

COMMONWEALTH OF KENTUCKY  
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

ELECTRONIC APPLICATION OF KENTUCKY-	)	
AMERICAN WATER COMPANY TO AMEND	)	CASE NO.
TARIFF FOR THE ESTABLISHMENT OF	)	2020-00027
QUALIFIED INFRASTRUCTURE PROGRAM	)	
CHARGE	)	

ORDER

On March 2, 2020, Kentucky-American Water Company (Kentucky-American) filed its initial Qualified Infrastructure Program (QIP) Rider seeking authority to implement a surcharge for recovery of certain capital expenses to replace a portion of its aging water system infrastructure. Kentucky-American requested a 1.62 percent QIP surcharge with an effective date of July 1, 2020.

There are no intervenors in this proceeding. Kentucky-American responded to four rounds of discovery and a formal hearing was held on May 12, 2020. Kentucky-American filed a post-hearing brief. This matter now stands submitted to the Commission for a decision.

BACKGROUND

In Case No. 2018-00358, Kentucky-American requested approval of a QIP Rider to make incremental capital improvements to replace its aging water distribution and treatment infrastructure, with a particular focus on aging mains.<sup>1</sup> In that proceeding,

---

<sup>1</sup> Case No. 2018-00358, Electronic Application of Kentucky-American Water Company for an Adjustment of Rates (Ky. PSC June 27, 2019), Order at 73-74.

Kentucky-American stated that it would prioritize the replacement of cast iron and galvanized steel mains, which represent 15 percent of the distribution system but accounted for 64.2 percent of annual main breaks.<sup>2</sup> In approving the QIP Rider, the Commission established a filing schedule, calculation methodology, and filing contents.

QIP applications are filed on an annual basis on or before April 2, have a 90-day review period that can be extended for good cause, are based on a forecasted test period of July 1 to June 30, and have an annual true-up filing of projected costs and actual costs. The QIP Rider is based upon a revenue requirement that is the sum of the pre-tax return for qualified additions and removal expenditures, plus the depreciation and property tax for the proposed projects in the forecasted test year. The QIP surcharge percentage is calculated as the amount of the QIP revenue requirement divided by the \$98,880,622 authorized revenue requirement established in Case No. 2018-00358.<sup>3</sup> The QIP Rider is applied as a percentage to all water revenue, excluding other surcharges or taxes, and is displayed as a separate line item on customer bills. The QIP Rider is reset to zero when the next base rates are approved because the next base rates will include recovery of the annual costs previously recovered through the QIP.

### PROPOSED QIP

#### QIP Rider Surcharge Amount

In its application, Kentucky-American requested a 1.62 percent QIP Rider, which would result in an increase of \$0.60 per month for average residential customers.<sup>4</sup>

---

<sup>2</sup> *Id.* at 76.

<sup>3</sup> Direct Testimony of Elaine K. Chambers (Chambers Testimony) at 6:11-14 and Exhibit 1.

<sup>4</sup> Chambers Testimony at 6:2-3.

Kentucky-American proposed a net change to rate base due to the QIP-related plant additions totaling \$12,767,190, and a QIP revenue requirement of \$1,603,757. Kentucky-American used a composite retirement rate of 7.24 percent for calculating the retirement expense associated with QIP-related plant additions during the forecasted year.<sup>5</sup> Kentucky-American asserted that the composite retirement rate produced a more reasonable result than using the individual rates for the QIP plant accounts, pointing out that the estimated retirement expenses will be trued up during the annual balancing mechanism.<sup>6</sup> Similarly, Kentucky-American used a composite depreciation rate to calculate depreciation expense for QIP-related plant during the forecasted year. Kentucky-American asserted that the difference between using a composite rate rather than individual plant account rate was immaterial, and that the depreciation expense would be trued up during the annual balancing mechanism.<sup>7</sup>

#### QIP Projects

Kentucky-American explained it identified replacement projects to include in the proposed QIP through engineering criteria developed from regulations, professional standards, and Kentucky-American engineering policies and procedures. The criteria includes the amount of water pressure, number of breaks or leaks, age, material type, size, water quality, and customer impact.<sup>8</sup> Kentucky-American further explained that, in

---

<sup>5</sup> *Id.* at 5:3-5.

<sup>6</sup> Kentucky-American Response to Commission Staff's First Request for Information (Response to Staff's First Request), Item 11.b; May 12, 2020 Hearing Video Transcript (HVT) at 10:35.

<sup>7</sup> Response to Staff's First Request, Item 13.a.; HVT at 10:37.

<sup>8</sup> Kentucky-American's Response to Commission Staff's Second Post-Hearing Request for Information (Response to Staff's Second Post-Hearing Request), Item 2(b) and Response 2B attachment.

rating and ranking mains to be replaced, the overall weighted score and rankings can change over time due to changed circumstances.<sup>9</sup>

Kentucky-American included nine budget line items deemed “recurring projects” and one budget line item deemed an “investment project” in the proposed QIP that will be constructed with internal labor or with identified contractors.<sup>10</sup> Recurring projects are smaller distribution system and treatment facility projects that address adequate capacity and service reliability.<sup>11</sup> Investment projects are larger projects that, per individual project, cost more than \$250,000 and that address regulatory compliance, infrastructure capacity expansion or rehabilitation, or ensure a safe working environment.<sup>12</sup> Although Kentucky-American identified the projects as budget lines, the projects are accounted for by discrete plant account numbers rather than by discrete projects.<sup>13</sup>

Kentucky-American explained that the projects were not developed for this QIP specifically, but instead were projects previously identified as part of Kentucky-American’s larger plan to accelerate spending on replacing aging infrastructure.<sup>14</sup> Kentucky-American stated that the QIP projects are not part of the capital investment plan projects that were included in base rates in the most recent rate case.<sup>15</sup>

---

<sup>9</sup> *Id.*

<sup>10</sup> Application at 7.

<sup>11</sup> Direct Testimony of Kurt A. Stafford (Stafford Testimony) at 4:5-14.

<sup>12</sup> *Id.* at 5:3-9.

<sup>13</sup> HVT at 9:09; Response to Staff’s First Request, Item 13, Attachment Excel No. 13, Tab “Placed in Service.”

<sup>14</sup> HVT at 9:29.

<sup>15</sup> HAVT 9:38; Response to Staff’s Second Post-Hearing Request, Item 1.

The nonrevenue plant replacement projects included in the proposed QIP Rider are as follows:

- Recurring Project Line B: QIP Mains Replaced/Restored. This project includes the scheduled replacement or improvement of 32,160 feet of existing water mains, including valves and other appurtenances necessary to perform the work that reached the end of their useful life or cause service problems to adjacent area serviced by the main.<sup>16</sup> Kentucky-American budgeted \$7,400,000 for four projects in the Versailles Road, State Street, Winchester Road, and Castlewood areas.<sup>17</sup> Kentucky-American stated that it developed the main replacement budget by reviewing historical spending on main replacement while also projecting an increase in spending between \$4,000,000 and \$6,900,000 annually over the next 25 years to accelerate main replacement.<sup>18</sup>

Kentucky-American testified that it maintains a pipe replacement model that helps to guide replacement projects.<sup>19</sup> Kentucky-American stated that the majority of replaced main in this budget line is cast iron and galvanized main that represent 15.9 percent of the total inventory of main that represent 60 percent of all breaks.<sup>20</sup> Kentucky-American explained that the break per mile for cast iron main is 1.1 breaks per mile of main compared to ductile iron, which has a break rate of 0.04 breaks per mile of main between

---

<sup>16</sup> Stafford Testimony at 7:21-8:1, 8:8.

<sup>17</sup> *Id.* at 8:7-9, 8:20-9:28.

<sup>18</sup> Kentucky-American Response to Commission Staff's Second Request for Information (Response to Staff's Second Request, Item 2, Attachment PSC 2-2 Excel.

<sup>19</sup> Response to Staff's Second Request, Item 2, Attachment PSC 2-2 Excel; HVT at 9:41.

<sup>20</sup> Stafford Testimony at 9:31-35.

January 2012 and December 2016.<sup>21</sup> Kentucky-American asserted that replacing aging water main infrastructure on a proactive, accelerated basis would result in a direct customer benefit of improved and sustained water quality, reducing water leaks and water main breaks, improved fire protection, fewer service disruptions, and lower operating and maintenance costs.<sup>22</sup>

- Recurring Project Line C: Mains Unscheduled. This project includes the unscheduled replacement or restoration of existing water mains, including valves and other appurtenances necessary to perform the work, with unexpected break or failure that requires replacement of a section of main that extends the service life of the main instead of repairing failure with a temporary clamp and replacing the main in the future.<sup>23</sup> Kentucky-American forecasted budget is \$900,000, based upon historic averages expended for unscheduled main replacement.<sup>24</sup> Kentucky-American maintained that the forecasted amount is consistent with 2019 total of \$900,000, but slightly higher than previous 2-year average spend of \$860,000 due to modifications to local paving and restoration ordinances that have increased the cost of repairs.<sup>25</sup> Kentucky-American asserted that including unscheduled main replacement in the QIP projects would provide a customer benefit because the replaced main would be more stable, which would permit

---

<sup>21</sup> *Id.* at 10:1-3.

<sup>22</sup> *Id.* at 8:3-6.

<sup>23</sup> *Id.* at 10:11-23.

<sup>24</sup> Stafford Testimony at 11:1-2; Response to Staff's First Request, Item 4; Response to Staff's Second Request, Item 2, Attachment PSC 2-2 Excel.

<sup>25</sup> Response to Staff's First Request, Item 4.

Kentucky-American to concentrate on replacement of mains with a larger history of breaks.<sup>26</sup>

- Recurring Project Line D: Mains Relocated. This project includes the relocation and replacement of existing water mains in the public right-of-way due to municipal or state agency improvement projects that conflict with Kentucky-American infrastructure.<sup>27</sup> Kentucky-American budgeted \$500,000 for this budget line based upon historical averages.<sup>28</sup> Kentucky-American identified four potential relocation projects in Fayette County, Kentucky: road-widening projects on Mount Tabor Road and Clays Mill Road, a road project along U.S. 460, and a sanitary sewer project at the University of Kentucky. Kentucky-American claimed that it was responsible for the cost to remove or relocate its mains from the public right of way under Lexington-Fayette Urban County Government (LFUCG) Ordinance 17C-19(e)(4), KRS 179.265, KRS 177.035, and 23 CFR 645.111 Subpart A.<sup>29</sup> Kentucky-American maintained that customers would benefit from this QIP project with greater system reliability due to the installation of newer main that is stronger than the main that would be removed.<sup>30</sup>

- Recurring Project Line F: Hydrants, Valves, and Manholes Replaced. This project includes the replacement of leaking, failed, or obsolete hydrants and valves owned

---

<sup>26</sup> Stafford Testimony at 11:1-4.

<sup>27</sup> *Id.* at 11:6-10.

<sup>28</sup> *Id.* at 11:6; Response to Staff's Second Request, Item 2, Attachment PSC 2-2 Excel.

<sup>29</sup> Stafford Testimony at 11:16-18; Response to Staff's First Request, Item 1; HVT at 9:17.

<sup>30</sup> Stafford Testimony at 11:10-14.

by Kentucky-American.<sup>31</sup> Based on inspections that identified hydrants that warranted replacement, Kentucky-American budgeted \$500,000 for this project, representing \$315,000 to replace 70 valves and \$175,000 to replace 32 hydrants.<sup>32</sup> Kentucky-American developed the forecasted budget based upon historical averages, explaining that the forecasted amount is comparable to the 2019 planned spend of \$492,960 and slightly higher than the 2-year average of \$481,580 because Kentucky-American has increased its focus on this type of work as part of its plan to accelerate aging water infrastructure.<sup>33</sup> Kentucky-American contended that customers will benefit from the replacement of hydrants and valves because, by replacing hydrants not functioning properly, Kentucky-American can ensure adequate and reliable service and maintain public safety through functioning hydrants.

- Recurring Project Line H: Services and Laterals Replaced. This project includes the replacement of up to 118 service lines and laterals that connect Kentucky-American's customers to Kentucky-American's distribution main.<sup>34</sup> Kentucky-American budgeted \$530,000 to replace services and laterals that cause reduction in water service or issues with water quality.<sup>35</sup> Kentucky-American developed the forecasted budget based on historical averages, noting that the forecasted amount is comparable to the

---

<sup>31</sup> *Id.* at 12:4-5.

<sup>32</sup> *Id.* at 12:5-8, 9-14; Response to Staff's Second Request, Item 2, Attachment PSC 2-2 Excel; Response to Staff's Second Request, Item 2, Attachment PSC 2-2 Excel.

<sup>33</sup> Response to Staff's First Request, Item 5.

<sup>34</sup> Stafford Testimony at 12:16-20, 13:1-3.

<sup>35</sup> *Id.* at 12:20-22.



2019 planned spend of \$532,500 and the average 5-year spend of \$505,800.<sup>36</sup> Kentucky-American maintained that customers would benefit because replacing aging infrastructure that reduces water service or impacts water quality will result in safe, adequate, and reliable water service.<sup>37</sup>

- Recurring Project Line J: Meters Replaced. This project includes the replacement or improvement of up to 6,332 meters and meter settings identified by Kentucky-American for replacement because the meters are nearing the end of their useful service life.<sup>38</sup> Kentucky-American budgeted \$1,200,000 based upon an average cost of \$189.20 per meter.<sup>39</sup> Kentucky-American based its forecasted cost on the unit cost of the meters and historical data on the number of meters that need to be replaced over 12 months.<sup>40</sup> Kentucky-American noted that all of its meters are automatic meter reading (AMR) meters, explaining that replacement meters will be AMR meters that are compatible with newer technology and potentially upgradeable at a later date.<sup>41</sup> Kentucky-American asserted that replacing meters at the end of their service life will

---

<sup>36</sup> Response to Staff's First Request, Item 6; Response to Staff's Second Request, Item 2, Attachment PSC 2-2 Excel.

<sup>37</sup> Stafford Testimony at 12:20-22.

<sup>38</sup> *Id.* at 13:5-9; HVT at 9:17; Kentucky-American's Response to Commission Staff's First Post-Hearing Request for Information, Item 1.

<sup>39</sup> Stafford Testimony at 13:10-12.

<sup>40</sup> Response to Staff's First Request, Item 6; Response to Staff's Second Request, Item 2, Attachment PSC 2-2 Excel.

<sup>41</sup> Response to Staff's First Request, Item 7.

provide customers with safe, adequate, and reliable service by avoiding service disruptions from failed meters.<sup>42</sup>

- Recurring Project Line L: SCADA Equipment and Systems. This project includes the installation or replacement of existing supervisory control and data acquisition (SCADA) equipment and systems, the computerized system for monitoring and operating the treatment plants and network facilities.<sup>43</sup> Kentucky-American budgeted \$325,000 to replace critical communications infrastructure, based upon historical averages.<sup>44</sup> Kentucky-American asserted that the project is necessary to meet safety and environmental requirements.<sup>45</sup>

- Recurring Project Line M: Security Equipment and Systems. This project includes upgrades to existing security equipment and systems for water treatment infrastructure, including fencing, alarm systems, cameras, barricades, and locking systems.<sup>46</sup> Kentucky-American budgeted \$130,000 for this project, based upon historical averages.<sup>47</sup> Kentucky-American explained that historical spending on security equipment and systems fluctuates based on needed projects, with a five-year average spend of

---

<sup>42</sup> Stafford Testimony at 13:6-9.

<sup>43</sup> *Id.* at 13:14-18.

<sup>44</sup> *Id.* at 13:21-22; Response to Staff's First Request, Item 6; Response to Staff's Second Request, Item 2, Attachment PSC 2-2 Excel.

<sup>45</sup> Stafford Testimony at 13: 18-20.

<sup>46</sup> *Id.* at 14:4-8.

<sup>47</sup> *Id.* at 14:13-14; Response to Staff's First Request, Item 8; Response to Staff's Second Request, Item 2, Attachment PSC 2-2 Excel.

\$237,000.<sup>48</sup> Kentucky-American asserted that these projects would benefit customers by maintaining and improving the security of existing facilities and complying with Homeland Security directives.<sup>49</sup>

- Recurring Project Line Q: Process Plant Facilities and Equipment. This project includes the replacement of existing older components of water treatment and storage plant.<sup>50</sup> Kentucky-American explained that the replacements include both scheduled replacements and unscheduled replacements due to equipment failure.<sup>51</sup> Kentucky-American budgeted \$750,000 for these replacements based upon historical averages.<sup>52</sup> Kentucky-American noted that the five-year historical average is \$1,820,000, and thus higher than the forecasted budget, explaining that the historical spend total includes projects that are not eligible to be included in the QIP Rider.<sup>53</sup> Kentucky-American explained that customers would benefit because the work to be performed in Line Q would result in more efficient equipment that uses less electricity and because the projects are necessary to meet water quality regulations.

- Investment project: Cox Street Booster Station. This project includes the replacement of a booster station, consisting of several below ground vaults that require

---

<sup>48</sup> Response to Staff's First Request, Item 8; Response to Staff's Second Request, Item 2, Attachment PSC 2-2 Excel.

<sup>49</sup> Stafford Testimony at 14:8-12.

<sup>50</sup> *Id.* at 14:18-20.

<sup>51</sup> *Id.* at 14:20-21.

<sup>52</sup> *Id.* at 15:3-4; Response to Staff's First Request, Item 9; Response to Staff's Second Request, Item 2, Attachment PSC 2-2 Excel.

<sup>53</sup> Response to Staff's First Request, Item 9.

confined space entry.<sup>54</sup> The Cox Street Booster Station was included in Kentucky-American's capital investment plan in Case No. 2018-00358 with a completion date of December 2019.<sup>55</sup> However, the replacement of the Cox Street Booster Station was not included in base rates approved in Case No. 2018-00358 because the capital investment plan was revised to move the project to the fall of 2020 and, thus, outside the forecasted test year.<sup>56</sup> Kentucky-American clarified that this project became the highest priority for replacement, and thus was included in the QIP, due to its age, confined space requirement, and deteriorating vault structures that post a safety hazard to Kentucky-American employees.<sup>57</sup> Kentucky-American budgeted \$1,000,000 for the project based upon historical costs.<sup>58</sup>

#### Monitoring QIP Project Spending

Under the terms of the QIP Rider tariffs, Kentucky-American will file an annual reconciliation in September 2021 that will true up projected and actual costs of projects between July 1, 2020, and June 30, 2021.<sup>59</sup> The reconciliation filing includes a progress report for work completed, the amount of progress payment, and costs of removal of old pipes.

---

<sup>54</sup> Stafford Testimony at 15:13-15.

<sup>55</sup> Case No. 2018-00358, Direct Testimony of Brent E. O'Neill (O'Neill Testimony) at 17.

<sup>56</sup> Case No. 2018-00358, Kentucky-American's Response to Commission Staff's First Request for Information, Item 13.

<sup>57</sup> Stafford Testimony at 15:15-16.

<sup>58</sup> *Id.* at 15:13; Response to Staff's First Request, Item 9.

<sup>59</sup> QIP Rider Tariff Sheet No. 49.

Between July 1, 2020, and June 30, 2021, Kentucky-American will monitor QIP project expenses using the same methodology that it uses for monitoring its capital investment plan spending. Kentucky-American's QIP spending will be monitored by the Capital Investment Management Committee (CIMC) that consists of Kentucky-American executives who meet monthly to review actual capital expenditures on the QIP projects as compared to budgeted levels.<sup>60</sup> Kentucky-American asserted that it did not include contingency costs in the QIP project budgets.<sup>61</sup> Kentucky-American testified that, in the monthly reviews, the CIMC will address any QIP projects that vary from the budgeted amount by 10 percent or higher.<sup>62</sup> Kentucky-American demonstrated the controls in place to ensure that QIP project expenses would remain separate from capital investment plan project expenses.<sup>63</sup>

## DISCUSSION AND FINDINGS

### QIP-eligible Plant

In Case No. 2018-00358, the Commission approved Kentucky-American's QIP to replace Kentucky-American's aging infrastructure, particularly its aging distribution system with cast iron and galvanized steel mains, 29 percent of which was installed between 1885 and 1970.<sup>64</sup> According to Kentucky-American, without an accelerated

---

<sup>60</sup> Stafford Testimony at 6:12-18; HVT at 9:24.

<sup>61</sup> Response to Staff's Second Request, Item 1.

<sup>62</sup> HVT at 9:28.

<sup>63</sup> Chambers Testimony, Elaine Chambers Workpapers, Tabs QIP Spend and Plant in Service; Response to Staff's First Request, Item 10; HVT at 9:23, 10:32.

<sup>64</sup> Case No. 2018-00358, Final Order at 73.

replacement under the QIP, it would take 57.4 years to replace the remaining cast iron main and approximately 377 years to replace the entire main in the system.<sup>65</sup>

In response to the question whether it was reasonable to recover the cost of all projects proposed in this proceeding through the QIP Rider, Kentucky-American argued that there were two distinct categories of projects that would be included in the QIP as approved by the Commission in Case No. 2018-00358: (1) distribution infrastructure, and (2) water treatment infrastructure.<sup>66</sup> Kentucky-American argued that the projects in this proceeding are consistent with the asset categories previously approved by the Commission in Case No. 2018-00358.<sup>67</sup>

Kentucky-American maintained that, based on professional operating and engineering judgment and experience operating a water utility, it is important to commit substantial resources to asset classes in addition to mains that are aging.<sup>68</sup> Kentucky-American asserted that a reasonable balance between asset classes having mains and asset classes not having mains will maximize the length of time between rate cases. However, if the Commission were to remove otherwise-eligible plant from the QIP but approve the total amount requested in this case, Kentucky-American would place more emphasis on main replacement projects than on other asset classes.<sup>69</sup>

---

<sup>65</sup> *Id.* at 74.

<sup>66</sup> Kentucky-American's Post-Hearing Brief at 1-2.

<sup>67</sup> *Id.* at 2.

<sup>68</sup> *Id.* at 3.

<sup>69</sup> *Id.* at 2; HVT at 10:47.

As the Commissioners emphasized at the May 12, 2020 hearing, the primary reason the Commission approved the QIP was to replace aging water main that has or will be reaching the end of its service life and contributes to unaccounted-for water loss.<sup>70</sup> Kentucky-American testified in Case No. 2018-00358 that the accelerated spend that reduced the time to reduce the aging mains from 500 years to 377 years was not sustainable without a more timely cost recovery for replacement of aging mains.<sup>71</sup> Recognizing that there may be aging plant other than mains that need to be replaced when aging mains are replaced, the Commission approved additional plant categories as QIP-eligible plant in Case No. 2018-00358. However, in this proceeding, Kentucky-American proposed to spend only 60 percent of the QIP budget on main replacement, with 40 percent spent on ancillary projects that are more akin to routine operation and maintenance, or capital projects that, in Case No. 2018-00358, were proposed to be recovered in base rates, such as the Cox Street Booster Station replacement. Moreover, Kentucky-American did not provide any evidence that the 40 percent spent on ancillary projects was necessary because those projects were incidental to replacing aging mains.

As we stated in Case No. 2018-00358, the Commission retains the statutory authority to terminate or limit the QIP.<sup>72</sup> Further, as part of the review of the QIP, we must make a determination whether each project proposed by Kentucky-American is reasonably related to the purpose of the QIP to replace “aging and failing drinking water

---

<sup>70</sup> HVT at 9:51.

<sup>71</sup> Case No. 2018-00358, Direct Testimony of Nick O. Rowe (Rowe Testimony) at 11:11-18.

<sup>72</sup> Case No. 2018-00358, Final Order at 82.

infrastructure” in order to “support the public health, safety, and economic vitality of our communities.”<sup>73</sup>

Based upon the case record and being otherwise sufficiently advised, the Commission finds that Kentucky-American established that Line B Mains Replaced/Restored and Line C Mains Unscheduled are reasonably related to the purpose of the QIP, and therefore recovery of the costs for projects within Line B and Line C, along with incidental or appurtenance projects necessary to support Line B and Line C projects, should be approved. Lines B replaces cast iron and galvanized main, and Line C replaces aging main with chronic issues that require immediate work to correct unexpected failures are precisely the type of projects for which the QIP was approved.

The Commission further finds that Kentucky-American did not establish that Line D Mains Relocated; Line F Hydrants, Valves and Manholes Replaced; Line H Services and Laterals Replaced; Line J Meters Replaced, Line L SCADA Equipment and System; Line M Security Equipment and Systems; Line Q Process Plant Facilities and Equipment; and the Cox Street Booster Station are reasonably related or incidental to replacing aging mains, and therefore costs for these projects should not be recovered through the QIP Rider. Line D represents cost incurred because of the location of the main in the public right of way to accommodate municipal or state projects, not because the main is aging. Lines F, H, L, M, and Q represent infrastructure being replaced because they are malfunctioning; there is no evidence in the case record that these projects implicate unaccounted for water loss or aging water main scheduled for replacement. As for meters, when the Commission has approved surcharges to replace meters, it was

---

<sup>73</sup> Case No. 2018-00358, O’Neill Testimony at 21.



because the meters were no longer functioning and the utilities struggled to find appropriate capital to fund their replacement. Here, Kentucky-American did not provide evidence that the meters replaced under Line J are malfunctioning or that, without their inclusion in the QIP, Kentucky-American is unable to fund their replacement. Thus, it is not reasonably related to the purpose of the QIP.

The Commission further finds that Kentucky-American's request to approve the original amount proposed for all of the proposed projects but limit spending to main replacement should be denied. The evidentiary record for this proceeding does not contain substantial evidence to support authorization of additional funds for unidentified projects.

Consistent with these findings, the Commission stresses to Kentucky-American that eligible plant other than scheduled or unscheduled replacement of aging main may be included in the QIP only if such plant is replaced incidental to the replacement of aging main.

#### Reasonableness of Forecasted QIP Costs in This Case

Kentucky-American based its projected costs for the QIP projects approved in this Order on historical spending averages, providing substantial evidence to support the calculations. Kentucky-American did not include contingencies in the QIP projections. Kentucky-American proposed to use a composite rate for calculating depreciation expense and a composite rate for calculating retirement costs. Kentucky-American asserted that it applied the same methodology for forecasted costs, depreciation expenses, and retirement costs in this proceeding as it used in Case No. 2018-00358.

Based on the evidence noted above, along with the Commission's experience, the Commission finds that the forecasted costs for QIP projects approved in this Order and the methodology for calculating depreciation expenses and retirement costs are reasonable and consistent with the methodology the Commission found reasonable and accepted in Case No. 2018-00358.

#### QIP Surcharge

Based upon the above findings, the Commission finds that the proposed 1.62 percent QIP Rider is not reasonable because it includes proposed projects that are outside the scope of the purpose of the QIP to replace aging mains.

In response to a discovery request, Kentucky-American calculated a revised QIP Rider of 0.97 percent based upon plant in Budget Lines B and C, which are the proposed projects that are in the scope of the purpose of the QIP to replace aging mains.<sup>74</sup> Based upon a review of this calculation, the Commission finds that the QIP Rider of 0.97 percent is reasonable and therefore should be approved.

#### QIP Projects are Extensions in the Ordinary Course of Business

KRS 278.020(1) requires a utility to obtain a Certificate of Public Convenience or Necessity (CPCN) prior to constructing any new facility that is intended to furnish regulated utility services to the public. However, this statute also provides an exemption from the certificate requirements if the new facility is an ordinary extension of existing systems in the usual course of business. Commission regulation 807 KAR 5:001, Section 15(3), defines an ordinary extension in the usual course of business as an extension that does not create wasteful duplication of plant or conflict with existing certificates of other

---

<sup>74</sup> Response to Staff's Second Post-Hearing Request, Item 4, Response 4 Excel Attachment.

utilities operating in the same area and under the jurisdiction of the Commission, and does not involve sufficient capital outlay to materially affect the existing financial condition of the utility or will not result in increased charges to its customers.

Kentucky-American asserted that the proposed QIP projects are replacement projects that do not require a CPCN because they are extensions in the ordinary course of business pursuant to KRS 278.020(1) and 807 KAR 5:001, Section 15(3). Kentucky-American stated that the facilities do not result in the wasteful duplication of utility plant because they are replacement facilities and do not compete with the facilities of existing public utilities because they are replacement of Kentucky-American's own facilities. Kentucky-American further asserted that none of the proposed projects involve a substantial level of investment or capital outlay, and do not represent a significant alteration or addition to the normal operation of Kentucky-American's facilities.

Having reviewed the record and being sufficiently advised, the Commission finds that the QIP projects approved in this Order are ordinary extensions in the usual course of business, and therefore exempt from the requirements of a CPCN pursuant to KRS 278.020(1). The QIP projects approved in this order involve replacement of existing infrastructure with similar and like-kind plant, and thus do not create a wasteful duplication of plant. The proposed net plant addition of \$7,623,282 is 1.2 percent of Kentucky-American's \$630,083,165 in net utility plant.<sup>75</sup> Thus, the cost of the proposed QIP eligible projects do not involve sufficient capital outlay to materially affect the financial condition of Kentucky-American.

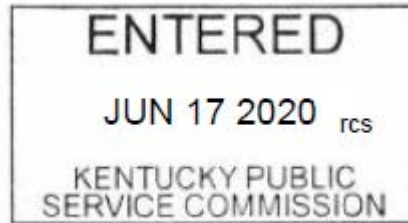
---

<sup>75</sup> Kentucky-American Annual Report for the Calendar Year Ending December 31, 2019 (filed May 12, 2020) at page 15 of 74.

IT IS THEREFORE ORDERED that:

1. The QIP Rider of 1.62 percent proposed by Kentucky-American is denied.
2. The QIP Rider of 0.97 percent is approved.
3. The QIP Rider of 0.97 percent is fair, just, and reasonable, and is approved for service rendered on and after July 1, 2020, through June 30, 2021.
4. Within 20 days of the date of this Order, Kentucky-American shall, using the Commission's electronic Tariff Filing System, file its revised tariffs setting out the rates authorized in this Order and the revised QIP Rider and reflecting they were approved pursuant to this Order.
5. This case is now closed and removed from the Commission's docket.

By the Commission



ATTEST:



---

Executive Director

Case No. 2020-00027

\*Kentucky-American Water Company  
2300 Richmond Road  
Lexington, KY 40502

\*Elaine K Chambers  
Director, Rates and Regulatory  
Kentucky-American Water Company  
2300 Richmond Road  
Lexington, KY 40502

\*John Dillon  
Kentucky-American Water Company  
2300 Richmond Road  
Lexington, KY 40502

\*Honorable Lindsey W Ingram, III  
Attorney at Law  
STOLL KEENON OGDEN PLLC  
300 West Vine Street  
Suite 2100  
Lexington, KENTUCKY 40507-1801