Study on pay for performance with focus on utilities

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A Study on Pay For Performance
With Focus on Utilities

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CHAPTER I

INTRODUCTION

Pay for performance is a method of setting very specific performance objectives for individual employees in a company and tying a substantial portion of an employee's compensation to the successful achievement of those objectives. Pay for performance differs from merit pay plans which have been tied more to job standards and less defined, more subjective performance criteria.

This study is limited to investigating pay for performance programs of other companies at the supervisory, manager and officer levels with the goal of improving existing Corporate programs. It will also be limited to cash compensation, since other forms of compensation is a study of considerable magnitude in itself.

Why look for new, more effective methods of employee compensation? Great Falls Gas Company (GFGC) is interested because traditional merit pay programs have not achieved what they were intended to achieve. Too often the difference between a raise for outstanding performance and one for satisfactory performance is not enough to influence performance.¹ Numerous articles researched in this study detailed these problems time and time again, as well as tying into the experience of Great Falls Gas Company's nine year old merit pay program.

The Company adjusts base pay, for each employee, under its merit pay program, which is tied to job standards. Performance reviews are given to each employee every six months. In addition, it
has pay for performance programs for its officers and managers and certain other key staff. Last year, the pay for performance concept was extended to first line supervisors.

In the next three to five years, the plan is to have the entire workforce on a pay for performance basis. Company management believes the pay for performance concept at Great Falls Gas has proven very successful by increasing the organization's focus on key strategic objectives, by improving corporate effectiveness in providing better customer service at lower cost, while maximizing returns to shareholders. Great Falls Gas is continually reviewing its pay for performance programs to determine effectiveness and to make improvements where needed.

Company management is making a concerted effort in this study to determine what other companies are doing in the pay for performance arena and what techniques and methods are producing the best overall results.

History of Great Falls Gas Company's Salary Program

The Board of Directors approved the pay for performance program for managers, officers and other key staff of Great Falls Gas Company in 1982. The reason the Board implemented the program was to build a sense of teamwork in the management group, for better year to year performance for the shareholder.
Great Falls Gas Company also has a merit pay program which has been in place since 1979. The salary program at GFGC has 17 different job grades with entry levels, midpoints and maximums. The midpoints of each job grade are compared to industry pay levels (obtained from salary surveys) each year, for similar positions. GFGC tries to maintain the midpoints of each job grade in line with comparable local or regional job positions, but when pay for performance incentive pay is included, pay levels for high achievers will be above comparable industry position pay for similar size companies. If incentive pay is not earned, then base pay will be slightly below industry levels.

During the first four years of the Company's pay for performance program, was based strictly on the return on equity level earned by the corporation. For the past two years, the program was revised to incorporate the setting of specific performance objectives for each participant. More aggressive goals have been integrated into individual performance objectives each year, which have resulted in higher overall organizational effectiveness.

The company must meet certain return on equity (ROE) levels. The program currently begins at 1.25 percent below the Public Service Commission's allowed return on equity before any bonuses are paid. If this threshold level of return on equity is attained, then the other provisions of the plan trigger. If the threshold level of return is not met, no bonuses are paid. A copy of the Company's plan is included in APPENDIX 1.
The GFGC plan at the threshold level of earnings has two elements: first, a return on equity of 11.00 percent (1.25 percent below PSC Allowed ROE) in the given year must be met to have a right to earn 50 percent of the incentive bonus pool; second, a 5 year rolling average ROE (5 yr. avg of PSC Allowed ROE) must be met to trigger the other 50 percent of the pool. A rolling average is defined as the most recent 5-year period, including the current year. If these two criteria are met then the employee receives 20 percent of the total bonus automatically; the other 80 percent is tied to specific performance objectives which are set at the beginning of each year. The percentage of achievement of these specific objectives determines the actual portion of the pool the individual earns.

Fiscal years 1987 and 1988 were extremely warm (warmest since 1934) and the participants were only eligible for half of the bonus in 1987 and none in 1988. There is now a loud chorus of participants who want to change the plan to where they can earn at least a portion of the bonus despite the actual earnings level of the Company. The participants of this plan earned 100 percent of their eligible bonus in the previous four years with few complaints from the participants about the plan structure. Proposed changes in the Company's plans are detailed in the recommendation section of Chapter V.

A year ago the Company extended the pay for performance program to first line supervisors. These supervisors control about two-thirds of the total workforce. Specific performance objectives have been set for each supervisor. Their bonus has been tied 25
percent to the same threshold of return on equity in the current year as described above and 75 percent to specific performance objectives. This latter portion will be paid regardless of what the Company's performance is and will be based on the percentage achievement of their objectives.

The above described pay for performance participants are also eligible for merit increases in pay, based on how well they perform their day to day job duties in relation to their job standards. Merit increases ranged from 1.5-3.0 percent for the past year. Because Company earnings were so poor, due to all time record warm weather through the middle of the second fiscal quarter of 1988, a salary freeze was implemented beginning in the last month of the second quarter for all supervisors, managers and officers of the Company. Supervisors were still eligible for their 75 percent portion of their incentive bonus. The salary freeze will stay in effect for twelve months or until the earnings of the Company improve, whichever is longer.

Each year the Company updates its strategic plan which defines the key results areas it wants management to focus on for the next three years. Each department sets goals for the upcoming year based on the ongoing corporate goals of the Company, which are:

1) Improve customer service

2) Build load on the system

3) Improve productivity
4) Improve employee development and challenges

Specific performance objectives are then set for each participant from department goals and from key results areas developed from the strategic plan of the Company. Usually four to eight specific performance objectives are established for each participant in the program with the employee and his or her supervisor agreeing on the final objectives. Currently one quarter of the employees (supervisors, managers, officers and key staffers) of the Company are included in the pay for performance programs.

Objectives of This Study

Management is seeking further information in this study to improve the Company's pay for performance program in the following areas. Specifically, management wants to know:

1) To what extent other companies include supervisors, managers and officers of their companies in their pay for performance programs? What successes and failures have they had with their programs?

2) How other companies structure their specific performance objectives, to obtain ideas on how to improve the setting of specific performance objectives, within the Company.

3) What the optimum equivalent percentage of employee's base pay should be to provide the strongest motivational tie to
performance achievement.

4) What incentive compensation levels other companies are setting for payout in total program funds and for individual performance achievement, once performance objectives are met.

5) Whether other companies are monitoring their pay for performance programs to determine their overall effectiveness and how they have structured their monitoring systems.

6) What are the advantages and disadvantages of pay for performance programs?
CHAPTER II

REVIEW OF LITERATURE

A review was made from secondary information sources to determine the business world's experience with pay for performance programs.

This method was selected because the author was aware of several trade journal articles outlining various aspects of success and failure of general business salary administration programs and new pay for performance approaches.

An information search was made through the America Society for Personnel Administration (ASPA) computer data base, covering pay for performance articles published during the past three years. This search developed a list of forty articles on incentive pay plans. From this list, nineteen of the articles were secured for review, from titles of articles and papers which appeared to be more pertinent to the study.

Only one of these articles, which was based on AT&T's experience, discussed pay for performance specifically for that utility sector. AT&T's pay for performance program was developed to help bring them from a regulated, monopoly business position to one of a highly competitive industry environment. Their program consisted of two parts, one of a special merit award plan for outstanding individual performance and a team incentive plan for unit performance. The individual performance program are paid
regardless of total corporate performance but the team incentive plan is tied directly to corporate performance and all participants share equally in the plan payout. Their incentive program cost is considered part of average pay when making survey comparisons with the market. To establish the fund pools for incentive pay, traditional merit pay increases were held and the comparable percentage of pay increase was put at risk over a three to four year period to establish the incentive pay funds.

Great Falls Gas Company was more interested in reviewing criteria specifically designed for the gas utility industry. It was for this reason Great Falls Gas Company set about gathering its own information from utilities through an information survey, the results are detailed in Chapter IV.

The following paragraphs contain information on pay for performance from secondary information sources such as periodicals, published papers, and other studies on pay for performance.

Motivational Theories and The Tie To Pay For Performance

There is a considerable body of research more than 100 studies attesting to the positive effects of setting difficult, as compared to easy, performance goals. If managers expect very little from subordinates, subordinates are not likely to excel; rather, low expectations will tend to be self-fulfilling.
Evidence indicates that the most powerful motivational systems are those that provide rewards for good performance, and withhold rewards for poor performance.4

It is not surprising to find numerous case studies and reports of lethargy and inefficiency in public sector organizations, opting for across the board approach to reward distributions. Lawler has pointed out, using pay to motivate improved job performance is not a "piker's game". To use pay, to motivate improved performance, it is essential that substantial differences exist in the range of benefits actually provided.5

Nash and Carroll, in their book The Management of Compensation, cite the results of five early surveys encompassing more that 4,700 interventions. Average increases in productivity after switching from time-based to output-based pay plans ranged from 29 to 63 percent, the median increase being 34.5 percent.6 More recently, an extensive literature review found that, on average, individual incentive plans increased output by 30 percent; group incentive plans typically increased output by 18 percent.7

Additionally, a comprehensive review of productivity experiments reported the results of seven studies which examined the effects of financial incentives. Results were positive in all cases, with performance output increases ranging from 18 to 46 percent.8

Money as a motivation tool is not a new idea. It can be traced as far back as to Julius Caesar who paid special incentives to his army for special achievement.9 Later, ships captains received a share
of the profits of their voyages. With the emergence of the professionally managed corporations, GM implemented the modern annual incentive plan in 1918. Incentives spread rapidly through dominant companies of the era: in the auto industry first, then the steel and chemical industries, and later in retailing. The Great Depression put a damper on incentives during the 1930s and extended through WWII. Beginning in 1950 with the new tax laws which favored stock options and for the next 15 years, the combination of annual performance based incentives with an effective long term option that linked executive rewards to the company's increased stock price provided a strong link of pay to performance.

Pay and performance linkage started diminishing in the mid-1960s and began a long 15-year downhill slide when Congress began amending the stock option and tax codes. In the early 1970s, research at Harvard Business School had shown that top management bonuses were related more to the size of the firm and to position level than to the performance of the company.¹⁰ A 1981 article in Compensation Review purported to prove conclusively that there was no correlation at all between pay and performance.¹¹

There have been numerous articles published in the past few years by Fortune, Business Week and other periodicals, stating that many chief executive officers of American corporations had forgotten that bonuses were supposed to be paid for output, not input. Many CEO's were able to sell their board of directors that they should still get their fat bonuses even though their corporate performance was
poor. With increased competition from both within the U. S. and abroad, boards of directors are not the "easy sell" they were a few years ago. Also there has been a chorus of workers screaming the "wrongs" of upper managements getting large bonuses while they have been required to take decreases in wages and benefits.\textsuperscript{12}

The magnitude of compensation to motivate management in the direction of achieving corporate goals will be discussed in detail from the results of the utility survey presented in the next section.

The necessary magnitude of strong motivational compensation found in secondary sources showed that, compensation experts generally agree that an incentive payment needs to reach a minimum of 15 percent of base pay in order to represent a meaningful motivating difference to plan participants.\textsuperscript{13}

**Problems With Most Existing Pay Plans**

Why search for new more effective methods of employee compensation? Primarily it is done because traditional merit pay programs have not achieved what they were intended to achieve. Too often the difference between a raise for outstanding performance and one for satisfactory performance is insufficient to influence performance.\textsuperscript{14}

Merit pay systems can break down because of problems with the performance appraisal systems on which they are based. In practice many merit pay systems fail to consistently fulfill their
mission of rewarding superior performance. In fact some merit pay plans hinder excellent performance by causing enthusiastic employees to become frustrated and disenchanted.

The three main problems with merit pay administration are:

1) pay is perceived as being unrelated to job performance,
2) secrecy of pay is related to perceived inequity; and
3) the size of the merit increases awarded has been too small to positively impact performance.\(^{15}\)

Why is there a perception that compensation is unrelated to job performance? One problem is that there is so much time elapse between performance and reward that the employee loses sight of the relationship. Also, the goals or objectives an employee is supposed to accomplish are often unclear and not well defined.

Another factor is that merit increases are based on other factors than performance, such as length of service, the manager's view of future potential, or the manager's perceived need to equalize pay with peers, where one employee's pay is low compared with that of others in the group.\(^{16}\) The performance appraisal is typically an undesirable task because the forms often do not describe what the employee's duties really are which makes it difficult to properly rate the employee's performance, and the employee feels that the ratings are too subjective and do not really reflect actual performance.

While the concept of rewarding outstanding performers with a
pay increase appears to be straightforward, in practice it is very difficult to implement properly. Most organizations do not have enough money for payroll increases in their budgets to pay for performance. Companies usually allot each department a set percentage for wage increases which limits the amount of raises that can be allowed.

Since most managers are restricted by budget constraints on the amount of dollars they have for merit increases in their departments, an individual's salary increase often is based on the manager's creativity in "backing into" performance ratings to make the numbers match up. Often these decisions are arbitrary or subjective, which many times enrage and often demoralize the workers affected.

Studies have shown that the average performance appraisal scores slowly creep up over time.17 This can be a major factor in increasing the average size of the merit increase and causes payroll budgets to be higher than budgeted levels. Higher annual ratings result from supervisor bias in the performance reviews, giving higher scores each year whether performance is improved or not. There is also evidence that performance scores vary substantially from supervisor to supervisor for the same level of employee performance, based on their view of what the ratings should be for a given level of performance.

Employee surveys have shown that employees with high appraisal scores believe that their appraisals reflected their true performance, and were satisfied with their appraisal from their supervisor. On the other hand, those employees who received
low supervisory appraisals were dissatisfied with their appraisal and felt it did not reflect their true performance. At least two conclusions are possible from these results. First, if appraisal scores reflect true performance, then employees, while dissatisfied, have nothing to gripe about. Second, if appraisal scores are not reflective of true performance, then the merit pay system is creating undesirable dissatisfaction.18

Surveys have shown that employees strongly disagree with the concept that all employees should get equal pay raises.19 Further, many employees appear to believe that supervisors do tend to use performance to make pay increase decisions. However, they apparently think that the supervisor's evaluations are biased since employees do not agree that their performance is reflected in their performance evaluation or in their merit pay increase.

Dissatisfaction with a merit program is not necessarily bad. For instance, if it is the poorest performers who are dissatisfied with their pay increases and the highest performers who are most satisfied, then the system is working. In other words, the program is rewarding high performers and giving low performers the proper feedback. Low performers then have a choice of improving their performance or exiting the organization.20

The Need For New Compensation Plans

Surveys have indicated that most pay raises are too small to be effective, a survey of 2,867 companies conducted by The Wall Street Journal in 1979 found that salary increases were too low to motivate employees.21

Pay can be motivating if the increase is large enough in relation to an individual's income to result in a significant change in
The number of companies using variable compensation below the top executive level is still fewer than 20 percent. In general, organizations are coming to accept the necessity of gearing pay to performance and giving employees a "cut" of the extra value they produce.

There are many other important reasons why almost any business today needs to implement a more effective compensation program. Companies that manufacture products competing with foreign products at home and abroad must continually strive to reduce their cost of production to be more competitive. The market place is very dynamic with shorter product life cycles a firm requires a continual analysis of strategic direction, and, to be successful, an organization must be able to change quickly with changing market conditions and customer demands.

Utility management today, despite a natural monopoly position, too, must be more aggressive to adapt to change. Day to day business transactions have become much more dynamic and complex with deregulation of gas supplies; more competition from other energy sources, especially industrial loads; customer by-pass by other gas suppliers; and more stringent demands from customers, employees, regulators and stockholders.

A prime way to gain flexibility to successfully deal with this new world is through the development of an effective compensation program, which leads management and the company as a whole in the direction of strategic goals. An effective program which ties pay
to performance can be the answer to many of these organizational needs.

Is The Current Generation of Pay For Performance Plans Producing Better Results?

Consultant and academic research is beginning to point to a greater correlation between pay and performance. Recent studies by K.R. Murthy's (updated) PhD thesis\textsuperscript{23}, a Hay Associates study\textsuperscript{24} and a recent study by Kevin Murphy of the University of Rochester\textsuperscript{25} found total compensation positively related to corporate performance as measured by shareholders' total return.\textsuperscript{26}

With the decline in the cost of living, compensation increases began to slow perceptibly in 1984, a trend that is likely to continue throughout the balance of the 1980s. Developments in the long term incentive area are also encouraging and bear witness to the viability of the pay for performance ethic. There is a renewed interest in stock options and the emergence of a second generation of performance unit plans. The latter reflects a more sophisticated understanding about the nature of performance measures that influence stock price performance, such as return on stockholders' equity.

The previous paragraphs contain discussion on the pros and cons of pay for performance programs. The following is a summary of the generally argued pros and cons of pay for performance.
programs, as described by Mr. Thomas Rollins, PhD, Hay Management Consultants.27

Advantages:

1) Money can serve as an extremely effective motivator of employee performance.

2) Superior employees resent automatic and indiscriminate pay increases for all.

3) Tying pay to performance puts teeth in the performance appraisal process.

4) Good pay for performance programs increase clarity of employee goals.

5) Pay for performance programs can give organizations much greater mileage for their compensation dollar.

6) Good pay for performance programs increase employees' sense of ownership and involvement in overall company performance.

7) Pay for performance systems are conducive to a "no surprise" policy of performance evaluation.
8) Pay for performance programs encourage employees to track their own performance against pre-established targets, thus creating a sense of challenge to improve levels of work efficiency.

Disadvantages:

1) Many employees are of a mind set where they prefer the security and guarantee of automatic increases.

2) Most pay for performance programs reward individual performance which is counter to establishing team efforts.

3) The need to generate tailored goals and measures that go beyond just budget numbers exceeds the capacity of many organizations to manage.

4) Employees view pay for performance not as a way of stimulating performance, but to contain compensation.
CHAPTER III

RESEARCH METHODOLOGY

Great Falls Gas, in order to obtain specific information on gas utility programs conducted a mail and telephone survey of seventeen gas utility companies with pay for performance programs. The survey was conducted during the period of April 15 to May 13, 1988. A summary of the responses to each survey question and a list of companies which furnished information on their pay for performance plans are included in APPENDIX 2 at the back of this report. Participating companies surveyed are included in APPENDIX 3.

It was decided not to do a random sample of companies because the Company was not interested in what a typical gas utility's pay for performance program design contained. But instead the study was designed to gather information from utilities with successful pay for performance programs.

A nineteen question survey form was developed by Great Falls Gas Company and was tested in-house with the human resource department checking it for completeness and clarity. A copy of the survey cover letter and survey questionnaire are included in APPENDIX 4.

A threshold level of companies with under $140 million in revenues was first selected from the American Gas Association's (AGA) member list of those responding to its 1987 Executive Salary Study indicating they had a management incentive program. These
companies were first selected because it was believed that smaller gas utilities pay for performance programs might be more appropriate to Great Falls Gas Company than the larger utilities programs. Their were only nine utilities of 69 included in the AGA Salary Study having under $140 million in revenues, which indicated they had incentive bonus pay programs.\textsuperscript{28}

Because only nine utility companies were found to be included in the first group, under the revenue criteria selected, AGA provided eight additional company names which they indicated had successful management incentive programs. These companies were larger, all having revenues over $500 million.

Of the survey forms sent to these seventeen companies, only three completed questionnaires were received by the two week deadline. Telephone calls were made to each utility; the majority said they would like to have another form sent to them because they had misplaced the first one. After one month only four forms had been returned. All four were filled out describing their merit pay plans instead of their pay for performance programs. In checking back, the person who filled out the forms was someone unfamiliar with their upper management pay for performance program.

At this point a telephone survey was made of all seventeen utilities on the original lists, using the survey form as the outline for the questions. Virtually all useable survey information obtained was from the telephone interviews with key human resource personnel of each company. If the initial telephone contact found that the
individual was not knowledgeable about their company's pay for performance program, follow up contacts were made until the person with such knowledge was interviewed.
CHAPTER IV

SURVEY RESULTS

The telephone survey concluded with eleven companies furnishing information on their plans. Two companies indicated they currently did not have pay for performance programs. The other four companies did not choose to participate for one reason or another. The information in this study is from those eleven completed surveys. Because there was no random sample of utilities made and because a small sample was used no statistical analysis was attempted.

Summaries of responses for each survey question are included in APPENDIX 2. The following paragraphs are summaries of the survey responses.

Major Reasons for Establishing Pay for Programs

According to survey results, utility companies established their pay for performance programs for the following major reasons:

1) to direct the management of the company to focus on key results areas of the company, to improve bottom line performance.
2) to build team effort to improve performance.

3) to help change the direction of the organization with a constantly changing business environment.

4) to enhance the ability to retain and attract talented employees.

5) to link pay to performance.

The surveyed companies have had their pay for performance programs from one to fifteen years, with the median program age at 5 years.

The common thread of almost all surveyed companies was that they are attempting to enhance their existing programs or enlarge their pay for performance programs to cover a larger portion of the management team.

Threshold Payout Criteria

Eight of the eleven companies responding to the survey use a combination of group and individual performance objectives. Two responding companies have group pay for performance programs. A group plan is one where all plan participants share in the pool funds in proportion to their base salary, regardless of their individual
performance. There appeared to be less enthusiasm for this type of program by its users than with programs where individual achievement was the basis for allocating incentive pool funds.

All responding companies used a threshold level of earnings, usually return on equity (ROE), to earn at least 50 percent of the incentive fund pool. This target must be met before the remainder of the plan is available for possible payout. Once the threshold level is met, most companies rely on specific performance objective achievement by each plan participant to distribute the pool of incentive funds.

Some Companies use other threshold criteria than ROE, they are:

- Profit Plan Returns
- Peer Group Rankings
- Return on Assets
- Retail Rate Comparisons With Peer Group Companies
- Controllable Operation and Maintenance Expenses
- Employees/Customer Ratios

Companies who use earnings as the threshold, used various criteria as mentioned above, but the two most popular methods were:

1) Comparing actual returns of the company with the allowed rate of return set by the governing regulatory authorities. This return in most cases was the ROE, but if the company had other companies under its ownership
umbrella, it likely used return on assets.

2) Comparing actual returns with a pre-approved profit plan or budget.

Minimum payouts (about 50 percent) in many plans begin when 80-85 percent of the return level set as the target objective is achieved and usually 100 percent payout is available for distribution when 100 percent of the target is achieved. Most plans also payout 110 to 150 percent of target incentive if higher levels of earnings above the target are reached.

Peer group rankings were used by three larger surveyed companies, to determine threshold payouts. Two of the companies used their 10 strongest competitors to compare their ROE to and then ranked themselves from 1 to 10. The higher they rank with their peer group companies, the higher their bonus pool payout.

One surveyed company ranked itself with peer group companies by comparing its retail gas rates with peer companies in the region for determining 30 percent of its threshold payout.

Another popular tool was to use budgeted controllable operation and maintenance expenses as the target and setting payout beginning at zero percent payout at budgeted levels and with higher payouts as expense levels were actually reduced. Comparing actual results with budgeted figures seemed to be most popular for companies who may be part of a larger unit. However, it is more difficult to determine actual return on equity, on a meaningful basis.
One fast growing utility, included in the survey, used the ratio of employees per customer as the criterion for part of their threshold payout. Evidently their management believed that this was a key element to their success. It was a new program, so insufficient history was available to test its effectiveness at this point in time.

Virtually all of the companies surveyed had a threshold level of earnings or return that must be earned before incentive bonus payout. No matter how hard management worked, or met other goals, if the shareholder did not do well, from an earnings standpoint, then, plan participants did not benefit. Some respondents indicated there were complaints from their utility management that they have too many factors affecting earnings beyond their control. Examples include the weather, regulatory climate, and so forth. They indicated their Boards look at these factors similarly to private business risks, such as competition, product obsolescence, the economy, and so forth. All businesses have risk of earnings loss, and aggressive management must find ways to insulate the corporation from those risks, utilities included.

Weightings Between Overall Corporate Performance and Individual Performance

Companies assigning a percentage weighting factor to overall corporate goal achievement and to individual performance objective achievement, in general, assign a higher percentage of weighting to overall corporate performance to individual positions higher in the corporate chain of command. The stated reason for this assignment
is that the broader an individual's responsibility in an organization, the better the understanding of corporate goals and the individual's ability to control the overall achievement of corporate goals.

Many plans in the surveyed companies have nearly 100 percent of their incentive compensation payout for the CEO and other top officers tied to overall corporate performance. As the organizational ladder is descended a smaller percentage of incentive payout is tied to overall corporate performance and a higher percentage is tied to individual performance, once threshold criteria are met. Utilizing this technique allows the pay for performance program to stay within the bounds of controlling goal achievement by the individual participant.

Eight of the eleven companies participating in the survey set individual performance objectives for each plan participate to determine how pool funds are distributed, once threshold criteria are met. Threshold criteria establish the level of pool funds available.

What criteria and methodology are used to establish individual performance objectives? This is usually done from the top down in the organization where the CEO, top officer group, and/or the Board of Directors of the organization establishes overall corporate objectives. These objectives are assigned to the appropriate senior executives of the organization. Senior executives, in turn, set the objectives of officers and managers reporting to them, which, when accomplished, will result in overall goal achievement. This process goes down the organizational line as far as needed to achieve the
goal.

Actual goal achievement is reviewed and certified by the reporting chain of command within the organization. In some companies there are senior officer or board compensation committees which review and certify all goal setting to make sure goals are set aggressively enough and in the right direction at the beginning of the plan year. They may also certify that the goals have been achieved at the end of the plan year, prior to payout.

Great Falls Gas Company has their outside auditors certify that the payouts are made according to the plan, when they complete their year end audit of the Company.

It is important to set clear, meaningful individual performance objectives. Many of the companies surveyed stated that improving the process of establishing individual performance objectives was an on-going high priority for plan effectiveness.

Many surveyed companies have target levels of performance to be achieved. If targets are surpassed, most plans payout more than 100 percent for those individuals. One plan allowed a 250 percent of payout to the individual exceeding target levels of performance. Other plan participants who do not meet target levels, usually must reach set threshold levels of performance before any payout is made. These levels are usually at least 80-85 percent of target levels to trigger a 25-50 percent payout.

Individual performance objectives are reviewed by the
Individual achiever as frequently as necessary. Individual objectives are always reviewed by superiors at the end of the plan year to determine objective achievement. Flexibility was built into most plans surveyed, to allow for changes in goals during the plan year, as necessitated by a change in corporate goals.

Individual goal achievers continuously assess factors affecting the need to change the direction of certain goals. If corporate strategy is changed at the top of the organization, this will likely necessitate the need to change individual performance objectives down the line immediately in order to achieve the new direction objectives. Adjustments are allowed by most plans to be made to the individuals affected by the change so they will know what they will have do to meet the new payout criteria and time frames. Also, usually some allowances are made for partial goal achievement on the original goals.

Most plans contain a very important feature in setting individual specific performance objectives, namely, to weight each objective based on its importance. Several surveyed companies indicated without weighting a participant may concentrate on the easier objectives and leave critical objectives till last. This can also be handled in an alternate way by assigning a completion date to each objective. This latter approach can be enhanced further by assigning a weighting to each objective (they must all add to 100 percent), so that a higher percentage of total payout is assigned to the more critical goals and therefore a higher level of effort is put forth to achieve those objectives. Approximately half of the
surveyed companies use the weighting approach.

Most companies using individual performance objectives, set from four to eight specific objectives for each plan participant. One company suggested that only two or three objectives be set for lower level managers and supervisors so that they can focus on the objectives better. The fewer objectives that can be set and still get the job done appears to be the better way to set objectives because it is easier to focus on a few rather than many. Examples of specific performance objectives are shown in APPENDIX 5.

**Level of Plan Payout Required to Adequately Motivate Participants**

The surveyed companies had wide variations in the amount of cash compensations for payout. The lowest was 6 percent and the highest was 50 percent of base pay for target goal achievement. The higher the participant's position in the organization, the higher the payout percentage of base pay for target level achievement. Because of the small size of the sample and the wide variation of payout levels reported, no attempt was made in this survey analysis to come up with an average payout level.

Larger companies usually had much higher individual target payout potentials than smaller companies. This is demonstrated below from AGA salary survey information gathered in the 1987 survey. The chart is a plot of key executive positions of all 99
companies reporting in the survey against 66 smaller companies with revenues under $500 million per year. Detailed summary tables from the AGA salary survey are included in APPENDIX 6.

FIGURE 1

A Comparison Of Pay For Performance Payout Percentages All AGA Companies Vs. Smaller AGA Member Companies (Under $500 Million in Annual Revenues)

Source:
The 1987 AGA Executive Salary Survey of Member Companies.

Note:
Officer Titles-Chief Ex. Officer (CEO), Chief Operating Officer (COO), Top Legal Officer (TLegal), Chief Financial Officer (CFO), Top Gas Supply Executive (GSE), Human Resource Executive (HRE), and Top Marketing Executive (Mkt).

Plans included in the AGA study were designed to trigger payout at target levels. The smaller companies survey showed that for lower level executives the payouts in the 10-12 percent of base pay range for target achievement, while in the larger companies they
were slightly higher at 15 percent. These lower payout percentages for target goal achievement were for the marketing executives and increased to 15 percent for CEO's of smaller companies. They reached near 30 percent for CEO's for the group containing the larger companies.

The AGA survey results, including the larger companies, show a larger spread of target payout levels between the CEO and other executives than did the smaller company group.

Have Pay For Performance Programs Accomplished Corporate Objectives?

In general, survey respondents believe that their pay for performance program is a strong tool in helping achieve corporate objectives and that if the program is designed properly, it stretches individual performance in the direction of corporate objectives. The "proof of the pudding" as stated by one plan coordinator, is when their industry is having difficulty in achieving satisfactory results but the company with a solid pay for performance program is doing well, that is, they are "bucking the trend." There were two surveyed companies which fit this category.

One company with a strong pay for performance program has reduced its workforce by 40 percent even though it is adding 10-15 thousand new customers each year and has not been before regulatory authorities to seek rate relief since 1982. That was the
year they implemented their pay for performance program.

There is broad belief by companies who have pay for performance programs that it has helped their organizations to better focus in on corporate objectives and has improved individual participant's performance. Also, by tying compensation to overall corporate objectives it builds team work. It rewards participants for a job well done, especially when tied to individual performance objective achievement.

There is a wide spread feeling by plan participants in companies not doing well financially that their plans need beefing up or changed even though they may acknowledge that their segment of the industry as a whole is not doing well at the present time.

Also if plan participants feel that a certain part of their plan compensation is out of their control, they believe that the plan is unfair and needs changing. As an example, one company had part of its threshold criteria tied to comparing its gas rates with peer group rate levels. It had not paid off since plan's inception. Consequently, there was a strong feeling by participants, that the criterion was not fair and that it needed changing.

**Major Problems with Pay For Performance Programs**

It appears from survey respondents that the designers of pay for performance programs should try to keep them as simple and straightforward as possible. If it is not clear to the plan participants
exactly how the plan works, there becomes suspicion and discontent with the plan.

One company surveyed had an elaborate formula that included the factors for threshold, group factors, individual goal weighting, and job ranking factors all plugged into the formula. The human resource manager responding to the survey gave his program a high rating for design and a much lower rating for effectiveness because of the lack of understanding of how the program works by most plan participants.

It seems clear from survey respondents that the more complexities a pay for performance program contains in its design the larger the on going communication effort required to satisfy the questions and understanding of the plan participants.

A second important problem with performance programs is the need to design effective, quality goals for individual achievement. This was mentioned several times in the survey, especially by respondents who were in the first year or two of the plan. It takes careful thought to construct an effective individual performance goal which is viewed as achievable by the plan participant but, yet, requires the employee to stretch his performance above levels previously achieved. Difficulty in setting specific performance objectives for individuals was not mentioned as often by plan respondents whose plans had been in service for several years.

Several respondents to the survey indicated that goals were too easy to achieve in the early phase of the program. They also
indicated that if this happens it is important to correct it quickly because plan participants can view the incentive awards as entitlements after receiving them for a few years without having to appreciably stretch their performance for them.

Another problem when program design leaves allocating all or part of the awards to the CEO or the Board based on their views of how the employee performed. Views can be very subjective. One large company responding to the survey had 25 percent of the incentive bonus left to the discretion of the CEO based on his judgement of how each participant performed. The practice was viewed as unfair by some plan participants. Other survey respondents also indicated that a program is more effective if individual goals are clear, so that the participant knows exactly what he has to accomplish to achieve his goal.

Two companies indicated problems with first line supervisors and lower middle management plan participants who did not relate well to corporate goals. Both did not believe they were getting the stretch in performance from these groups. Some were leaning toward having fewer individual objectives for lower level managers so that they might better focus on their objectives. Another respondent thought that the payout level was too low for lower level managers to provide the proper motivation toward the goals. One company was going to have focus groups of plan participants to determine the strengths and weaknesses of the plan. The plan would then be redesigned to consider overcoming the weaknesses.
One company indicated that because its plan included only job grades eleven and higher, they had a lot of requests to raise grade ten positions to grade eleven so they could be included in the plan. The company solved this problem by setting policy where all job grade changes from ten to eleven had to be approved by the CEO.

Overall, survey respondents were more likely to rate their pay for performance programs high if corporate objectives were being met and plan payout was occurring. Companies which were not doing well financially, in most cases, found respondents indicating major problems with the structure or administration of the program.

**Do Companies Design Their Own Pay For Performance Programs?**

Five of the eleven companies responding to the survey developed their own programs, usually after visiting with other companies as to how their programs were structured. Two companies used consultants to design their programs and four used a combination of company personnel and consultants. Even where consultants were used to design a company's program, the company has used in house expertise to refine and upgrade the program during the years of use. All survey respondents were in the process of refining some aspect of their pay for performance programs; it appears from the survey that pay for performance programs require continual honing to make them work effectively under changing
None of the companies responding to the survey has a formal auditing program to test the effectiveness of their pay for performance programs. The two companies which compare their bottom line performance with peer group companies indicated that their standing in the ranking with peers was the true test as to whether their programs were effective or not. One of these companies was ranked very high with peers and thought its performance plan was working very well. The other company was not ranked near the top with peers and thought its program was not working.

One responding company has a group of senior officers review the goals of each participant and they follow goal progress from goal reports. This helps them keep on track with corporate objective achievement and improves the quality of individual performance objectives.

There was only one respondent that indicated having a problem selling the concept of pay for performance to regulatory authorities. The PSC would not buy the concept that incentive awards which were based on current year ROE, was a known and certain quantity, even though incentive pay had been earned four years in a row by plan recipients. In the most current rate application the regulatory authority has challenged the company to set up an auditing program so it can be demonstrated how the pay for performance program is benefitting the ratepayer.
One company used the consulting firm which designed their program as an expert witness to sell the program to the Commission. Other respondents indicated that there was no problem because it was relatively easy to sell the Commission on the concept that tying pay to performance enhances overall effectiveness and is the "best bang for the buck" for the consumer. Three respondents indicated that had yet to test their incentive pay for performance programs with their regulatory authorities.
CHAPTER V

STUDY CONCLUSIONS AND RECOMMENDATIONS

Conclusions

The following conclusions are drawn from research and reflect the experiences—both good and poor—of other companies and their pay for performance programs. They also serve as guidelines for GFGC.

1.) Sending out survey forms to selected companies to gain information is not an effective method of collecting data about successful pay for performance programs. The telephone survey, which Great Falls Gas Company ended up using, is a very effective method to collect this information. It is important that the most knowledgeable individual about pay for performance is contacted to gain the most reliable information. In this case it was the human resource manager or officer of each company.

It is believed that a sufficient number of other company’s pay for performance programs were reviewed to gain the knowledge to effectively update Great Falls Gas Company’s pay for performance program.

2.) This study confirmed the importance of the need of utility management, today, to adapt to change. A prime way to gain flexibility to successfully deal with this changing world is through the development of an effective compensation program, which leads management and the company as a whole in the direction of strategic
objectives. An effective program which ties pay to performance can be the answer to many of these organizational needs.

Consultant and academic research is beginning to confirm that a greater correlation between pay and performance is occurring more frequently throughout the business world today than just a few years ago.

Gas utility companies reported the following advantages of their pay for performance programs:

a. Directs management focus on key results areas of the company, which will improve bottom line performance.

b. Helps build team effort to effective corporate performance.

c. Helps an organization change directions rapidly, which is critical in a constantly changing business environment.

d. Assists in the ability to retain and attract talented employees.

e. Is a program, if designed and implemented correctly, links pay to performance.

3.) Approximately 40 percent of the utilities reporting in the 1987 AGA Salary Survey had pay for performance programs, at least for their officers and many including middle managers and supervisors. As company size decreases, fewer companies have such programs.
It was not found that smaller companies, similar in size to GFGC, had tailored programs more suitable to GFGC, as originally hypothesized. Smaller companies had more modest pay for performance programs, which in many cases appeared to be less effective in motivating participants. Larger companies had better designed plans, which produced better overall results.

Great Falls Gas has had a program since 1982 and sees no logical reason why other small, as well as larger utilities, should not have such programs. The same proportional benefits should accrue to small utility shareholders, as well as to larger ones from pay for performance programs.

4.) A common thread of almost all surveyed companies was that they are looking to enhance their existing programs or enlarge their pay for performance programs to cover a larger portion of the management team. Three companies surveyed are looking to expand pay for performance to their entire work force in the next three years.

5.) All companies surveyed used threshold criteria tied to overall corporate performance to determine the amount of funds available in the payout pool. Threshold criteria was usually tied in large part to return on equity in some manner.

Companies who use earnings as the threshold used various criteria but the two most popular methods were:

A. Comparing actual returns of the company with the Allowed
Rate of Return set by the governing regulatory authority. This return was in most cases was ROE, but if the company had other companies under its ownership umbrella, it may use return on assets.

B. Comparing actual returns with a pre-approved profit plan or budgeted controllable expenses.

Minimum payouts (about 50%) in many plans began when 80-85 percent of the return levels set as the target objective are achieved and usually 100 percent payout is available for distribution when 100 percent of the target is achieved. Most plans also payout 110-150 percent of target incentive if higher levels of earnings above target are reached.

6.) Over half of the companies responding to the survey assigned a percentage weighting factor to overall corporate goal achievement and part to individual performance objective achievement. In general, they assign a higher percentage of weighting to overall corporate performance to positions higher in the corporate chain of command. The reason for this assignment is that the broader an individual's responsibility, the better understanding of overall corporate objectives, and the more direct influence he has in the overall achievement of corporate objectives.

7.) Many plans in the surveyed companies have nearly 100 percent of their incentive compensation payout for the CEO and other top officers tied to overall corporate performance. As the organizational ladder is descend, a higher percentage of payout is
tied to individual objective achievement, and a lesser amount to overall corporate performance.

8.) It is important that all participants in the program realize, that the company must perform well before individuals can do well. This brings home the realization that it is bottom line results that count for payoffs and not just working hard without looking ahead to the benefits to the total organization. Said another way it is "output that counts, not input."

Several respondents indicated that there were numerous in-house discussions that utilities were different because utility returns are tied to weather, while other types of businesses were not. It appears that utility Boards are not "buying the argument" that utilities are different because all plans surveyed were tied to threshold earnings levels.

Several respondents indicated that their Board's views were that utility earnings can be somewhat insulated from severe weather impacts by proper design of rates, aggressively seeking industrial loads, which are not weather sensitive, plus diversify into businesses with non-weather sensitive earnings.

9.) The methodology used to establish individual performance objectives usually starts from the top of the organization down. The CEO, top officer group, and/or Board of Directors of an organization establishes overall corporate objectives. These objectives are then assigned to the appropriate senior executives of the organization. Senior executives in turn set the objectives of officers and managers
reporting to them and so on down the line to the level necessary for
goal achievement.

The success of pay for performance is no doubt dependent on
the setting of corporate objectives in the direction which will produce
effective results. If ineffective corporate objectives are established
and achieved the outcome will be still be unsatisfactory. This
emphasizes the importance of sound strategic planning in order to
establish effective corporate goals.

10.) It is important to set clear, meaningful individual
performance objectives. For good motivation, it is also important
that plan participants buy into their performance objectives. They
should believe they are achievable and are worthy of achievement.
All companies surveyed, stated that improving the process of
establishing individual performance objectives was an on-going high
priority for plan effectiveness. Companies were more comfortable
writing performance objectives after the plan had been in effect for
several years. Companies with new plans showed more concern
about writing effective individual performance objectives.

Another very important feature in setting individual specific
performance objectives is to weight each objective based on its
importance. Without weighting, a participant may concentrate on
those more easily attained, and, perhaps, less important, until last.
Designers of pay for performance programs should try to keep them
as simple and straightforward as possible. If it is not clear to the
plan participants exactly how the plan works, there becomes
suspicion and discontentment with the plan.

11.) One of Great Falls Gas Company's prime questions going into this study was: Are payout levels for its own plan participants at a high enough level to get them to stretch their performance? Company lower level managers and officers are at a payout level of 6 and 7.5 percent of base pay respectively. Both secondary research and the gas utility survey results pointed towards minimum payouts at the 12-15 percent of base pay levels to adequately motivate plan participants.

CEO's incentive compensation levels were in the range of 25-50 percent of base pay and most plans tapered the incentive bonuses down for lower job grades to the minimum levels indicated above. Larger companies usually set higher incentive bonuses as a percent of base pay than smaller companies. It is not clear from this study why this latter phenomena occurs because smaller companies have lower base pay for comparable job title positions than larger companies. Lower base pay would result in smaller dollar payout even by setting the same percentage of base pay.

Several responding companies indicated that in determining the reasonableness of an individual's salary level with the marketplace, incentive pay is added to base pay in making such comparisons. Base pay with incentive pay should be a minimum of 5-10 percent above comparative marketplace midpoint base compensation levels to have an effective program. Base pay without incentive pay will usually be 5-10 percentage points below midpoint
market salary levels.

The cost or payout of an effective corporate pay for performance program usually ranges from 5-10 percent of total payroll. This is only paid in good earnings years because payout is based on meeting set earnings threshold criteria.

12.) A problem with pay for performance programs which leaves the allocation of all or part of the individual performance awards to the CEO or the Board, based on their view of how the employee performed, can cause suspicion by plan participants because the decision is subjective.

It is better to have all performance criteria clearly defined so that plan participants know exactly what has to be done in order to achieve payout.

13.) Two survey respondents indicated problems with first line supervisors and lower middle management plan participants not relating well to corporate goals. Both did not believe they were getting the improvement in performance from these groups to the extent of justifying incentive bonuses actually paid. To try to correct this situation companies are leaning toward fewer individual objectives, two to four, for lower level managers, so that they might better focus on their objectives. Another respondent to the survey thought that the payout level set for first line supervisors was too low and suggested raising it to at least 10 to 12 percent of base pay.

Since lower level supervisors frequently have a larger part of
their overall job responsibilities tied to routine work, many companies use their more established merit pay and job standards systems to evaluate performance in addition to setting incentive bonuses for specific performance objective achievement for this group.

14.) None of the companies responding to the survey have formal auditing programs to test the effectiveness of their pay for performance programs. Two companies think the use of peer group rankings of ROE is a true test on program effectiveness, i.e., if they rank high its working and vice versa.

15.) Great Falls Gas was the only company included in the survey statistics that indicated having a problem selling the concept of pay for performance to regulatory authorities.

Recommendations

After reviewing the results of the secondary research findings and the gas company's utility information survey, it appears that Great Falls Gas has good basic design of its pay for performance program. It has clear threshold criteria, based on ROE, to establish the payout pool. It has a higher percentage of payout tied to overall corporate objectives for top officers. Higher percentage of payout is tied to individual performance objective achievement further down the organization ladder. Individual performance objectives are weighted based on their importance.
The study results indicate that the payout level for lower level managers and supervisors, in Great Falls Gas' program are set too low. Payout for these participants should be raised from the 6-7.5 percent levels to the 12-15 percent range in order to provide the proper performance motivation! It also appears that the CEO should receive payout at 25 percent of base pay or higher, for achieving target objectives, while other lower level positions should taper down to the 12-15 percent range, as minimum pay levels.

The number of individual performance objectives for lower level managers and supervisors should be limited to two to four goals, so they can better focus on these goals. The merit pay plan should be continued to evaluate the routine portion of lower level supervisors and managers performance until more effective methodology is developed.

The findings from this study are convincing to Great Falls Gas management that continuing to hone and expand its pay for performance program is in the best interest of the shareholder. But expansion of the program should be done carefully and a step at a time so that full evaluation of the program can be made as it progresses. Honing of its existing program is a continuous process because of the changing marketplace and the changing needs of its employees from a motivational viewpoint.

If a utility has experienced several bad earnings years in a row due to weather, this should not necessarily mean the plan should be changed. If the plan is deemed fair by plan participants in good
earnings years, it may well be a sound program in poor earnings years too. A company should not be too hasty in plan changes before management has a chance to change conditions to be successful through goal achievement. It may take two to three years to show real progress in poor business climate conditions.

Overall, Great Falls Gas Company believes it achieved its information goals in this study, as set out in Chapter I.

There is need for further study on how pay for performance programs can be established for the remainder of the work force. Plus further study needs to be made to see if there are other forms of compensation, other than cash, which might be as effective or more effective in motivating employees to higher performance levels.
ENDNOTE REFERENCES:

1 Verespej, Michael A.; We'll Have To Earn Our Keep, April 18, 1988, Industry Week, pg. 57.


10 Ibid., 9


12 Ibid., 1
ENDNOTES CONTINUED:


14 Ibid., 1


16 Ibid., 15

17 Hills, Federick S.; Scott, K. Dow, Markham, Steven E. and Vest, Michael J.; Merit Pay: Just or Unjust Desserts, Personnel Administrator. September 1987, pages 53-59.

18 Ibid., 17

19 Ibid., 8

20 Ibid., 17

21 Ibid., 13

22 Ibid., 13


24 See Executive Compensation and Performance ( New York: Pentacle Press, 1982).


26 Ibid., 14
ENDNOTES CONTINUED:


28 AGA 1987 Executive Salary Survey, plus supplement for small utilities.
APPENDICES
APPENDIX 1

A COPY OF GREAT FALLS GAS COMPANY'S

1987 PAY FOR PERFORMANCE

MANAGEMENT INCENTIVE PLAN
Great Falls Gas Company & Subsidiaries
Pay for Performance Plan
F1988

A.I. ELIGIBLE PARTICIPANTS TYPE OF PROGRAM

Group A
Larry D. Geske, President & CEO ) Fixed
Warren L. Robinson, Sr. Vice President) Variable
&CTO

Group B
William J. Quast, Vice President
& Treas./Sec. )
Sheila Rice, Vice President Marketing ) Variable

Group C
John Allen, Corp. Attorney & Asst. Sec. )
Lee Conwell, Dir. Human Resources )
Gerald Dasinger, Dir. Corp Taxes & Acct.) Variable
George Malin, Asst. V.P. Operations )
Gary Parker, Asst. V.P. Administration )
Earl Terwilliger, Mgr. Cust. Acct. & )
Admin. Services. )

Pay for performance proceeds will be allocated on the basis of pay for performance criteria established by the Board of Directors and Senior Management of the Company (See Schedule I).

A II. PLAN COMMENCEMENT

The pay for performance program of Great Falls Gas Company will be 50% funded if the five year average on return on equity is greater than or equal to 12.5%. If the return on common equity is greater than or equal to 11.0% in the current fiscal year, the pay for performance plan will be funded by 50%. Either portion of the plan can be funded exclusive of the other portion of the plan. The rate of return on equity is to be based and calculated after tax.
The determination of the qualification of funding for the pay for performance plan will be determined by Arthur Young & Company of Denver Colorado at the end of the fiscal year.

The earned pay for performance dollars, if any, will be paid to a participant on a prorated basis if the participant is employed for more than nine (9) months of the plan year. The plan however, does not create a contractual obligation with the employees of Great Falls Gas Company. The Plan may be continued, discontinued, and/or modified at the discretion of the Board of Directors.

A. III. FUNDING LEVEL -- GROUP A

The pay for performance plan will be based on 16% of base salaries as the minimum funding level and would increase by 1% of base salaries for each 1% increase in the fiscal year return on equity over the PSC allowed rate of return, up to a maximum of 26.5% of base salaries. If only one of the fund criteria is met (fiscal year or five year average), the one qualifying the funding is used to determine the pay for performance payout. If both criteria are met, the highest return is used in determining the funding level.

A. IV. FUNDING LEVEL -- GROUP B

The pay for performance plan will be based on 10% of base salaries as the minimum funding level and would increase by 1% of base salaries for each 1% increase in the fiscal year return on equity over the PSC allowed rate of return, up to a maximum of 17.5% of base salaries. If only one of the fund criteria is met (fiscal year or five year average), the one qualifying the funding is used to determine the pay for performance payout. If both criteria are met, the highest return is used in determining the funding level.

A. V. FUNDING LEVEL -- GROUP C

The pay for performance plan will be based on 7.5% of base salaries as the minimum funding level and would increase by 1% of base salaries for each 1% increase in the fiscal year return on equity over the PSC allowed rate of return, up to a maximum of 12% of base salaries. If only one of the fund criteria is met (fiscal year or five year average), the one qualifying the funding is used to determine the pay for performance payout. If both criteria are met, the highest return is used in determining the funding level.
year average), the one qualifying the funding is used to determine the pay for performance payout. If both criteria are met, the highest return is used in determining the funding level.

SCHEDULE I

GREAT FALLS GAS COMPANY & SUBSIDIARIES
PAY FOR PERFORMANCE DISTRIBUTION CRITERIA

PAYOUT SCHEDULE

The pay for performance funds will be approved and paid out to participants at the first regularly scheduled meeting of the Board of Directors following the annual audit of the books of the company. The funds will be distributed in accordance with the following guidelines and with the individual performance rating being determined by the Board of Directors and Senior Management.

The pay for performance fund will be calculated using the base Compensation of the participants in the plan. Distribution of the funds will be based on a fixed percentage of the fund as outlined below.

<table>
<thead>
<tr>
<th>Incentive Group</th>
<th>Description</th>
<th>Factor</th>
<th>Weight</th>
<th>Rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>A</td>
<td>President &amp; CEO</td>
<td>Corporate 100%</td>
<td>55%</td>
<td></td>
</tr>
<tr>
<td>A</td>
<td>Senior Vice-President &amp; CFO</td>
<td>Corporate 40%</td>
<td>45%</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Individual* 60%</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>B</td>
<td>Vice President</td>
<td>Corporate 20%</td>
<td>50%</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Treasurer/Sec.</td>
<td>Individual* 80%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>B</td>
<td>Vice President</td>
<td>Corporate 20%</td>
<td>50%</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Marketing</td>
<td>Individual* 80%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>C</td>
<td>Asst. Vice-President Admin.</td>
<td>Corporate 20%</td>
<td>18%</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Individual* 80%</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

58
*Based on special objectives approved by the President, each year.

(SEE ATTACHMENT 1 FOR LISTING OF INDIVIDUAL PERFORMANCE OBJECTIVES)
APPENDIX 2

A SUMMARY OF UTILITY SURVEY RESULTS
Q1. A.) Does your company have a pay for performance program

Responses From 17 surveys sent out:

11 yes. 2 No 4 No response

Q1.B.) Please describe the general structure of your pay for performance plan

<table>
<thead>
<tr>
<th>Threshold Qualification for plan payout</th>
<th>Specific Performance for Actual Payout</th>
<th>Level of Payout- % Pay</th>
</tr>
</thead>
<tbody>
<tr>
<td>Co. 1 5 year rolling Average ROE=50%</td>
<td>President 100% Based on threshold criteria</td>
<td>16% of actual sal. paid</td>
</tr>
<tr>
<td></td>
<td>Each additional 1% ROE over threshold</td>
<td>1% additional bonus</td>
</tr>
<tr>
<td></td>
<td>Sr. V.P. 40% Based on threshold-60% spec. perf. obj.</td>
<td>15% of actual sal. paid</td>
</tr>
<tr>
<td></td>
<td>Each additional 1% ROE</td>
<td>same as president</td>
</tr>
<tr>
<td></td>
<td>V.P. 20% Based on threshold -80% spec. perf. obj.</td>
<td>10% of actual sal. paid</td>
</tr>
<tr>
<td></td>
<td>Each additional 1% ROE over threshold</td>
<td>1% additional bonus</td>
</tr>
<tr>
<td></td>
<td>mgs &amp; Key Staff Same as V. P.</td>
<td>7.5% of actual sal. paid</td>
</tr>
<tr>
<td></td>
<td></td>
<td>1% additional bonus</td>
</tr>
<tr>
<td>Current Year ROE =25%</td>
<td>Supvrs 25% Based on threshold ROE</td>
<td>1.50%</td>
</tr>
<tr>
<td>Specific Performance Object=75%</td>
<td>75% Based on Spec. Perf. Objectives</td>
<td>4.50%</td>
</tr>
</tbody>
</table>

Q1.B.) Please describe the general structure of your pay for performance plan (Continued)

<table>
<thead>
<tr>
<th>Threshold Qualification for plan payout</th>
<th>Specific Performance for Actual Payout</th>
<th>Level of Payout- % Pay</th>
</tr>
</thead>
<tbody>
<tr>
<td>Co. 2 Must Achieve min. of 80% of ROE</td>
<td>Chrm-CEO 50% of Base Pay</td>
<td></td>
</tr>
<tr>
<td>Stated in Approved Profit Plan</td>
<td>Vice Chrm 45 * * *</td>
<td></td>
</tr>
<tr>
<td>80 % = 50% Payout</td>
<td>EX. V.P. 40 * * *</td>
<td></td>
</tr>
<tr>
<td>85 % = 62.5% Payout</td>
<td>Sr. V.P. 37.5 * * *</td>
<td></td>
</tr>
<tr>
<td>90 % = 75% Payout</td>
<td>V.P. 35 * * *</td>
<td></td>
</tr>
<tr>
<td>100 % = 100% Payout</td>
<td>Ast. V.P. 32.5 * * *</td>
<td></td>
</tr>
<tr>
<td>105 % = 112.5% Payout</td>
<td>RegionMgr 30 * * *</td>
<td></td>
</tr>
<tr>
<td>110 % = 120% Payout Maximum</td>
<td>Sr. Mgrs-Lrg Areas 25 * * *</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Grd 13 Dept Hds. 20 * * *</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Grd 12 Mgrs-Dir 15 * * *</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Grd 11 Mgrs.-Stff(sml dept) 12.5 * * *</td>
<td></td>
</tr>
</tbody>
</table>
Co. 3
Must Achieve min. of PSC allowed ROE
20 Controllable Expense items = 50%
Return on Total Assets (PSC Allow) = 50%

Group
Bonus  Scale of payout if Controllable Exp is a-
inclds  100% Budgeted Exp. = 0% Payout
Officers+  95% Budgeted Exp. = 1.0%
Dept Heads  90% Budgeted Exp. = 2.0%
Supvrs.  85% Budgeted Exp. = 2.5%

Scale of Payout if Return on Total Asset
PSC Allowed Return on Assets = 0%
1% Over PSC Allowed = 1.0%
1.5% Over PSC Allowed = 1.5%
2.0% Over PSC Allowed = 2.0%
2.5% Over PSC Allowed = 2.5%
3.0% Over PSC Allowed = 3.0%

Co. 4
Threshold - must earn PSC Allow ROE

Co. 5
Compensation at risk is two pronged-
1. Long Term Incentive earned over 3 years,
   stock options- tied to corporate ROE peer group
   ranking- higher then 25 percentile- 50% payout,
   above 50th percentile- 100% payout
   above 75th quartile (150% Payout)
   Stock options awarded to individuals as they
deem performance warrants
2. Annual Cash Bonus tied to meeting specific
   performance objectives for each participant which enhance the
   Company's bottom line performance-
   top 10 salary grades eligible down to Asst. VP

<table>
<thead>
<tr>
<th>Job Grade</th>
<th>titles eligible</th>
<th>Thres.</th>
<th>Target</th>
<th>Max (% Base)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1- COB/Pres/C</td>
<td>15</td>
<td>35</td>
<td>70</td>
<td></td>
</tr>
<tr>
<td>2-4 V. Chrm/Pr</td>
<td>15</td>
<td>35</td>
<td>60</td>
<td></td>
</tr>
<tr>
<td>5-6 EX. Vp/Sr. V</td>
<td>15</td>
<td>30</td>
<td>55</td>
<td></td>
</tr>
<tr>
<td>7-8 Sr VP/VP</td>
<td>12</td>
<td>25</td>
<td>45</td>
<td></td>
</tr>
<tr>
<td>9-10 Avp</td>
<td>10</td>
<td>20</td>
<td>35</td>
<td></td>
</tr>
</tbody>
</table>

Q1.B.) Please describe the general structure of your pay for performance plan (Continued)
Specific Performance for Actual Payout
8 Employees Eligible- 8 officers, mgs, key staff
CEO and two Board Members (one inside-one ou
determine who gets how much, determination is
strictly subjective based on how they saw each
participant's performance in prior year.
Q1.B.) Please describe the general structure of your pay for performance plan (Continued)

**Threshold for plan payout qualification**

Company No. 6

<table>
<thead>
<tr>
<th>Current year Utility Rate of Return Compared to Profit Plan ROE</th>
</tr>
</thead>
<tbody>
<tr>
<td>Two criteria:</td>
</tr>
<tr>
<td>1) Return on Equity less inflation rate - 60%</td>
</tr>
<tr>
<td>2) Ranking with peer group companies of ratio of customers/employees - 40% weighting</td>
</tr>
</tbody>
</table>

**Specific Performance for Actual Payout**

<table>
<thead>
<tr>
<th>Min Payout Level</th>
<th>Target Payout Level</th>
<th>Max. Payout</th>
</tr>
</thead>
<tbody>
<tr>
<td>67% if Profit Plan ROE less inflation rate is met</td>
<td>100% if Profit Plan met</td>
<td>150%</td>
</tr>
</tbody>
</table>

% payout by job title not obtained

**Company No. 7 Weighted on 3 factors**

- 15% on Meeting ROE of Parent Co
- 45% on “ “ Distbr Co.
- 40% on Meeting individual specific perf. object

**Guideline Bonus Amounts**

<table>
<thead>
<tr>
<th>Division Heads</th>
<th>Executives Levels 17 and Above</th>
<th>Management Levels 14-16 and PAT 8</th>
<th>Management Levels 9-13</th>
</tr>
</thead>
<tbody>
<tr>
<td>12%</td>
<td>10</td>
<td>6</td>
<td>4</td>
</tr>
</tbody>
</table>

**Individual performance rating**

<table>
<thead>
<tr>
<th>Perf. Rating</th>
<th>% Payout</th>
</tr>
</thead>
<tbody>
<tr>
<td>5</td>
<td>100%</td>
</tr>
<tr>
<td>6</td>
<td>150%</td>
</tr>
<tr>
<td>7</td>
<td>200%</td>
</tr>
<tr>
<td>8-9</td>
<td>250%</td>
</tr>
</tbody>
</table>

**Threshold based on ranking of company with 10 peer group companies-each year Board of Directors decides min. ranking to qualify for incentive program—This year Company must rank 4th highest of peer group in order for program to trigger to min. levels last year were at bottom of peer group co.s no pay out top of peer group - 150% payout 2nd 100% 3rd 50 4th 25

Company can be losing money and individual can still receive some payout

Program applies to Sr. V.P.'s and above

% Payout of base pay not available
Q1.B.) Please describe the general structure of your pay for performance plan (Continued)

Threshold for plan payout qualification
Company No.9  Must achieve ROE threshold set level
weighting of award: 60% ROE
-40% on controllable O & M

Specific Performance for Actual Payout
There are 60 people in program
awards based on individual achievement of goals

Pool dollars determined for ROE and Control O&M By:
Min payout-85% of target
Target- 100%
Max - 110%

Payout target awards
CEO-25%
Executives Direct Reporting to Pres-20%
Officers reporting to Exec.s-15%
Mid Managers-10%

Company No.10  3 year rolling ROE set at PSC allow ROE
23 executives eligible for program- participants
selected by president

pool is 10% of aggregate salaries
Maximum award is 25% of base pay
awards are made based on achievement of
individual goal achievement

only information available

Company No.11 Bonus program is tied to major corporations
management incentive program
50% weighting to consolidated corp.'s ROE
50% * * individual performance

payout to individual
ROE-3% of payroll
Individual performance-3% max.

Parent company has been very depressed
in earnings for many years, not much payout
Q. 2. Why did your Company establish your pay for performance program?

Summary of responses: Wanted to establish a pay system which:

a. Directed individual effort of officers and managers to key results areas of the Company to improve bottom line results.

b. Wanted a program to build a team effort to improve performance

c. Wanted a program to help change direction of the organization with a constantly changing business.

Q.3. How long have you had your pay for performance program?

<table>
<thead>
<tr>
<th>Number of Responses</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 year-</td>
</tr>
<tr>
<td>2-5 years-</td>
</tr>
<tr>
<td>6-10 years-</td>
</tr>
<tr>
<td>over 10 years-</td>
</tr>
<tr>
<td>no response</td>
</tr>
</tbody>
</table>

median Length of Time Since Inception= 5 years
Q.4. Do you set individual or group performance objectives?

<table>
<thead>
<tr>
<th>Individual</th>
<th>Group</th>
<th>Both</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>2</td>
<td>8</td>
</tr>
</tbody>
</table>

Q.5. Could you please provide at least four (4) examples of individual or group performance objectives?

Response: Several examples were sent in and they are included in the Appendix of this report.

Q.6. How frequent are performance objectives reviewed for change?

<table>
<thead>
<tr>
<th>Quarterly</th>
<th>semiannual</th>
<th>annually</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>10*</td>
<td></td>
</tr>
</tbody>
</table>

*Four responses: If a change in department or corporate strategy changes during the year, specific performance objectives are changed at that time.

Q.7. A.) How do you measure whether an individual has achieved all or a portion of his or her objectives?

Responses: An employee may receive partial credit for an
objective it the supervisor so chooses. Objectives are hard and fast and it is relatively simple to determine if objectives have been achieved.

B.) Do you weight each objective?
Responses: Weighted Not Weighted
5 6

Q.8. Who is included in your pay for performance program?
Responses: See Q.1. Responses too.

Senior Officers Only All Officers Officers, Managers Off., Mgrs., Supvr.
2 1 4 4

Q.9. Why have you limited your program to only these individuals listed above

Responses:
Have expanded program Other Responses:
which used to only include Has included same individuals
for over 10 years since incept.

8* Will expand to supvr. level next year.

*Three responses: Plan on expanding pay for performance to entire work-force in near future.

Q.11. Has your program accomplished your overall corporate objectives for establishing the program?

Responses:

Company No. 1-It has accomplished most of our objectives. I believe we may need to raise the level of potential pay out for supervisors and managers to make the incentive more motivating to participants. We want to expand the program to all employees within 3 years. Officers and Managers take the same risks as shareholders; i.e. regulatory, weather, and the economy. Supervisors only take 25% of shareholder risk the other 75% is tied to their specific performance objectives which are paid if achieved, whether the Company earns its return or not.

Company No. 2- The 30% weighting tied to comparing our rates with other utilities in the region is a comparison which is difficult to make and plan participants feel it is out of their control. We are looking for other criteria which may be more meaningful to the company and participants.

Plan are designed so that participants take the same risks as shareholders, such as, regulatory, weather, and the economy. They believe this is the way it should be; i.e. if the shareholder benefits,
shareholders, such as, regulatory, weather, and the economy. They believe this is the way it should be; i.e. if the shareholder benefits, then they should too, and vice versa.

Company No. 3- Our Company is a small part of the total consolidated corporation. The return on assets 50% weighting we feel is out of our hands since corporate adds and deletes to capital additions. We feel we do not have control of this portion of the program. Plan participants take the same risks as the shareholder. If the shareholder benefits plan participants benefit if 20 controllable expense item criteria is met total payout occurs.

Company No. 4- The granting of the bonus awards is strictly up to the compensation committee of the Board and I'll admit is very subjective. I'm looking for a more formal plan and will look forward to receiving a copy of your study.

Company No. 5- Yes, the proof of the pudding is that our ROE is at the top of our peer group companies. In the cash bonus program, we need to set more specific performance criteria for each participant for more accurate determination of goal achievement.

Company No. 6- plan has been in place only one year. There were several bugs in the plan on implementation which are now being worked out. It has for manager level on up. Also the CEO has discretion to change to a particular employee based on how the CEO values each individual's performance. This discretion can equate to up to 25% increase or decrease in individual's performance.

Company No. 7- The results at the supervisory level have been disappointing in that we don't feel they relate to overall corporate goals very well and therefore have not seen measurable
improvements in their performance.

Company No.9.- Program has increased focusing in on corporate goals and has improved individual participant's performance. Our industry segment is going through tremendous change and we're still struggling. People now know that they have to produce or there's no big payoff.

Company No.10.- Prior to this time the Board made the decision as to how incentive awards were made. Now corporate goals are met and personal objectives must be achieved too, for payout.

Company No. 11.-No. Incentive levels too low.

Q.12. What are the true strengths of your program?

Summary of Responses: Corporate objectives are met and employees have bought into the program. We are more successful. We are working more as a team. One of the performance objectives is that ROE must rank well among our peer group companies; since our earnings are the highest of the group I would say we are successful.

Goals are set annually top to bottom, more cohesive organization; more challenges to all members of management.

Our program has only been in place for a year so it's difficult to say whether it's successful yet.

Reward managers for jobs well done.

Shoves decision responsibility down the organization for more effective decision making. We have also implemented zero based
budgeting in our organization which has kept us out of filing for rate increases since 1982. Our work force has decreased from 2500 employees to 1650 but are still adding 10-15 thousand new customers per year. Our whole management team is geared to the thinking that there is always a better way to get the job done, thanks to pay for performance.

Focuses in on Corporate and individual goals and performance.

Tightens the tie of individual performance to corporate objectives.

Q.13. What are the weaknesses of your program?

Responses:

Co. 1- see responses in Q.11

2- Much upward pressure was experienced to upgrade grade 10 employees into the program since it starts at grade 11. Now the Chairman of the Board must approve all grade changes for 10 to 11, which has solved the problem.

Co. 3- see responses in Q.11

Co. 4- " " " "

Co. 5- " " " "

Co. 6- Concerned of the cost of the program which equates to a max of 1 % of earnings. Plus the way our pension benefits program is written it may run pension costs up too fast.

Co. 7- Incentive program at the supervisory level is not effective; they do not seem to have a grasp of overall corporate goals and the meaning of return to shareholder. Also, need better quality goals for all; we now have 4-7 for each participant, I believe 2-3 for
first line supervisors might focus their attention better.

Co. 8- Very difficult to get agreement on fairness of goals and payoff between our 6 different companies, there is a lot of bickering about how unfair some goals are compared to their tough goals. Many don't fully understand the program which causes more friction. I believe our program is too complicated and needs to be simplified and better communicated as to how it works.

Co. 9- Communications difficult. Lower level managers think it is an entitlements program; doesn't seem to be a strong enough tie of pay to performance. We are setting up focus groups to get feedback as to what the strengths and weaknesses are from participants so program can be improved. Some feedback indicates that they do not fully understand how the program works, so we may need to do a better job of explaining the program to participants.

Co. 10- Plan only two years old, some worried about the cost of the program.

Co. 11- No response to this question.

Q.14. If you were just setting up your program today what would you do differently?
Responses: Answers the same as Q.11 outlining weaknesses.

Q.15. On a scale of 1 to 10 where would your rank your pay for performance program( with 10 being the highest and best rating)?
Responses:
Co. No. 1- 7 rating
" " 2- 8 "
" " 3- 5 "
" " 4-No rating given
" " 5-No rating given

Co. No. 6- on enthusiasm an 8 or 9 rating, on other areas the program is too new to rate (1 yr).

Co. No. 7- I would rate our program an 8 w/o first line supervisors and only a 5 rating with them in the program.

Co. No. 8-A 5 rating.

Co. No. 9-Rating on the design of program=8-9
Rating on the administration of plan=5-6

Co. No. 10 & 11- No rating given

Q.16. Has your Company developed its own Pay for Performance program or what was the source of its origination?

Responses:

<table>
<thead>
<tr>
<th>Developed own program</th>
<th>Used Consultants</th>
<th>Used Both</th>
</tr>
</thead>
<tbody>
<tr>
<td>5</td>
<td>2</td>
<td>4*</td>
</tr>
</tbody>
</table>

* Three responses: Used consultants initially to set up program and have been trying to streamline it in house.

Q.17. Did you use the aid of an outside consultant to establish your program? If so who was the consultant?

Response to first part of this question is shown in Q.16.

Consultants Used: Booz-Allen (Lou Brandize)
Q.18. Do you have a measurement system, which determines how cost effective your program is, such as, comparing the payroll cost of your program with bottom line improvement?

Responses:

Not at this time  Yes
7*  4**

*Co. No. 1- We have set up an auditing task group to develop the criteria for determining the success of the pay for performance program.

** Co.s No. 5 & 8- We feel the comparison with our peer group ROE is a good indication of how effective the program is; i.e. compensation dollars spent on at risk incentive pay, returns to shareholder many times over.

Co. No. 7- Have a group of senior managers who review goals of each participant from goal reports to check progress of goal achievement.

Co. No. 9- Board must approve targets, plus we review how we did as a whole group.

Q.19. Have you sold the concept of pay for performance to your Public Utility Commission for rate making purposes?
Responses:

Company No. 1- The PSC allowed half of our bonus in the cost of service which was tied to the rolling 5 yr. average of ROE, but denied the other half tied only to the current year's ROE. In our most recent case they allowed all of the pay for performance incentive pay but warned us that next rate case we would have to fully justify all of it as to how it benefitted the rate payers. That is why we have set up an auditing task force to develop the audit criteria.

Co. No. 2. PSC is aware of the program but are just testing the concept.

Co. No. 3. Program is new and untested with PSC.

Co. No. 4. No response to this question.

Co. No. 5. FERC has no problem with program- one state Commission is currently having problems with understanding our long term stock option program.

Co. No. 6. Our's is a new program and has not been presented to PSC's.

Co. No. 7. Had no problem selling program to PSC because it enhances our overall effectiveness and its the best bang for the buck.

Co. No.8. Have had no problem with regulatory approvals.

Co. No.9. Program was reviewed in 1984 by PSC, we had the consultant testify to the merits of the program; since then no problems from regulators.

Co.'s No. 10 & 11. No response to this question.
APPENDIX 3

A LISTING OF GAS UTILITIES PARTICIPATING IN

THE GAS UTILITY SURVEY
Listing of Gas Utility Companies
Who Responded To This Survey

1. ARKLA
2. Carnigie Natural Gas Company
3. Citizens Gas Company
4. Consumers Power Company
5. Gas Company of New Mexico
6. Great Falls Gas Company
7. Kansas Public Service Company
8. Michigan Gas Utility
9. Michigan Gas Utility
10. Southwest Gas Corporation
11. TRANSCO
APPENDIX 4

SOLICITATION COVER LETTER AND

UTILITY SURVEY FORM
Dear Name:

Great Falls Gas Company has had an executive and managerial Pay for Performance Program since 1982, two years ago we extended it to include first line supervisory personnel. We are continually looking for information to make our program more effective. This survey is an attempt to accomplish this objective.

We are surveying two dozen gas utility companies who have Pay for Performance programs, so that we might adopt the most effective methods and techniques found by other’s experience.

We will consolidate our survey findings into a report which we would be happy to share with participants of this study. All corporate names will be kept confidential and the information will be consolidated and tabularized as much as possible. We will list the companies who have participated in the study.

We are thanking you in advance for your participation and look forward to receiving your response and reviewing your program. If you have questions about the survey, please call me (406 761-7100).

We would appreciate the return of the completed survey form by May 6, 1988. A pre-paid envelope is enclosed for your convenience. A copy of the finished report will be sent to you by mid June 1988.

Sincerely,

Larry D. Geske  
President and CEO
Survey Form
Pay For Performance

Pay for performance is defined as a compensation program which sets individual performance objectives for individual supervisors, managers and officers of the company and are paid additional compensation for achieving those objectives. If you need additional space please attach additional sheets and refer to survey question number.

1. Does your company have a pay for performance program? If so would you please describe or include a copy of program description?

2. Why did your Company establish your pay for performance program?

3. How long have you had your pay for performance program?

4. Do you set individual or group performance objectives? If group how have you set up your groups (who is included)?
5. What is the basic corporate criteria used in setting individual or group performance objectives? Could you please provide at least four (4) representative examples for corporate objectives (such as return on equity, customers / employee) and four for specific individual or group performance objectives (performance objectives set specifically for their job or group achievement)?

6. How frequent are performance objectives reviewed with the individual by superior(s)?

7. How do you measure whether an individual has achieved all or a portion of his or her objectives (do you weight each objective)? Could you please provide examples?
8. Who is included in your pay for performance program? Would you please list them by job title and include the % of their base pay which is at risk (amount tied to specific performance objectives)?

<table>
<thead>
<tr>
<th>Individuals included, by job title</th>
<th>% Base Pay Tied To Perf. Objectives</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
</tr>
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<td></td>
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</tbody>
</table>

9. Why have you limited your program to only these individuals listed above?

10. How do you tie pay for performance objective achievement into compensation (i.e. is part of the at risk compensation tied to overall corporate performance, such as return on equity and part to specific individual performance objectives)? Please state the % of compensation tied to overall corporate objectives versus % tied to individual performance objectives for each individual or group.

-----------
11. Has your program accomplished your overall corporate objectives for establishing the program? Please elaborate as to why you think it has or has not accomplished corporate objectives?

12. What are the true strengths of your program?

13. What are the weaknesses of your program? Briefly state why they are weaknesses.

14. If you were just setting up your program today what would you do differently?

15. On the scale shown where would you rank your Company's Pay For Performance Program for effectiveness? (please circle your choice)

Worst 1 2 3 4 5 6 7 8 9 10 Best
16. Has your Company developed its own Pay For Performance program or what was the source of its origination?

17. Did you use the aid of an outside consultant to establish your program? If so who was the consultant?

18. Do you have a measurement system, which determines how cost effective your program is, such as, comparing the payroll cost of your program with bottom line improvement?

19. Have you sold the concept of pay for performance to your Public Utility Commission for rate making purposes?
APPENDIX 5

EXAMPLES OF SPECIFIC PERFORMANCE

OBJECTIVES BY THREE COMPANIES
<table>
<thead>
<tr>
<th>Position Objective Number</th>
<th>Statement of Position Objectives</th>
<th>Target Date</th>
<th>Actual Accomplishment</th>
<th>Performance Evaluation</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Maintain uncollectibles at or below 1987 budget level of 18,014.86.</td>
<td>12/31/87</td>
<td>$13,115.00 or 15.7%</td>
<td>E</td>
</tr>
<tr>
<td>2</td>
<td>Maintain 1987 Customer Services Department expenditures at or below the 1987 budgeted level of $19,614.61.</td>
<td>12/31/87</td>
<td>$19,614.61</td>
<td>E</td>
</tr>
<tr>
<td>3</td>
<td>Identify and implement revenue expansion and/or cost reduction actions resulting in annual Company benefits of $1,000,000.</td>
<td>12/31/87</td>
<td>$1,000,000</td>
<td>E</td>
</tr>
<tr>
<td>4</td>
<td>Maintain 60-day receivables quality within the 95% guidelines established in the financial stabilization borrowing agreement with Citizens.</td>
<td>12/31/87</td>
<td></td>
<td>E</td>
</tr>
<tr>
<td>5</td>
<td>Implement at least five action steps of the Customer Relations Plan.</td>
<td>12/31/87</td>
<td></td>
<td>E</td>
</tr>
<tr>
<td>6</td>
<td>Complete the major customer database phase of the Customer Information Project.</td>
<td>12/31/87</td>
<td></td>
<td>E</td>
</tr>
</tbody>
</table>

**Performance Evaluation**

- E: Excellent
- D: Decent
- F: Fair
- P: Poor
- I: Incomplete

**Rating Scale**

- Overall Rating of Accomplishment: %
- Date: 12/31/87

**Established by: **

**Reviewed by: **

Date: 02/06/87

Date: 02/27/87
DEPARTMENT HEAD
FLEET 6 FACILITIES
1988 GOALS

<table>
<thead>
<tr>
<th>GOAL</th>
<th>STRATEGY</th>
<th>METHOD OF MEASUREMENT</th>
</tr>
</thead>
<tbody>
<tr>
<td>Develop a long-term facilities plan for the Metro facilities which responds to corporate needs and community development pressures.</td>
<td>1.A. Evaluate all available customers, employees, and system design information to determine future needs for facility locations.</td>
<td>1 A.1. Detailed report developed by 5/1/88.</td>
</tr>
<tr>
<td></td>
<td>1.B. Analyze space and use requirements by Division/Departments to develop building and site needs to establish base costs.</td>
<td>1.B.1. Building and site needs established and documented by 6/1/88.</td>
</tr>
<tr>
<td></td>
<td>1.C. Identify alternatives to existing facilities and sites along with projected financial impact to</td>
<td>1.C.1. Alternatives and financial impacts developed by 10/1/88.</td>
</tr>
<tr>
<td></td>
<td>1.D. Incorporate all analysis into a comprehensive plan which will be responsive to future needs.</td>
<td>1.D.1. Comprehensive Plan developed and approved by 12/31/88 and implemented consistent with milestones.</td>
</tr>
<tr>
<td>Evaluate Assigned Car Policy eligibility and financial impact to</td>
<td>2.A. Evaluate current fleet practices and fleet information on eligibility criteria and cost to employees of a company furnished car.</td>
<td>2.A.1. Poll completed by 2/31/88 and documented.</td>
</tr>
<tr>
<td></td>
<td>2.C. Recommend changes supported by analysis and publish to all affected management personnel.</td>
<td>2.C.1. Changes recommended and approved by 6/1/88 and implemented per milestones identified in final report.</td>
</tr>
</tbody>
</table>
**FLEET & FACILITIES**  
**1988 GOALS**

<table>
<thead>
<tr>
<th>GOAL</th>
<th>STRATEGY</th>
<th>METHOD OF MEASUREMENT</th>
</tr>
</thead>
<tbody>
<tr>
<td>Manage operating expenses not to exceed $5,407,500 for 1988 Budget.</td>
<td>3.A. Analyze and evaluate operational effectiveness for services provided and implement plans to achieve $0,000 in savings through more efficient utilization of available resources.</td>
<td>3.A.1. Plans developed by 4/15/88 and implemented consistent with milestones.</td>
</tr>
<tr>
<td>WEIGHTED 0 15%</td>
<td>3.B. Review all departmental spending plans for 1988 and reduce expenditures by $50,000 while maintaining quality services to</td>
<td>3.B.1. Document expense reductions by 3/15/88 and implement.</td>
</tr>
<tr>
<td></td>
<td>3.C. Evaluate departmental operating programs and assure a flexible organization where functions are cost effective, with programs and procedures effectively supporting Company, divisional, and departmental goals using a zero-based management approach.</td>
<td>3.C.1. Plans developed by 3/15/88 and implemented consistent with established milestones.</td>
</tr>
<tr>
<td></td>
<td>3.D. Develop key operating indicators for Fleet &amp; Facilities which can be used to measure and improve performance.</td>
<td>3.D.1 Measures identified by 2/28/88.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>3.D.2 Tracking system implemented by 3/31/88 with reporting to divisional VP on a semi-annual basis</td>
</tr>
</tbody>
</table>
# Fleet & Facilities
## 1988 Goals

<table>
<thead>
<tr>
<th>Goal</th>
<th>Strategy</th>
<th>Method of Measurement</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Develop a comprehensive corporate security plan to protect property and ensure employee safety.</td>
<td>4.A. Analyze and evaluate all current security problems and recommend solutions to enhance site and building integrity.</td>
<td>4.A.1. Detailed report developed by 7/1/88.</td>
</tr>
<tr>
<td></td>
<td>4.B. Incorporate all findings and recommendations into a comprehensive plan for ensuring safety and security at all property sites.</td>
<td>4.B. Plan developed and approved by 9/1/88 and implemented consistent with milestones.</td>
</tr>
<tr>
<td></td>
<td>4.C. Clearly communicate to all employees corporate security expectations for all buildings and property sites.</td>
<td>4.C.1. Security expectations communications to all employees by 12/31/80.</td>
</tr>
<tr>
<td>5. Develop at least 2 enhanced services to customers in other divisions or companies.</td>
<td>5.A. Evaluate services provided to other divisions and DEI companies and develop plans for providing services at a more cost efficient rate or increased quality at the same rate.</td>
<td>5.A.1. Services identified and plan developed by 3/30/88.</td>
</tr>
<tr>
<td>6. Market excess properties to effectively support financial goals.</td>
<td>6.A. Evaluate all excess properties and develop a strategic marketing plan which establishes criteria for sale of properties.</td>
<td>6.A.1. Plans developed for all major properties by 3/15/80 and implemented consistent with plan milestones.</td>
</tr>
<tr>
<td>GOAL</td>
<td>STRATEGY</td>
<td>METHOD OF MEASUREMENT</td>
</tr>
<tr>
<td>----------------------------------------------------------------------</td>
<td>--------------------------------------------------------------------------</td>
<td>---------------------------------------------------------------------------------------</td>
</tr>
<tr>
<td>Manage operating expenses consistent with Division and Company Goals. (20%)</td>
<td>1.A. Departmental operating expenses will not exceed: $284,883.</td>
<td>1.A.1. Financial reports.</td>
</tr>
<tr>
<td></td>
<td>1.B. Utilising zero-based management, evaluate service programs and</td>
<td>1.B.1. Plan developed and opportunities identified by the end of first quarter 1988</td>
</tr>
<tr>
<td></td>
<td>internal departmental procedures, including automated systems, to</td>
<td>and implemented consistent with established milestones.</td>
</tr>
<tr>
<td></td>
<td>identify approaches for effectively supporting Company and divisional</td>
<td></td>
</tr>
<tr>
<td></td>
<td>goals.</td>
<td></td>
</tr>
<tr>
<td></td>
<td>2.A. Develop and implement at least one enhanced service to customers in</td>
<td>2.A.1. Service developed by 3/30/88.</td>
</tr>
<tr>
<td></td>
<td>other divisions.</td>
<td>2.A.2. Develop and implement tracking system by 4/30/88 with reports to Div. V.P. by</td>
</tr>
<tr>
<td></td>
<td></td>
<td>7/30/88 and 9/30/88.</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>2.B. Identify and implement at least one enhanced service for other</td>
<td>2.B.1. Service identified and developed by 4/1/88.</td>
</tr>
<tr>
<td></td>
<td>companies.</td>
<td>2.B.2. Tracking system in place by 5/1/88.</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Enhance services to other divisions and other companies. (20%)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>GOAL</td>
<td>STRATEGY</td>
<td>METHOD OF MEASUREMENT</td>
</tr>
<tr>
<td>------</td>
<td>----------</td>
<td>-----------------------</td>
</tr>
</tbody>
</table>
| 3. Increase variety of media available through Information Resources to more adequately meet employee information needs and appropriate to modern technologies and lifestyles. (20%) | 3.A. Select, acquire, organize and promote a core collection of audio cassettes on topics relevant to current company interests. Provide equipment and expertise to support the service. | 3.A.1. Plan of approach submitted and approved by 7/31/88.  
| 3.B. Identify sources and develop and promote clearinghouse service for borrowing and renting videotapes and films. | | 3.B.1. Service in place by 10/31/88 |
| 3.C. Analyze A-V equipment needs  Prepare 3 year plan to update necessary support equipment. | 3.C.1. Plan developed by 4/30/88  
3.C.2. Implement consistent with plan as part of budget process. | |
| 3.D. Develop a plan of approach to improve services which support rapidly increasing information needs of employees using PC systems. | 3.D.1. Approach determined and approved by 11/30/88, and implemented as scheduled. | |
## Information Resources

### 1988 Goals

<table>
<thead>
<tr>
<th><strong>Goal</strong></th>
<th><strong>Strategy</strong></th>
<th><strong>Method of Measurement</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Improve access to and delivery of information without increasing storage space or staff requirements. (20%)</td>
<td>4.A. Evaluate at least 3 new online retrieval systems for their applicability to company needs.</td>
<td>4.A.1. Recommendations by 5/31/88 for 1989 budget planning.</td>
</tr>
<tr>
<td></td>
<td>4.B. Evaluate usefulness of software systems which facilitate downloading and editing online data, and of &quot;gateway&quot; systems which facilitate use of current online systems. Recommend appropriate systems and develop schedule for phased implementation or future evaluation.</td>
<td>4.B.1. Recommendations by 8/31/88. Implemented consistent with established milestones.</td>
</tr>
<tr>
<td>5. Establish a planned approach to acquisition of new information resources to provide adequate support for current and future company projects. (15%)</td>
<td>5.A. Develop criteria for analyzing and prioritizing potential resources to be purchased for print and A-V collections.</td>
<td>5.A.1. Criteria developed by 9/30/88 and implemented as recommended.</td>
</tr>
<tr>
<td>GOAL</td>
<td>STRATEGY</td>
<td>METHOD OF MEASUREMENT</td>
</tr>
<tr>
<td>------</td>
<td>----------</td>
<td>-----------------------</td>
</tr>
<tr>
<td>5.</td>
<td>Continued.</td>
<td>5.0. Identify data requirements to adequately analyze collection usage and areas needing development. Establish milestones to design and implement the system.</td>
</tr>
</tbody>
</table>
Incentive Goals for Corporate Attorney
Fiscal 1988

Company wide return on equity target 20% weight

Legal Collections: 30% weight
25% earned if 60% collected
50% earned if 75% collected
100% earned if 80% collected with interpolation of actual final #

Regulatory: 40% weight
10% achieve new classifications as proposed
10% accomplishment recovery of balancing account dollars
10% obtain increased revenues in final order over interim level - 1/2 achieved if additional revenues exceed $25,000, 100% earned if additional revenues exceed $50,000
10% achieve reduction in City Gate of 6%, 9%, 12% to acquire 50%, 75% and 100% of this 10%

Corporate: 10% weight
3% perform analysis of total expenditures for legal services by all company departments and propose plan to reduce those expenditures by 20% annually
3% keep expenditures for Legal Department 10% below budget
4% assist in load building by either providing marketing department with five leads or two additional appliance conversions; and by accomplishing regulatory approval for outdoor gas lighting

Signature - Supervisor  Signature - Participant

Date
ASSISTANT VICE PRESIDENT AND OPERATING SUPERINTENDENT

FISCAL - 1988 MANAGER BONUS GOALS

GOALS TO BE COMPLETED BY DUE DATES LISTED OR BY JUNE 30, 1988 TO QUALIFY 80% AVAILABLE BONUS UNDER THE MANAGEMENT BONUS PROGRAM.

25% 1. Implementation of Random Sampling Meter Program to replace present 10 year Periodic Test Program.

25% if implemented by November 1, 1987
15% if implemented by January 1, 1988
10% if implemented by March 31, 1988

20% 2. Reduce Distribution Department Operations and Maintenance expenses through productivity improvements and manpower planning.

100% - 5% decrease in expenses from Fiscal 1988 budget level
50% - 3% decrease in expenses from Fiscal 1988 budget level
25% - 1% decrease in expenses from Fiscal 1988 budget level
10% - .5% decrease in expenses from Fiscal 1988 budget level

15% 3. Reduce fleet gasoline usage by increased C.N.G. usage

15% if a 50% reduction in gallons of gasoline is realized
10% if a 30% reduction in gallons of gasoline is realized
5% if 10% reduction in gallons of gasoline is realized

5% 5. Develop good working relationship and open communications with Distribution Foreman

a. Inform foreman of Company's and superintendents expectations before August 1, 1987
b. Have distribution foreman meet with superintendent each Friday afternoon at 4:15 with tentative work schedule for following week.
c. Foreman to spend at least 1 hour per day in the office planning the following days work schedule, complete paper work, stores issue sheets, arrange utility locations, and answer requests of Fran or Marylou.
d. Foreman to plan main renewal projects on week in advance of scheduling work. Hold a 15 min pre-con meeting Friday morning with construction personnel to discuss project and receive input.
e. Work with superintendent to improve planning abilities. Superintendent to submit quarterly report to president on general foreman's progress in getting work distributed by 4:30 previous day and general overview of 4:15 planning improvements.

5% 6. Increase sales by marketing leads.

100% if 40 leads convert to new gas appliance sales
50% if 25 leads convert to new gas appliance sales
35% if 15 leads convert to new gas appliance sales

5% 7. Rewrite performance standards of subordinates to be results oriented.

5% if 100% are rewritten
3% if 75% are rewritten
2% if 50% are rewritten
I. FURTHER IMPROVE CUSTOMER SERVICE

Customer service superiority will be improved when we recognize that customer relations mirror employee relations. To this extent, Human Resources will focus its attention on management and front-line supervisors to provide training in supportive skills which should build abilities of effective management.

A. Each manager and supervisor will be trained on how to conduct more effective performance appraisals by the end of F1988.

35% Measurable Specific Objective: Halo effect of performance evaluations to be held at F1987 levels (4.01) or below:

* 100% earned if average ratings are below 3.86
* 95% earned if average ratings are 3.87 - 3.89
* 90% earned if average ratings are 3.90 - 3.92
* 85% earned if average ratings are 3.93 - 3.95
* 80% earned if average ratings are 3.96 - 3.98
* 75% earned if average ratings are 3.99 - 4.01

B. A more effective performance appraisal system for the Service Center union personnel will be developed. Job standards will be geared more to measurable objectives. This will be completed by June 1, 1988.

5% Measurable Specific Objective: Twenty positions completed;

* 5% earned if 15 - 20 positions are completed
* 3% earned if 10 - 15 positions are completed
* 2% earned if 5 - 10 positions are completed
* 0% earned if less than 5 positions are completed

C. An on-going training program coordinated to include managers in the training process will continue for first level supervisors to develop skills in:

- Communications - October, 1987
- Delegation - December, 1987
- Reward-Discipline - January, 1988
- Time Management - March, 1988
- Other areas as needed.
10% Measurable Specific Objective: After productivity training, managers should be able to cut payroll budgets by 10%. The Human Resource Department will lead by example.

*10% earned if payroll budget is cut more than $1644
* 9% earned if payroll budget is cut $1534-$1643
* 8% earned if payroll budget is cut $1423-$1533
* 7% earned if payroll budget is cut $1312-$1422
* 6% earned if payroll budget is cut $1201-$1311
* 5% earned if payroll budget is cut under $1200

D. Provide input from employee developmental plans to design overall training programs, in cooperation with the Training Task Force. To be completed by September, 1987.

11. PROVIDE MORE CHALLENGING AND REWARDING WORK FOR EACH EMPLOYEE.

Job enrichment and challenging employees' creativity will be enhanced as position descriptions more closely resemble actual duties. These duties must carry realistic job standards to measure productivity.

A. Job standards for each non-union, non-exempt employee will be developed to reflect at least three new measurements for each position. Managers, supervisors, and employees will be involved in the process to reflect effective and measurable criteria in order to make intelligent evaluations. At the same time, job descriptions will be reviewed to recommend changes in major responsibilities. Standards are to be upgraded by June 30, 1988.

15% Measurable Specific Objective:

*15% earned if 116 - 125 new measurements
*14% earned if 106 - 115 new measurements
*13% earned if 96 - 105 new measurements
*12% earned if 86 - 95 new measurements
*11% earned if 76 - 85 new measurements
* 0% earned if less than 75 new measurements

B. Reduce employee absenteeism by 20% from 1987 records. This is recorded absence for illness or doctor hours five days of less in duration.

5% Measurable Specific Objective:

*5% earned if absenteeism is reduced by 20%
C. The 1988 Wage and Salary Program will be announced to the employees by June 24, 1987. This includes an explanation of the salary survey conducted, the six point evaluation criteria, and the pay-for-performance grid. Emphasis will be stressed that merit is the key to raises. An on-going individual plant will continue to show employees exactly where they placed in the survey, and also the potential for raises under the new grid. A guideline for managers on how to justify exceptional and outstanding performers will be issued by July 31, 1987. A monitoring system for the salary program to continuously record the following will be developed:

<table>
<thead>
<tr>
<th>DATE</th>
<th>DEPT</th>
<th>EMPLOYEE</th>
<th>WAGE</th>
<th>INCREASE</th>
<th>INCREASE</th>
<th>RATINGS</th>
</tr>
</thead>
</table>

Total:

This system will allow senior management to monitor wage increases quarterly. Completion date is September 30, 1987.

III. SELL MORE GAS

In concert with the Marketing Department, develop and implement an Employee Incentive Plan to encourage maximum participation.

A. Submit leads for new (or converted) gas appliances which result in ten such actual appliance sales.

10% Measurable Specific Objective:

*100% earned if ten appliances are sold.

Both employee and supervisor have agreed to the above objectives on this 10th day of August, 1987.
75% of the incentive bonus will be based on specific objectives. 25% of the incentive plan will be based upon the company's overall performance (R.O.E.)

1. 10% of bonus will be achieved when a typed detailed construction report for main renewals is prioritized and time table with estimated starting dates has been submitted on or before April 1, 1988.

40% 2. Reduction of temporary laborer payroll costs. By scheduling temporary employee hiring to coincide with peak work load periods.

<table>
<thead>
<tr>
<th>REDUCTION</th>
<th>Raw salary's costs</th>
</tr>
</thead>
<tbody>
<tr>
<td>100%</td>
<td>30% $15,000</td>
</tr>
<tr>
<td>50%</td>
<td>20% 10,500</td>
</tr>
<tr>
<td>25%</td>
<td>10% 5,500</td>
</tr>
<tr>
<td>10%</td>
<td>5% 2,700</td>
</tr>
</tbody>
</table>

15% 3. Reduce regular payroll costs by improved productivity and planning.

50% This goal will be satisfied when the next days scheduled work is distributed to the crews prior to 4:30 p.m.

50% Also provide fill in work log for personnel when assigned jobs have been completed ahead of scheduled or have been cancelled, and you are not available. Copy of log submitted to superintendent monthly indicating fill jobs, completion dates, and signatures.

15% 4. Reduce overall service line installation costs by reducing the average payroll unit cost per service as calculated from the Year to Date Data Processing Payroll Account Report.
REDUCTION OF AVERAGE PAYROLL UNIT COSTS

5%  $2.00
10%  5.00
15%  10.00

10% 5. Reduce 380 account installation average unit costs per service stub.

REDUCTION OF AVERAGE PAYROLL UNIT COST

5%  1.00
10%  3.00

10% 6. Increased sales by marketing leads.

100% if 6 leads convert to new gas appliance sales.

50% if 3 leads convert to new gas appliance sales.

35% if 2 leads convert to new gas appliance sales.

Approved
Disapproved

Approved
Disapproved

EMPLOYEE
SUMMARY TABLES OF
AGA EXECUTIVE SALARY SURVEY RESULTS 1987

SUMMARY TABLES FOR INCENTIVE PAY PLANS

All Member Respondents

Smaller Company Survey
August 1, 1987

Dear Participant,

The 1987 American Gas Association Compensation Surveys reflect a number of significant changes from prior surveys. The Compensation & Benefits Committee, the staff of A.G.A. and the consultants of Mercer-Heidinger-Hansen have combined their efforts to improve the comprehensiveness, quality and timeliness of the surveys. We trust that you will find the results more useful and reliable.

The survey this year contains four sections. Those in which you have participated are included, or will be forwarded to you shortly. The sections and the number of firms participating in each are:

- Corporate Board of Directors: 37
- Executive: 95
- Managerial, Supervisory and Professional: 99
- Administrative Policies: 100

All of the data is effective as of March 1, 1987. The introduction to each section clarifies the way that the data is presented. Please take the time to read these clarifications.

The formats have been developed to maximize the relevance of the analysis and protect the confidentiality of the participant data. Where data may have allowed individual company information to be identified, the data has not been shown. We also want to remind you that every participant has signed an agreement to treat the results of this survey confidentially.

A data listing of your firm's position matches to the survey positions is enclosed for your reference. If some of your initial position responses were not included in the survey, it means that the Mercer Consultants did not believe that the data submitted met their comfort level for degree of match. This should not necessarily preclude you from deciding the match is appropriate for your purposes.

While we believe major improvements have been made in this year's survey, the need for numerous other format improvements has become evident as we implemented our plans. Your support in the form of comments and recommendations is necessary to make next year's survey even better.
In the near future you will receive a questionnaire asking for your assessment of this year’s survey and what is needed for next year. We are also planning a meeting in Orlando, Florida on October 15th to develop plans for next year’s survey. You are invited to attend.

If you have any questions on the survey process please contact Pat Curley at A.C.A. (703/341-9497). Questions on specific position information should be directed to Hoyt Doyel or Barbara Markovetz at Mercee-Meidinger-Manssen (303/831-7100).

We appreciate your participation in the group surveys and look forward to serving you in the future.

Sincerely,

Michael I. German

Enclosures
Copyright, 1987
by the American Gas Association
### Table II

**INCENTIVE PLAN ANALYSIS**

**All Firms**

<table>
<thead>
<tr>
<th>Position</th>
<th>Title</th>
<th>% Eligible</th>
<th>Target %</th>
<th>Maximum %</th>
</tr>
</thead>
<tbody>
<tr>
<td>901</td>
<td>Chief Executive Officer</td>
<td>39%</td>
<td>29%</td>
<td>47%</td>
</tr>
<tr>
<td>902</td>
<td>Chief Operating Officer</td>
<td>49%</td>
<td>22%</td>
<td>32%</td>
</tr>
<tr>
<td>903</td>
<td>Executive Vice President</td>
<td>42%</td>
<td>21%</td>
<td>25%</td>
</tr>
<tr>
<td>960</td>
<td>Top Exploration and Production Executive</td>
<td>46%</td>
<td>22%</td>
<td>45%</td>
</tr>
<tr>
<td>928</td>
<td>Top Legal Executive</td>
<td>46%</td>
<td>20%</td>
<td>33%</td>
</tr>
<tr>
<td>912</td>
<td>Top Financial Executive</td>
<td>42%</td>
<td>20%</td>
<td>32%</td>
</tr>
<tr>
<td>910</td>
<td>Top Administrative Executive</td>
<td>43%</td>
<td>15%</td>
<td>25%</td>
</tr>
<tr>
<td>950</td>
<td>Top Operations Executive</td>
<td>39%</td>
<td>19%</td>
<td>29%</td>
</tr>
<tr>
<td>956</td>
<td>Top Gas Supply Executive</td>
<td>43%</td>
<td>17%</td>
<td>30%</td>
</tr>
<tr>
<td>914</td>
<td>Controller</td>
<td>37%</td>
<td>19%</td>
<td>37%</td>
</tr>
<tr>
<td>926</td>
<td>Top Human Resources Executive</td>
<td>38%</td>
<td>16%</td>
<td>29%</td>
</tr>
<tr>
<td>916</td>
<td>Treasurer</td>
<td>36%</td>
<td>16%</td>
<td>28%</td>
</tr>
<tr>
<td>940</td>
<td>Top Marketing Executive</td>
<td>39%</td>
<td>17%</td>
<td>31%</td>
</tr>
<tr>
<td>934</td>
<td>Top Rate Executive</td>
<td>43%</td>
<td>14%</td>
<td>27%</td>
</tr>
<tr>
<td>938</td>
<td>Top Governmental Affairs Executive</td>
<td>38%</td>
<td>19%</td>
<td>35%</td>
</tr>
<tr>
<td>930</td>
<td>Secretary - Legal</td>
<td>60%</td>
<td>14%</td>
<td>23%</td>
</tr>
<tr>
<td>952</td>
<td>Division Operations Executive</td>
<td>46%</td>
<td>18%</td>
<td>29%</td>
</tr>
<tr>
<td>954</td>
<td>Top Engineering Executive</td>
<td>33%</td>
<td>17%</td>
<td>26%</td>
</tr>
<tr>
<td>936</td>
<td>Top Public Relations Executive</td>
<td>29%</td>
<td>15%</td>
<td>27%</td>
</tr>
<tr>
<td>922</td>
<td>Top D.P./M.I.S. Executive</td>
<td>24%</td>
<td>16%</td>
<td>26%</td>
</tr>
<tr>
<td>932</td>
<td>Secretary - Non-Legal</td>
<td>34%</td>
<td>18%</td>
<td>31%</td>
</tr>
<tr>
<td>918</td>
<td>Top Tax Executive</td>
<td>31%</td>
<td>15%</td>
<td>27%</td>
</tr>
<tr>
<td>924</td>
<td>Top Purchasing Executive</td>
<td>14%</td>
<td>18%</td>
<td>29%</td>
</tr>
<tr>
<td>920</td>
<td>Top Internal Auditor</td>
<td>22%</td>
<td>14%</td>
<td>25%</td>
</tr>
</tbody>
</table>

**Corporate**

<table>
<thead>
<tr>
<th>% Eligible</th>
<th>Avg Target %</th>
<th>Avg Maximum %</th>
</tr>
</thead>
<tbody>
<tr>
<td>39%</td>
<td>29%</td>
<td>47%</td>
</tr>
<tr>
<td>49%</td>
<td>22%</td>
<td>32%</td>
</tr>
<tr>
<td>42%</td>
<td>20%</td>
<td>32%</td>
</tr>
<tr>
<td>43%</td>
<td>15%</td>
<td>25%</td>
</tr>
<tr>
<td>39%</td>
<td>19%</td>
<td>29%</td>
</tr>
<tr>
<td>43%</td>
<td>17%</td>
<td>28%</td>
</tr>
<tr>
<td>39%</td>
<td>17%</td>
<td>31%</td>
</tr>
<tr>
<td>43%</td>
<td>14%</td>
<td>27%</td>
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<tr>
<td>38%</td>
<td>19%</td>
<td>35%</td>
</tr>
<tr>
<td>37%</td>
<td>19%</td>
<td>37%</td>
</tr>
<tr>
<td>38%</td>
<td>16%</td>
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**Subsidiaries**

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NS = Insufficient data for analysis
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<th>Subsidiary</th>
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<tr>
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<tr>
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</tr>
<tr>
<td>921</td>
<td>Top Legal Exec.</td>
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</tr>
<tr>
<td>922</td>
<td>Top Fin. Exec.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>923</td>
<td>Top Adm. Exec.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>924</td>
<td>Top Opr. Exec.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>925</td>
<td>Top Gas Supply Exec.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>926</td>
<td>Controller</td>
<td></td>
<td></td>
</tr>
<tr>
<td>927</td>
<td>Top H. R. Exec.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>928</td>
<td>Treasurer</td>
<td></td>
<td></td>
</tr>
<tr>
<td>930</td>
<td>Top Mktg Exec.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>931</td>
<td>Top Rate Exec.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>932</td>
<td>Top Gov. Affairs Exec.</td>
<td></td>
<td></td>
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<tr>
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<td>Secr. - Legal</td>
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<tr>
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<td>Top F. R. Exec.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>937</td>
<td>Top D.P./M.I.S. Exec.</td>
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</tr>
<tr>
<td>938</td>
<td>Secr. - Non-Legal</td>
<td></td>
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</tr>
<tr>
<td>939</td>
<td>Top Tax Exec.</td>
<td></td>
<td></td>
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<tr>
<td>940</td>
<td>Top Purch. Exec.</td>
<td></td>
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</tr>
<tr>
<td>941</td>
<td>Top Internal Aud.</td>
<td></td>
<td></td>
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</table>

ISO = Incentive Stock Options
NQ = Non-Qualified
RS = Restricted Stock
SAR = Stock Appreciation Rights
Dear Participant:

Subject: Smaller Company Compensation Survey

The Compensation & Benefits Committee and the staff of A.G.A. have worked together to produce a special edition of our compensation for smaller companies survey. This special edition is tailored for companies whose gross annual revenues are in the 0-500 million size range. We trust that you will find the results useful and reliable.

The special edition contains three sections. Those in which you have participated are included, or will be forwarded to you shortly. The sections and the number of firms participating in each are:

- Executive: 69
- Managerial, Supervisory and Professional: 66
- Administrative Policies: 71

All of the data is effective as of March 1, 1987. The introduction to each section clarifies the way that the data is presented.

The formats have been developed to maximize the relevance of the analysis and protect the confidentiality of the participant data. Where data may have allowed individual company information to be identified, the data has not been shown. We also want to remind you that every participant has signed an agreement to treat the results of this survey confidentially.

A data listing of your firm's position matches to the survey positions is enclosed for your reference. If some of your initial position responses were not included in the survey, it means that the Mercer Consultants did not believe that the data submitted met their comfort level for degree of match. This should not necessarily preclude you from deciding the match is appropriate for your purposes.
January 20, 1988
Page Two

If you have any questions on the survey process please contact Pat Curley at A G A (703/841-8497). We appreciate your participation in the group surveys and look forward to serving you in the future.

Sincerely,

Michael I. German

jbt:pjc

enclosures
Table B
INCENTIVE PLAN ANALYSIS
All Firms

<table>
<thead>
<tr>
<th>Position</th>
<th>Title</th>
<th>Eligible</th>
<th>Avg Target %</th>
<th>Avg Maximum %</th>
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</thead>
<tbody>
<tr>
<td>901</td>
<td>Chief Executive Officer</td>
<td>38%</td>
<td>15%</td>
<td>26%</td>
</tr>
<tr>
<td>902</td>
<td>Chief Operating Officer</td>
<td>46%</td>
<td>9%</td>
<td>23%</td>
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<tr>
<td>910</td>
<td>Top Administrative Executive</td>
<td>43%</td>
<td>9%</td>
<td>20%</td>
</tr>
<tr>
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<td>Top Legal Executive</td>
<td>40%</td>
<td>14%</td>
<td>27%</td>
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<tr>
<td>912</td>
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</tr>
<tr>
<td>903</td>
<td>Executive Vice President</td>
<td>33%</td>
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<td>20%</td>
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<tr>
<td>960</td>
<td>Top Exploration and Production Executive</td>
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<td>13%</td>
<td>25%</td>
</tr>
<tr>
<td>956</td>
<td>Top Gas Supply Executive</td>
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<td>11%</td>
<td>25%</td>
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<tr>
<td>950</td>
<td>Top Operations Executive</td>
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<td>11%</td>
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<tr>
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<tr>
<td>920</td>
<td>Top Internal Auditor</td>
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NIP = For this position no companies have incentive programs.
## Table C

**INCENTIVE PLAN CHARACTERISTICS**  
**PERCENT OF EMPLOYEES ELIGIBLE FOR PROGRAMS**

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BIBLIOGRAPHY


Butler, Stephen; Maher, Michael, Management Incentive Compensation Plans, Management Accounting, September 1986, pg 20.


Hills, Frederick S.; Madigan, Robert M.; Scott, K. Dow; Markham, Steven E.; Tracking the Merit of Merit Pay, Personnel Administrator, March 1987, pg. 50.


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