

COMMONWEALTH OF KENTUCKY  
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

ELECTRONIC APPLICATION OF KENTUCKY-	)	
AMERICAN WATER COMPANY TO AMEND	)	CASE NO.
TARIFF TO REVISE QUALIFIED	)	2024-00173
INFRASTRUCTURE PROGRAM CHARGE	)	

ORDER

On May 31, 2024, Kentucky-American Water Company (Kentucky-American) filed its fifth Qualified Infrastructure Program (QIP) Rider (QIP 5) seeking authority to implement a surcharge for recovery of certain capital expenses to replace a portion of its aging water system infrastructure. Kentucky-American proposed an effective date of September 1, 2024, and ending on December 31, 2024. There are no intervenors in this proceeding. 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 mains that otherwise would not be replaced in a timely manner.<sup>1</sup> In that proceeding, Kentucky-American stated that it would prioritize the replacement of cast iron and galvanized steel mains, which represented 15 percent of the distribution system but accounted for 64.2 percent of annual main breaks.<sup>2</sup> Kentucky-American further stated that the QIP would utilize a

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<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. According to Kentucky-American, its infrastructure was deteriorating at a faster rate than the replacement rate.

<sup>2</sup> Case No. 2018-00358, June 27, 2019 final Order at 76.

“systematic replacement plan” with a 25-year replacement cycle, and provided a list of QIP-eligible projects for the first five years.<sup>3</sup>

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 \$122,919,594 authorized revenue requirement established in Case No. 2023-00191.<sup>4</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 updated base rates are approved because the updated base rates include recovery of the annual costs previously recovered through the QIP.

In the first QIP tariff (QIP 1), Case No. 2020-00027, Kentucky-American proposed QIP investment that consisted of 60 percent main replacement projects and 40 percent non-main plant replacement stand-alone projects, which were not incidental to main replacement.<sup>5</sup> In the final Order for Case No. 2020-00027, the Commission emphasized that the primary reason it approved Kentucky-American’s QIP was to replace aging water mains that were reaching the end of their service life and contributing to Kentucky-

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<sup>3</sup> Case No. 2018-00358, (filed Nov. 28, 2018) Direct Testimony of Brent E. O’Neill (O’Neill Direct Testimony), Exhibit 1 and Exhibit 2 at 12.

<sup>4</sup> Case No. 2023-00191 *Electronic Application of Kentucky-American Water Company for an Adjustment of Rates, A Certificate of Public Convenience and Necessity for Installation of Advanced Metering Infrastructure, Approval of Regulatory and Accounting Treatments, and Tariff Revisions* (Ky. PSC May 3, 2023) (rehearing pending).

<sup>5</sup> Case No. 2020-00027, *Electronic Application of Kentucky-American Water Company to Amend Tariff for the Establishment of Qualified Infrastructure Program Charge* (Ky. PSC June 17, 2020).

American's unaccounted-for water loss.<sup>6</sup> The Commission rejected stand-alone projects for non-main plant replacement, finding 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."<sup>7</sup>

For Case No. 2021-00090,<sup>8</sup> the QIP 2 tariff rider (QIP 2) application, Kentucky-American proposed a strategic capital expenditures plan (SCEP) for QIP 2 that included four budget line items deemed "recurring projects"<sup>9</sup> that were not specifically developed for the QIP 2, but instead were projects previously identified as part of Kentucky-American's larger plan to systematically accelerate spending on replacing aging infrastructure.<sup>10</sup> Based upon its interpretation of Commission Case No. 2020-00027, Kentucky-American accelerated the replacement cycle of its main replacements in QIP 2 from a 25-year cycle to a 20-year cycle.<sup>11</sup> The proposed reduction in the main replacement cycle increased Kentucky-American's projected main replacement spending from \$7,623,282 in net plant additions approved in Case No. 2020-00027 to \$20,028,974 requested in QIP 2.<sup>12</sup>

In the final Order of Case No. 2021-00090, the Commission found that Kentucky-American's main replacement projects in future QIP applications should be based on a

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<sup>6</sup> Case No. 2020-00027, June 17, 2020 Order at 15.

<sup>7</sup> Case No. 2020-00027, June 17, 2020 Order at 17.

<sup>8</sup> Case No. 2021-00090, *Electronic Application of Kentucky-American Water Company to Amend Tariff to Revise Qualified Infrastructure Program Charge* (Ky. PSC June 21, 2021), Order.

<sup>9</sup> Case No. 2021-00090, June 21, 2021 Order at 3.

<sup>10</sup> Case No. 2021-00090, June 21, 2021 Order at 3.

<sup>11</sup> Case No. 2021-00090, June 21, 2021 Order at 6.

<sup>12</sup> Case No. 2021-00090, June 21, 2021 Order at 6.

25-year replacement cycle, be limited to annual main replacements of 10 to 13 miles, and be for QIP projects consistent with the amounts approved in Case No. 2018-00358.<sup>13</sup> The Commission directed Kentucky-American to be prepared to explain how each proposed project meets the prioritization matrix and external drivers in its 2022 QIP filing, and demonstrate what efforts Kentucky-American has implemented with contractors, suppliers, local transportation and engineering officials, and other utilities to contain and manage project costs.<sup>14</sup> Additionally, the Commission ordered Kentucky-American to provide evidence of the steps it has taken to control such costs.<sup>15</sup>

Further, in Case No. 2021-00090, the Commission found that “Kentucky-American must demonstrate that it is more proactive in planning for and managing construction costs, and relaying accurate data to the Commission, given that costs that are not found to be reasonable cannot be recovered from ratepayers.”<sup>16</sup> The Commission requested that in the 2022 QIP filing Kentucky-American include what efforts it had “. . . implemented with contractors, suppliers, local transportation and engineering officials, and other utilities to contain and manage project costs.”<sup>17</sup>

Kentucky-American proposed expenditures for QIP 3 that were limited to the “Budget Line B: QIP Mains Replaced/Restored items,”<sup>18</sup> to be constructed with internal

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<sup>13</sup> Case No. 2021-00090, June 21, 2021 Order at 12.

<sup>14</sup> Case No. 2021-00090, June 21, 2021 Order at 13.

<sup>15</sup> Case No. 2021-00090, June 21, 2021 Order at 17.

<sup>16</sup> Case No. 2021-00090, June 21, 2021 Order at 17.

<sup>17</sup> Case No. 2021-00090, June 21, 2021 Order at 17-18.

<sup>18</sup> Case No. 2022-00032, (filed Mar. 1, 2022), Direct Testimony of Krista Citron (Citron/Porter Direct Testimony) at 4.

labor or with pre-qualified contractors to whom Kentucky-American submitted requests for proposals.<sup>19</sup> Kentucky-American explained that the projects are based on a 10 to 13 mile per year replacement rate to meet its 25-year replacement goal.<sup>20</sup> Specifically, the investments included in the proposed QIP 3 were intended to replace aging infrastructure that were non-revenue producing.<sup>21</sup>

Kentucky-American explained it used a similar prioritization model to identify QIP three projects to that used to develop proposed QIP projects in Case Nos. 2018-00358, 2020-00027, and 2021-00090.<sup>22</sup> The prioritization matrix criteria includes the amount of water pressure, number of breaks or leaks, main age, main material type, main size, and water quality, and are evaluated along with external drivers, such as customer impact and scheduled paving by other governmental entities, to develop a final project list and schedule.<sup>23</sup> Kentucky-American stated that the majority of replaced mains in that budget line are cast iron and galvanized mains and these mains represent 15.9 percent of the total inventory and 64 percent of all breaks.<sup>24</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 January 2012 and December 2016.<sup>25</sup> Kentucky-American asserted that replacing cast iron and galvanized

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<sup>19</sup> Case No. 2022-00032, Citron/Porter Direct Testimony at 5-6.

<sup>20</sup> Case No. 2022-00032, Citron/Porter Direct Testimony at 4.

<sup>21</sup> Case No. 2022-00032, Citron/Porter Direct Testimony at 4.

<sup>22</sup> Case No. 2022-00032, Citron/Porter Direct Testimony at 7-8.

<sup>23</sup> Case No. 2022-00032, Citron/Porter Direct Testimony at 7-8.

<sup>24</sup> Case No. 2022-00032, Citron/Porter Direct Testimony at 6.

<sup>25</sup> Case No. 2022-00032, Citron/Porter Direct Testimony at 6-7.

steel water main infrastructure would result in a direct customer benefit of improved and sustained water quality and ensure reliability of water service to Kentucky-American customers.<sup>26</sup>

In accordance with the final Order in Case No. 2021-00090, Kentucky- American provided detailed descriptions of how each proposed project included in QIP 3 addressed the aspects of its prioritization matrix in its selection.<sup>27</sup>

In the final Order of Case No. 2023-00030, the Commission directed Kentucky-American in all future QIP filings to include detailed, supporting documentation justifying how Kentucky-American develops its scope of work and cost estimates for each project, including an itemized breakdown for material, labor, and paving and reasoning for each variance from the original estimate.<sup>28</sup> Accordingly, the Commission put Kentucky American on notice that, in future QIP applications, it would hold the utility accountable for cost overruns that are a result from Kentucky-American's actions or inactions.<sup>29</sup>

#### QIP 5

Kentucky-American proposed no new projects for QIP 5 and a four-month effective period of September 1, 2024, to December 31, 2024, to allow future QIP periods to align with a calendar year.<sup>30</sup> The Commission, in its rehearing final order in Case No. 2023-

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<sup>26</sup> Case No. 2022-00032, Citron/Porter Testimony at 7.

<sup>27</sup> Case No. 2022-00032, Citron/Porter Testimony, Exhibit 3.

<sup>28</sup> Case No. 2023-00030, *Electronic Application of Kentucky-American Water Company to Amend Tariff to Revise Qualified Infrastructure Charge* (Ky. PSC Sept. 29, 2023), final Order at 12-13.

<sup>29</sup> Case No. 2023-00030, Sept. 29, 2023 final Order at 12-13.

<sup>30</sup> Newcomb Direct Testimony and Exhibits (filed May 31, 2024), Ex. 1-2 at 3.

00300, granted Kentucky-American’s request that the QIP filing schedule align with calendar year using the schedule below.<sup>31</sup>

<b>Filing</b>	<b>Filing Date</b>	<b>QIP Period Start / Rates Effective</b>	<b>QIP Period End</b>	<b>Balancing Adjustment</b>
QIP 5*	5/31/2024	9/1/2024	12/31/2024	None*
QIP 6	8/31/2024	1/1/2025	12/31/2025	QIP 4
QIP 7	8/31/2025	1/1/2026	12/31/2026	QIP 5
QIP 8	8/31/2026	1/1/2027	12/31/2027	QIP 6

\*Filing to remove QIP 3 Balancing Adjustment and proposing no new QIP investments.

Kentucky-American also proposed the removal of the of the QIP 3 balancing adjustment from the QIP 5 charge because the QIP 3 Balancing Adjustment should be fully recovered by the beginning of the QIP 5 period.<sup>32</sup>

Kentucky-American’s proposed QIP Rider is 6.41 percent including the removal of the QIP 3 balancing adjustment and requested rehearing revenues of \$120,635,314 from Case No. 2023-00191.<sup>33</sup> As of the date of this order, Kentucky-American’s request for rehearing implicating its authorized revenues remains pending before the Commission. Consequently, the Commission finds that Kentucky-American’s proposed QIP Rider of 6.41 relies upon revenue numbers that are not known or measurable, thus is not reasonable.

QIP Rider Surcharge Amount

Based upon the above findings, the Commission rejects Kentucky-American’s proposed 6.41 percent QIP Rider and finds that a Kentucky-American QIP Rider of

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<sup>31</sup> Case No. 2023-00300, *Electronic Application of Kentucky-American Water Company for a Balancing Adjustment for Its QIP Charge* (Ky. PSC Aug. 12, 2024), rehearing final Order.

<sup>32</sup> Newcomb Direct Testimony and Exhibits 1-2 at 3.

<sup>33</sup> Application (filed May 31, 2024), Newcomb Workpapers.

6.29 percent<sup>34</sup> to be reasonable based upon the authorized revenues from the final Order of Case No. 2023-00191 of \$122,919,594<sup>35</sup> and removing the QIP 3 balancing adjustment. The calculation of the Commission's QIP rider for Kentucky-American is set forth in the Appendix to this Order. If the authorized revenues change as a result of the rehearing final Order in the Case No. 2023-00191 the difference may be addressed in a future QIP filing.

IT IS THEREFORE ORDERED that:

1. The QIP Rider of 6.41 percent as proposed by Kentucky-American is rejected.
2. The QIP Rider of 6.29 percent is approved for service rendered on and after September 1, 2024, through December 31, 2024.
3. In all future QIP filing applications, Kentucky-American shall include detailed, supporting documentation justifying how it develops its scope of work and cost estimates for each project, including an itemized breakdown for material, labor, and paving as well as reasoning for each variance from the original estimate.
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 revised QIP Rider and reflecting it was approved pursuant to this Order.
5. This case is now closed and removed from the Commission's docket.

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<sup>34</sup> 0.83 (QIP 1) +1.87% (QIP 2) + 2.55% (QIP 3) +1.05% (QIP 4) +0.00% (QIP 5) = 6.29% (Total QIP).

<sup>35</sup> Case No. 2023-00191, May 3, 2024 final Order.



PUBLIC SERVICE COMMISSION

Chairman



Vice Chairman

Commissioner



ENTERED  
AUG 30 2024  
KENTUCKY PUBLIC SERVICE COMMISSION <sup>rCS</sup>

ATTEST:



Executive Director

## APPENDIX

### APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE COMMISSION IN CASE NO. 2024-00173 DATED AUG 30 2024

	QIP 1 July 2020 - June 2021	QIP 2 July 2021 - June 2022	QIP 3 July 2022 - June 2023	QIP 4 July 2023 - June 2024	QIP 5 September 2024 - December 2024	Total QIP
QIP Plant Additions	\$9,328,645	\$19,931,459	\$28,150,400	\$9,728,609	\$0	\$67,139,113
Retirements	(633,049)	(414,148)	(524,527)	(219,472)		(1,791,196)
<b>Net Change to Gross Plant</b>	<b>8,695,596</b>	<b>19,517,311</b>	<b>27,625,873</b>	<b>9,509,137</b>	<b>0</b>	<b>65,347,917</b>
Cost of Removal	549,261	2,433,439	(659,177)	972,861		3,296,384
Retirements	633,049	414,148	524,527	219,472		1,791,196
Depreciation Accrual - QIP 1	(137,516)					(137,516)
Depreciation Accrual - QIP 2		(311,545)				(311,545)
Depreciation Accrual - QIP 3			(422,676)			(422,676)
Depreciation Accrual - QIP 4				(145,490)		(145,490)
<b>Net Change to Accum Depr</b>	<b>1,044,794</b>	<b>2,536,041</b>	<b>(557,326)</b>	<b>1,046,843</b>	<b>0</b>	<b>4,070,353</b>
<b>Net Change to Net Plant</b>	<b>9,740,390</b>	<b>22,053,352</b>	<b>27,068,547</b>	<b>10,555,980</b>		<b>69,418,270</b>
Accumulated Deferred Taxes - QIP 1	(1,550,183)					(1,550,183)
Accumulated Deferred Taxes - QIP 2		(3,674,353)				(3,674,353)
Accumulated Deferred Taxes - QIP 3			(1,663,894)			(1,663,894)
Accumulated Deferred Taxes - QIP 4				(1,747,671)		(1,747,671)
<b>Net Change to Rate Base</b>	<b>8,190,207</b>	<b>18,379,000</b>	<b>25,404,653</b>	<b>8,808,309</b>	<b>0</b>	<b>60,782,170</b>
Pre-Tax Rate of Return	9.28%	9.28%	9.28%	9.28%		9.28%
QIP Revenue on Net Change to Rate Base	760,223	1,705,957	2,358,085	817,596	0	5,641,862
QIP Depreciation Expense - QIP 1	137,516					137,516
QIP Depreciation Expense - QIP 2		311,545				311,545
QIP Depreciation Expense - QIP 3			422,676			422,676
QIP Depreciation Expense - QIP 4				145,490		145,490
QIP Property Taxes - QIP 1	120,869	21,361	(4,348)	7,826		145,708
QIP Property Taxes - QIP 2		261,532	(9,759)	17,566		269,339
QIP Property Taxes - QIP 3			362,929	24,376		387,305
QIP Property Taxes - QIP 4				274,540		274,540
<b>QIP Revenue Requirement Rate Adj</b>	<b>\$1,018,608</b>	<b>\$2,300,395</b>	<b>\$3,129,584</b>	<b>\$1,287,393</b>	<b>\$0</b>	<b>\$7,735,980</b>
Authorized Revenues 2023-00191	\$122,919,594	\$122,919,594	\$122,919,594	\$122,919,594	\$122,919,594	\$122,919,594
QIP Rider Charge	0.83%	1.87%	2.55%	1.05%	0.00%	6.29%

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

\*Jeffrey Newcomb  
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

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