and typical market practice define an element of total
2 compensation as being competitive if it falls in a range that extends between 10% below
3 to 10% above the market median level of total compensation.

4
5 **Q. Please describe how you assessed the competitiveness of Missouri-American**
6 **Water’s target total direct compensation levels.**

7 A. Willis Towers Watson assessed the competitiveness of target total direct compensation
8 provided by Missouri-American Water to its short-term at-risk eligible population
9 based on a selection of Missouri-American Water jobs (“benchmark jobs”). Benchmark
10 jobs are those positions that are common across comparable organizations and for
11 which compensation data are available from published surveys.

12 To conduct this analysis we reviewed compensation data provided to us by Missouri-
13 American Water and examined Willis Towers Watson’s compensation surveys in our
14 Compensation Databank (CDB). These surveys are comprised of compensation data
15 from over 1,000 U.S. based companies, and Willis Towers Watson has been conducting
16 these surveys for over 20 years.

17 Missouri-American Water’s current compensation levels were compared to the market
18 50th percentile (market median) for two different market perspectives to determine the
19 competitiveness of pay and to validate the alignment with American Water’s current
20 compensation philosophy (targeting compensation at the 50th percentile of market).

21 Willis Towers Watson’s assessment of benchmark jobs represents approximately 70%
22 of the population of Missouri-American Water employees as of March 14, 2017, who
23 are eligible for at-risk compensation. Specific details regarding our study, which

1 includes a detailed description of the study methodology, are included in Schedule
2 RVM-1 HIGHLY CONFIDENTIAL.

3

4 **Q. How did you derive 50th percentile (median) market values?**

5 A. To derive 50th percentile (median) market values, Willis Towers Watson weighted
6 energy services and general industry survey data 60% and 40% respectively to place a
7 greater weight on the energy services market data since this includes regulated entities
8 most similar to Missouri-American Water for positions that are not industry specific.
9 Given that these positions can be recruited or lost to companies in any industry, the use
10 of general industry survey data ensures that non-industry specific positions are being
11 compensated competitively. Industry specific positions were compared only to energy
12 services industry data.

13

14 **Q. Please describe how you determined the competitiveness of Missouri-American
15 Water's target total direct compensation?**

16 A. Two different market perspectives were examined to validate the competitiveness of
17 Missouri-American Water's target total direct compensation.

18 A national market perspective was examined which consisted of the entire population
19 of survey participants in Willis Towers Watson's Energy Services and General Industry
20 databases. This perspective represents a U.S. national compensation perspective and is
21 aligned with American Water's compensation philosophy.

22 A Midwest regional perspective including Arkansas, Illinois, Indiana, Iowa, Kansas,
23 Kentucky, Missouri, Nebraska, Ohio, Oklahoma, Tennessee, Wisconsin, and West
24 Virginia labor markets was examined for non-executive positions, which consisted of

1 the same entire survey participant population from Willis Towers Watson's Energy
2 Services Industry and General Industry databases but was customized to identify a
3 Midwest-specific geographic dataset. This dataset identified employees that work in
4 the thirteen states listed above for companies headquartered anywhere in the United
5 States.

6
7 **Q. What were the compensation study results from the national perspective?**

8 A. Using a weighted average of all positions reviewed, Missouri-American Water's target
9 total direct compensation, as reported in Exhibit 1 (below), is below the range of
10 competitive market median by being 19% below the market median. Again, Willis
11 Towers Watson and typical market practice considers market competitiveness to be a
12 result that falls within plus or minus 10% of median range.

13 **Exhibit 1**

Summary of Missouri-American Water's Target Total Direct Compensation vs. Market Median (National Market Perspective)		
Base Pay	Target Total Cash Compensation	Target Total Direct Compensation
-20%	-19%	-19%

14
15 **Q. What were the compensation study results from the Midwest Regional
16 perspective?**

17 A. Missouri-American Water's target total direct compensation is below the market
18 median range, as reported in Exhibit 2, because it falls 12% (represents a weighted
19 average of all positions reviewed) below the market median.

1

2

Exhibit 2

Summary of Missouri-American Water's Target Total Direct Compensation vs. Market Median (Midwest Regional Market Perspective)		
Base Pay	Target Total Cash Compensation	Target Total Direct Compensation
-12%	-12%	-12%

3

4 **Q. What would be the impact on the competitiveness of Missouri-American Water's**
5 **target total direct compensation if short-term and long-term at risk compensation**
6 **were not part of its compensation program?**

7 **A. If we compare Missouri-American Water's total compensation program excluding at-**
8 **risk compensation (that is, base salary alone) to market pay levels that include at-risk**
9 **compensation, as reported in Exhibits 3 and 4, Missouri-American Water's target total**
10 **direct compensation would not be competitive because it would fall 31% below median**
11 **from a national perspective and 25% below median from a Midwest Regional**
12 **perspective.**

13

Exhibit 3

Summary of Missouri-American Water's MOAW Base Salary Only vs. Market Median (National Market Perspective)		
Base Pay	Target Total Cash Compensation	Target Total Direct Compensation
-20%	-27%	-28%

14

15

1

Exhibit 4

Summary of Missouri-American Water's MOAW Base Salary Only vs. Market Median (Midwest Regional Market Perspective)		
Base Pay	Target Total Cash Compensation	Target Total Direct Compensation
-12%	-20%	-21%

2

3 Q. In your opinion and based on the results of the study, are Missouri-American
4 Water employees overcompensated?

5 A. No. Missouri-American Water employees are generally below the range of market
6 median for each element of compensation.

7 VI. SUMMARY OF WILLIS TOWERS WATSON'S SHORT-TERM
8 AT-RISK PROGRAM ASSESSMENT

9 Q. Did you conduct an assessment of American Water's short-term at-risk program?

10 A. Yes.

11

12 Q. What was the purpose of your assessment?

13 A. This assessment was completed to compare the design of American Water's short-term
14 at risk program (that is applicable to Missouri-American Water) and its various
15 elements to market practice.

16

17 Q. What were the findings of the assessment?

18 A. Overall our review indicates that American Water's annual incentive program is
19 comparable to and competitive with designs of utility peers, based on a review of the

1 Large Utility Peer Group and the Small Utility Peer Group that I referenced earlier.
2 Like American Water, practically every company reviewed has a short-term at-risk
3 compensation program that it uses to help attract, motivate and retain critically skilled
4 employees needed to successfully run the business. Companies design their short-term
5 at-risk compensation programs to align with their business strategies and
6 circumstances, so there tends to be a range of practices regarding how the programs are
7 designed.

8 American Water's short-term at-risk compensation program assesses performance
9 using a balanced scorecard approach, incorporating financial, safety, customer
10 satisfaction, environmental, and operational efficiency metrics to determine a corporate
11 funding pool. American Water's program requires the achievement of at least 90% of
12 target earnings per share performance (EPS) to ensure the financial viability of the plan
13 before any short-term variable compensation payment can be made to any participant.

14 American Water's short-term program design is within the range of market practice for
15 utilities. Specific details regarding our assessment are included in Schedule RVM-1

16 HIGHLY CONFIDENTIAL.

17
18 **VII. SUMMARY OF WILLIS TOWERS WATSON'S LONG-TERM**
19 **AT-RISK PROGRAM ASSESSMENT**

20 **Q. Did you conduct an assessment of American Water's long-term at-risk program?**

21 **A. Yes.**

22

1 **Q. What was the purpose of your assessment?**

2 A. This assessment was completed to compare the design of American Water’s long-term
3 at-risk program (that is applicable to Missouri-American Water) and its various
4 elements to market practice.

5
6 **Q. What were the findings of your assessment?**

7 A. Overall our review indicates that American Water’s long-term at-risk program is
8 comparable to and competitive with designs of utility peers, based on a review of the
9 Large Utility Peer Group and the Small Utility Peer Group referenced earlier. Like
10 American Water, every company but one in the Large Utility Peer Group and every
11 company but two in the Small Utility Peer Group has a long-term at-risk compensation
12 program which is used to help attract, motivate and retain key senior level employees
13 needed to successfully run the business. Companies design their long-term at-risk
14 compensation programs to align with their business strategies and circumstances, so
15 there tends to be a range of practices regarding how the programs are designed.
16 American Water’s long-term at-risk compensation program design is within the range
17 of market practice for utilities. Specific details regarding our assessment are included
18 in Schedule RVM-1 HIGHLY CONFIDENTIAL.

19

20

21

1 **VIII. OVERALL FINDINGS REGARDING MISSOURI-AMERICAN**
2 **WATER'S COMPENSATION PROGRAMS**

3 **Q.** What are the overall findings and conclusions of your analysis of the
4 compensation of Missouri-American Water?

5 A. Overall, our analysis indicates that Missouri-American Water's total direct
6 compensation programs are comparable to and competitive with market practices of
7 other similarly-sized utilities and are therefore reasonable. Missouri-American Water,
8 like the companies it competes with for talent, has to provide a competitive total direct
9 compensation opportunity delivered via programs that benefit employees, customers
10 and shareholders. Missouri-American Water attempts to achieve this goal with its
11 balanced and competitive base salary and short-term and long-term at-risk
12 compensation programs. My experience working with both utilities and general
13 industry companies, and the results of the study included as Schedule RVM-1 HIGHLY
14 CONFIDENTIAL, indicate the programs at Missouri-American Water are within a
15 broad range of market norms and are not excessive in design or level of compensation.

16
17 **Q.** Does this conclude your testimony at this time?

18 A. Yes, it does.