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October 22, 2024

VIA ELECTRONIC FILING

Hon. David Jones, Chairman
c/o Ectory Lawless, Docket Room Manager
Tennessee Public Utility Commission
502 Deaderick Street, 4th Floor
Nashville, TN 37243
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Electronically Filed in TPUC Docket Room
on October 22, 2024 at 2:22 p.m.

RE: *Petition of Tennessee-American Water Company to Modify Tariff, Change and Increase Charges, Fees, and Rates, and for Approval of a General Rate Increase, TPUC Docket No. 24-00032*

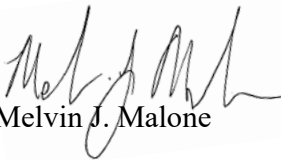
Dear Chairman Jones:

Attached for filing please find *Tennessee-American Water Company's Rebuttal Testimonies for (1) Heath Brooks; (2) Ann Bulkley; (3) Dominic J. DeGrazia; (4) Grant Evitts; (5) Nicholas Furia; (6) Larry Kennedy; (7) Bob Lane; (8) Robert V. Mustich; (9) Robert Prendergast; (10) Charles Rea; (11) Linda Schlessman; (12) Grady Stout; (13) Harold Walker, III; and (14) John Watkins* in the above-captioned matter.

As required, the original plus four (4) hard copies will follow. Should you have any questions concerning this filing, or require additional information, please do not hesitate to contact me.

Very truly yours,

BUTLER SNOW LLP



Melvin J. Malone

clw

Attachments

cc: Bob Lane, TAWC
Shilina Brown, Consumer Advocate Division
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TENNESSEE-AMERICAN WATER COMPANY, INC.

DOCKET NO. 24-00032

REBUTTAL TESTIMONY

OF

ROBERT V. MUSTICH

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

2 A. My name is Robert V. Mustich. I am Managing Director and East Region Rewards
3 Business Leader for Willis Towers Watson.

4 **Q. Did you previously submit direct testimony in this proceeding on behalf of Tennessee-**
5 **American Water Company, Inc. (“Tennessee-American,” “TAWC” or the**
6 **“Company”) in this proceeding?**

7 A. Yes. I filed direct testimony on May 1, 2024.

8 **Q. On whose behalf are you submitting this testimony?**

9 A. Tennessee-American, a wholly owned subsidiary of American Water Works Company Inc.
10 (“AWK”).

11 **Q. What is the purpose of your rebuttal testimony?**

12 A. The purpose of my testimony is to rebut the testimony of David Dittmore, who pre-filed
13 testimony on behalf of Consumer Advocate Division of the Office of the Tennessee
14 Attorney General, and Mark Garrett, who pre-filed testimony on behalf of the City of
15 Chattanooga. I will also demonstrate that their arguments against recovery of 55% and
16 50%, respectfully, of the Annual Performance Plan (“APP”) aligned with earnings per
17 share,¹ as well as Mr. Dittmore’s testimony regarding DEI and against 100% of the Long-
18 term Performance Plan (“LTPP”),² are inconsistent with providing reasonable and effective

¹ *Pre-filed Direct Testimony of CAD Witness David N. Dittmore* (“Dittmore Direct Testimony”) at 25:16-17, TPUC Docket No. 24-00032 (Sept. 17, 2024); *Pre-filed Direct Testimony of City of Chattanooga Witness Mark E. Garrett* (“Garrett Direct Testimony”) at 26:10-15, Docket No. 24-00032 (Sept. 17, 2024).

² *See* Dittmore Direct Testimony at 39:4-9 for recommendations relating to DEI; *see* Dittmore Direct Testimony at 28:10-11 for recommendations against 100% of the LTPP.

1 employee compensation programs that serve as management tools to drive positive
2 customer outcomes.

3 **Q. Do they provide reasons for their recommendations?**

4 A. Yes, they believe that the portion of the Company's APP that is aligned with earnings per
5 share and, in Mr. Dittmore's case, DEI and the entirety of the Company's LTPP primarily
6 benefit shareholders and do not provide measurable benefits to customers.

7 **Q. Mr. Mustich, are you familiar with the practices of industry, generally, and public**
8 **utility companies in particular, with respect to performance-based compensation?**

9 A. Yes, I am.

10 **Q. With respect to the utilities industry and industry in general, is it common for**
11 **businesses across America to have in place performance-based compensation plans**
12 **similar to TAWC'S APP and LTPP?**

13 A. Yes, it is. Based on WTW's study referenced in my Direct Testimony, my personal
14 experience working with hundreds of companies, and WTW advising thousands of
15 companies annually, the vast majority of companies have APPs that use financial and non-
16 financial metrics. These companies also have LTPPs that use financial and/or relative total
17 shareholder return metrics. Consequently, it is safe to say that the performance-based
18 compensation plans that TAWC maintains are consistent with the practice followed by a
19 vast amount of corporations in American business.

1 **Q. Generally, what is the purpose of such performance-based compensation plans?**

2 A. With respect to plans such as the APP, the purpose is to attract and retain a performance-
3 oriented workforce that is provided tangible financial incentives in the form of variable
4 performance based compensation, to improve productivity, efficiency and other desirable
5 goals (such as safety, environmental compliance, customer satisfaction, etc.) that
6 management deems important to conducting a successful business. These plans send
7 powerful messages to employees because their compensation is contingent on these
8 important customer-oriented goals. In the case of the LTPP-type metrics, the goal is to
9 reduce the costs and disruptions associated with employee turnover by providing incentives
10 to remain with the company and improve company performance. As noted, both of these
11 types of plans are quite common in American business and are time-tested and successful
12 ways to increase productivity, efficiency and employee performance while reducing the
13 costs and inefficiencies of employee turnover. In addition, employees expect to participate
14 in such plans since they are widely prevalent and the absence of them would make TAWC
15 less competitive from a talent attraction perspective.

16 **Q. Do Mr. Dittmore's and Mr. Garrett's testimonies suggest that customers and**
17 **shareholders have competing interests when financial metrics are in performance**
18 **plans?**

19 A. Yes, they do.

20 **Q. How do they suggest this?**

21 A. They recommend that the expenses related to financial metrics and stock performance
22 primarily benefit shareholders and that related performance plan expenses be allocated to

1 shareholders. They also recommend that operational/customer metrics benefit customers
2 and that only those specific incentive plan expenses should be allocated to customers. In
3 addition, Mr. Dittmore argues that DEI does not benefit customers and therefore DEI
4 expenses should not be recovered by the Company either.

5 **Q. What is incorrect about Mr. Dittmore's and Mr. Garrett's recommendations?**

6 A. Their recommendations fail to recognize that including financial goals in performance pay
7 programs, like the approach that TAWC takes, reflects the interdependence of a company's
8 financial performance with its operational success. Strong financial performance enables
9 the Company to invest in resources—both people and infrastructure—that help ensure the
10 efficient operation of the Company, which ultimately benefits customers. Incorporating
11 financial metrics in performance plans is common across all types of organizations, even
12 those that are not publicly traded or owned by publicly traded parent companies, as TAWC
13 is. In fact, many privately held companies, and even mission based not-for-profit
14 organizations, incorporate financial metrics in their performance pay programs to send the
15 message to employees that financial efficiency and viability are essential to operational
16 success, and to delivering on customer objectives and expectations. In addition, Mr.
17 Dittmore and Mr. Garrett arbitrarily assign cost allocations without recognizing the
18 holistic benefit that TAWC's reasonably designed program provides customers, employees
19 and shareholders. Another example of this is Mr. Dittmore's recommendation against
20 TAWC recovering the performance plan costs for DEI because having a diverse, equitable
21 and inclusive workforce does not directly benefit customers in his view.

22 **Q. If TAWC employees did not receive their performance pay, how would it affect their**
23 **compensation?**

1 A. If TAWC employees did not receive all or even a portion of their performance pay, they
2 would receive compensation that is at the low end of reasonable and below competitive
3 levels of market median total remuneration, particularly for employees in positions for
4 which performance compensation comprises a significant portion of total direct
5 compensation.

6 **Q. In his testimony, Mr. Garrett relies on Table 1, which includes results from a survey**
7 **his group conducted, to support his argument that most states do not include**
8 **performance pay costs in rates. Did you review that table?**

9 A. Yes. He relied on his 24 Western State Incentive Survey that his firm conducted.³

10 **Q. Do you have any observations about information shown in Table 1?**

11 A. Yes. Although certain American Water affiliate jurisdictions are included in Mr. Garrett's
12 Table 1, the American Water affiliate jurisdictions where 100% of performance pay costs
13 are recovered in rates are not included in Table 1.

14 **Q. What state affiliates are you referring to?**

15 A. West Virginia-American Water Company, Indiana-American Water Company,
16 Pennsylvania-American Water Company, and Virginia-American Water Company all
17 recover 100% of performance pay in rates. Mr. Garrett did not include those states in
18 forming his recommendation according to Table 1.

19 **Q. Both witnesses argue that the Tennessee Public Utility Commission has previously**
20 **denied recovery of the financial metrics component of the performance plans and**

³ Garrett Directory Testimony, p. 22.

1 **therefore this component should not be recoverable in this proceeding. (Dittmore pp.**
2 **24:20 – 25:4; Garrett pp. 18:3 – 19:25). Why is this the wrong viewpoint?**

3 A. Both Mr. Dittmore and Mr. Garrett argue that the Commission should deny full recovery
4 of performance-based compensation to TAWC because the Commission denied full
5 recovery in TPUC Docket No. 18-00017.⁴ This is the only case cited by either witness. The
6 problem with this narrow viewpoint is that it fails to recognize that compensation programs
7 and perspectives evolve over time and having holistic programs that align to customer,
8 employee and shareholder objectives are mutually beneficial and create sustainable, long-
9 term positive performance.

10 **Q. Do you have an example of where viewpoints have changed or a rate case in which**
11 **performance compensation has been accepted by a regulatory authority?**

12 A. Yes. In 2015, the Public Service Commission of West Virginia acknowledged in a rate
13 case filed by West Virginia-American Water Company that “[Annual Performance Plans]
14 that tie some portion of an employee’s compensation to an employee’s actual performance
15 are prevalent in the compensation packages for larger businesses and [have] become the
16 ‘norm’ for major utility companies.”⁵ The Public Service Commission of West Virginia
17 further agreed that “the [Annual Performance Plan] is an integral part of the overall
18 compensation plan of [West Virginia-American Water Company] and that the total
19 compensation (the combination of base pay and incentive pay) to eligible employees is
20 intended to place that total compensation at or near the market rate for each particular job
21 or salary band.”⁶ In the 2015 case, the Commission also approved a portion of the

⁴ Dittmore Direct Testimony at 24:20-25:4; Garrett Direct Testimony at 18:3-25.

⁵ *Final Order*, p. 48-49, Public Service Comm’n of West Virginia, Case No. 15-0675-S-42T (Feb. 24, 2016).

⁶ *Id.* at 49.

1 company's long-term performance plan costs.⁷ In 2021, the Public Service Commission
2 of West Virginia went further in allowing 100% of the demonstrated long-term
3 performance compensation in its revenue requirements after concluding that "[i]t is not
4 reasonable to pick one expense and arbitrarily eliminate it or reduce it by 50% because it
5 indirectly benefits shareholders."⁸ This was reaffirmed by the Public Service Commission
6 of West Virginia in 2023.⁹ This is just one example of the evolution of regulatory
7 acceptance of this compensation methodology.

8 **Q. Do you have another example of how viewpoints or regulations have changed?**

9 A. Yes, legislation^[6] passed in Texas in 2023 related to the consideration of compensation and
10 benefits in establishing the rates of electric utilities. Employee compensation includes base
11 salary, wages and incentive compensation. It states: "when establishing an electric utility's
12 rates, the regulatory authority shall presume that employee compensation and benefits
13 expenses are reasonable and necessary if the expenses are consistent with market
14 compensation studies issued not earlier than three years before the initiation of the
15 proceeding to establish rates."¹⁰ There are certain items, not included in the term of
16 compensation and benefits, but overall total compensation (base salary, APP and LTPP) at
17 a utility for the vast majority of its employees is fully recoverable provided it is
18 competitively reasonable and consistent with peers, as determined through recent market
19 studies. The WTW study of TAWC compensation cited in my direct testimony is a recent
20 market study.

⁷ *Id.* at 51.

⁸ *Final Order*, p. 40, Public Service Comm'n of West Virginia, Case No. 21-0369-W-42T (Feb. 24, 2022).

⁹ *See Final Order*, p. 31, Public Service Comm'n of West Virginia, Case No. 23-0383-W-42T (Feb. 23, 2024).

¹⁰ *Id.*

1 **Q. Would the recommendation to remove a portion of the Company's total market-**
2 **based compensation from recoverable costs be impacted by changing the Company's**
3 **compensation structure?**

4 A. It appears the full market-based compensation would be completely recovered from
5 customers if TAWC included the disputed portion of compensation in employees' base pay
6 rather than awarding it through APP and LTPP. No testimony contradicts the Company's
7 demonstration that its total market-based employee compensation, including performance
8 pay, is reasonable and prudent. The Intervenor's only dispute the manner in which the
9 Company pays part of the compensation. In other words, if the amount of the performance
10 compensation were included in base pay, there would be no objection because the pay
11 would still be market-based. Changing the manner of compensating employees to remove
12 the disputed methods (APP and LTPP) and placing all of the compensation in base pay
13 apparently would result in recovering one hundred percent (100%) of the higher base pay
14 in the Revenue Requirement. However, making this adjustment would be inconsistent with
15 market practice.

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

17 A. Yes, it does.

CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing was served via U.S. Mail or electronic mail upon:

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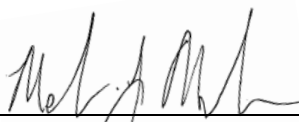
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This the 22nd day of October 2024.



Melvin J. Malone