COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

ELECTRONIC APPLICATION OF KENTUCKY-AMERICAN WATER COMPANY FOR AN ADJUSTMENT OF RATES	)))	CASE NO. 2025-00122

O R D E R

On May 16, 2025, Kentucky-American Water Company (Kentucky-American), pursuant to KRS 278.180, KRS 278.190, and 807 KAR 5:001, Section 16(1)(b)(1), filed an application requesting an increase to its rates.

BACKGROUND

Kentucky-American, a wholly owned subsidiary of American Water Works Company, Inc. (American Water), is a jurisdictional utility that distributes and sells water across three divisions, including its Central Division, which consists of Bourbon, Clark, Fayette, Harrison, Jessamine, Nicholas, Scott, and Woodford counties; its Northern Division, which consists of Gallatin, Owen, Grant, and Franklin counties; and its Southern Division, which consists of Rockcastle and Jackson counties.[1] Kentucky-American

[1] Application (filed May 16, 2025) at 1.

provides water service to more than 139,532 customers throughout its three divisions.[2] Kentucky-American last applied for a general rate adjustment in 2023.[3]

PROCEDURAL HISTORY

Kentucky-American filed its application on May 16, 2025. In its application, Kentucky-American requested an increase in water revenues of $26.9 million per year for the forecasted test period,[4] compared to the operating revenues for the forecasted test period under existing water rates. Kentucky-American asserted this would result in a 19.9 percent increase in water service revenues, net of Qualified Improvement Plan (QIP) revenues.[5]

By Order entered May 27, 2025, the Commission suspended the proposed rates up to and including December 16, 2025, and set forth a procedural schedule.[6] The Attorney General of the Commonwealth of Kentucky, by and through the Office of Rate Intervention (Attorney General),[7] and Lexington Fayette Urban County Government (LFUCG)[8] were granted intervention in this matter. The Attorney General and LFUCG

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[2] *Annual Report of Kentucky-American Water Company for the Year ended December 31, 2024* (2024 Annual Report), at 55.

[3] 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, 2024), as modified by Order (Ky. PSC May 17, 2024).

[4] Application at 3.

[5] Application at 3.

[6] Order (Ky. PSC May 27, 2025).

[7] Order (Ky. PSC May 6, 2025).

[8] Order (Ky. PSC May 27, 2025).

filed a memorandum of understanding and co-sponsored two witnesses (jointly, Attorney General/LFUCG).[9] An informal technical conference was held on June 12, 2025.[10]

On September 15, 2025, Kentucky-American filed a base period update (Base Period Update) that provided an updated revenue deficiency of $27.2 million; however, Kentucky-American stated that it did not intend to amend its application.[11]

Kentucky-American responded to a total of seven requests for information from Commission Staff.[12] Kentucky-American responded to four requests for information from the Attorney General.[13] Kentucky-American responded to two requests for information from LFUCG.[14] The Attorney General/LFUCG responded to one request for information

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[9] Memorandum of Understanding (filed Aug. 6, 2025).

[10] Notice of Filing (filed June 17, 2025).

[11] Base Period Update (filed Sept. 15, 2025); Rebuttal Testimony of Dominic DeGrazia (Degrazia Rebuttal Testimony) at 2.

[12] Kentucky-American's Response to Commission Staff's First Request for Information (Staff's First Request) (filed June 5, 2025); Kentucky-American's Response to Commission Staff's Second Request for Information (Staff's Second Request) (filed July 7, 2025); Kentucky-American's Response to Commission Staff's Third Request for Information (Staff's Third Request) (filed Aug. 4, 2025); Kentucky-American's Response to Commission Staff's Fourth Request for Information (Staff's Fourth Request) (filed Sept. 8, 2025); Kentucky-American's Response to Commission Staff's First Post-Hearing Request for Information (Staff's First Post-Hearing Request) (filed Oct. 6, 2025); Kentucky-American's Response to Commission Staff's Second Post-Hearing Request for Information (Staff's Second Post-Hearing) (filed Oct. 21, 2025); Kentucky-American's Response to Commission Staff's Third Post-Hearing Request for Information (Staff's Third Post-Hearing Request) (filed Oct. 27, 2025).

[13] Kentucky-American's response to Attorney General's First Request for Information (Attorney General's First Request) (filed July. 7, 2025); Kentucky-American's response to Attorney General's Second Request for Information (Attorney General's Second Request) (filed Aug. 4, 2025); Kentucky-American's response to the Attorney General's First Post-Hearing Request for Information (Attorney General's First Post-Hearing Request) (filed Oct. 6, 2025); Kentucky-American's response to Attorney General's Second Request for Information (Attorney General's Second Post-Hearing Request) (filed Oct. 21, 2025).

[14] Kentucky-American's Response to LFUCG's First Request for Information (LFUCG's First Request) (filed July 7, 2025); Kentucky-American's Response to LFUCG's Second Request for Information (LFUCG's Second Request) (filed Aug. 4, 2025).

from Commission Staff and one request for information from Kentucky-American.[15] Several supplemental responses were filed throughout the processing of this matter as well.

The Commission held an evidentiary hearing on September 23, 2025. All parties filed simultaneous post-hearing briefs on October 27, 2025. On November 26, 2025, Kentucky-American filed a motion and a supplemental response to a post-hearing request for information which was granted by Order issued December 10, 2025.[16] This matter now stands submitted to the Commission for a decision.

TEST PERIOD

Kentucky-American used as its forecasted test period the 12-month period ending December 31, 2026.[17] Its base period is the 12-month period ending August 31, 2025.[18] The base period and test year period meet the requirements in KRS 278.192 and KAR 5:001, Sections 16(6), (7), and (8). Neither the Attorney General nor LFUCG objected to use of the test period. The Commission finds that it is reasonable to use the 12-month period ending December 31, 2026, as the test period in this case.

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[15] Attorney General/LFUCG's Response to Commission Staff's First Request for Information (filed Sept. 8, 2025); Attorney General/LFUCG's Response to Kentucky-American's First Request for Information (filed Sept. 8, 2025).

[16] Motion for Leave to File Supplemental Testimony and Supplemental Response to Staff's First Post-Hearing Request, Item 12 (filed Nov. 26, 2025); Order (Ky. PSC Dec. 10, 2025).

[17] Application at 2.

[18] Application at 2.

REVENUE REQUIREMENT

Description	Forecasted Test Period Application	Company Update Adjustments	Forecasted Test Period Updated	Commission Adjustments	Forecasted Test Period
Operating Revenues	$ 136,559,853	$ (686,892)	$ 135,872,961	$ -	$ 135,872,961
Less Deductions:					
Operating & Maintenance	51,026,925	(397,673)	50,629,252	(2,634,280)	47,994,973
Depreciation	34,995,892	-	34,995,892	-	34,995,892
Amortization of UPAA	14,723	-	14,723	-	14,723
Amortization Expense	57,080	-	57,080	(559,620)	(502,540)
State Income Taxes	1,136,434	(14,238)	1,122,196	174,560	1,296,756
Federal Income Taxes	3,549,403	(56,809)	3,492,594	696,493	4,189,087
Investment Tax Credits	-	-	-	-	-
General Taxes	12,861,924	(1,067)	12,860,857	(134,950)	12,725,907
Total Operating Expenses	103,642,381	(469,787)	103,172,594	(2,457,798)	100,714,798
Operating Income	$ 32,917,472	$ (217,105)	$ 32,700,367	$ 2,457,796	$ 35,158,163

Rate Base Adjustments

Growth Factor – In order to forecast expenses, Kentucky-American stated that it developed a company-specific Operations and Maintenance growth factor (O&M Growth Factor) in response to the Commission's directive to employ a forecasting methodology that is more reflective of Kentucky-American's experience than using general consumer price index (CPI) inflationary factors as seen in its most recent rate case.[19] In Case No. 2023-00191, Kentucky-American applied a three-year-average inflation factor, based on the CPI from the Bureau of Labor Statistics, to its base period to arrive at its test year level of expense for the following expenses:

- Fuel and Power Expense,
- Support Services Expense,

[19] 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, 2024), final Order at 18; Kentucky-American's Response to Staff's Second Request, Item 1.

- Contracted Services Expense,
- Building Maintenance and Services Expense,
- Office Supplies and Services Expense,
- Employee Related Expense,
- Miscellaneous Expense,
- Rents Expense,
- Customer Accounting (Other) Expense, and
- Maintenance Supplies and Services Expense

Alternatively, in this proceeding, Kentucky-American utilized a three-year average of its own costs for each of the following expenses based on the O&M Growth Factor of 5.16 percent to increase these expenses:

- Support Services Expense,
- Contracted Services Expense,
- Building Maintenance and Services Expense,
- Telecommunication Expenses,
- Office Supplies and Services Expense,
- Employee Related Expense,
- Miscellaneous Expenses,
- Rents Expense,
- Customer Accounting (Other) Expense, and
- Maintenance Supplies and Services Expense.[20]

Then, Kentucky-American, in most instances, applied its O&M Growth Factor on a prorated basis to each of these expenses in both the forecasted portion of its base period and its forecasted test period (O&M Growth Factor Adjustment). The application of this growth factor resulted in an increase to Kentucky-American's Operations and Maintenance expenses, in aggregate, of $919,307 to the forecasted test year. Each individual adjustment is described below.

The Attorney General/LFUCG argued that the costs for the expenses listed above fluctuate over time and, as such, an assumed "growth factor" increase for the forecasted

[20] Kentucky-American's Response to Staff's First Request Item 1, Excel Files, KAWC 2025 Rate Case – KAW O&M Growth Factor Workpaper.

test year is unknown and unwarranted.[21] The Attorney General/LFUCG recommended the Commission reject Kentucky-American's O&M Growth Factor adjustment in its entirety.[22]

In its post-hearing brief, Kentucky-American argued the O&M Growth Factor was not an arbitrary inflation factor but instead a company-specific percentage grounded in actual experience.[23] Kentucky-American argued that it addresses the Commission's concerns regarding the Company's use of general inflationary percentages in prior rate proceedings.[24] In its brief, the Attorney General argued that, when the expenses are reviewed over time, the expense amounts vary, negating the need for a growth adjustment factor.[25] The Attorney General averred the growth factor approach was high-level approach and not a "more robust forecasting" methodology as discussed in the final Order in Case No. 2023-00191.[26] In conclusion, the Attorney General stated that the Commission disallowed the Kentucky-American's proposed inflation adjustment for similar expense categories in the 2023 rate case and should likewise in this case.[27]

The Commission finds that the company-specific O&M Growth Factor is more indicative of Kentucky-American's experiences than CPI inflationary growth factors. The

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[21] Attorney General/LFUCG's Direct Testimony (filed Aug. 13, 2025), Direct Testimony of John Defever (Defever Direct Testimony) at 27.

[22] Defever Direct Testimony at 27.

[23] Kentucky-American's Post Hearing Brief (Kentucky-American's Brief) (filed Oct. 27, 2025) at 30.

[24] Kentucky-American's Brief at 30.

[25] Attorney General's Brief (filed Oct. 27, 2025) at 21.

[26] Attorney General's Brief at 22, *citing* Case No. 2023-00191 (Ky. PSC May 3, 2024), final Order at 17–19.

[27] Attorney General's Brief at 22.

Commission notes that Kentucky-American's utilization of its own trends in historical expenses to forecast its future expenses represents a forecasting methodology that is more reasonable than applying inflationary factors to its base period. Because of this, the Commission finds that the O&M Growth Factor Adjustment should be accepted as filed, with the exception of the Contracted Services Expense and Rent Expense, as further discussed below.

However, while the Commission agrees that the inclusion of the company-specific O&M Growth Factor is more indicative of Kentucky-American's experiences, the Commission expects a utility with the size and experience of Kentucky-American, along with the shared resources of American Water, to forecast each operating expense in a way that is more reflective of Kentucky-American's internal budgeting process for each expense, rather than using a blanket growth factor to increase a number of expenses. The Commission notes that, during the evidentiary hearing, Kentucky-American stated that the growth factor did not represent its own, internal budgeting practices,[28] and while it was similar, the Commission expects Kentucky-American to follow its internal budgeting process when forecasting its test year expenses in its next base rate proceeding.

<u>Support Services Expense</u> – Kentucky-American proposed a forecasted Support Services Expense in the amount of $14,821,708.[29] In its initial application, Kentucky-American stated that the forecasted level of its Support Services Expense reflected changes in labor, labor related, and other costs, as well as the removal of charitable contributions, advertising, severance, and the allocation applied to its sewer division

[28] Hearing Video Transcript (HVT) of the September 23, 2025 Hearing, Robert Prendergast at 02:15:08–02:16:50.

[29] Application, Exhibit 37, Schedule C-1.

(0.06 percent).[30] However, in response to discovery, Kentucky-American stated that it included a 12-month compound annual growth rate (CAGR) adjustment in its calculation of Support Services Expense in the test year, which utilized the Kentucky-American O&M Growth Factor.[31] The O&M Growth Factor Adjustment increased Kentucky-American's Support Services Expense by $244,429. As noted above, the Attorney General objected to this adjustment.[32]

The Commission finds that Kentucky-American's Support Services Expense is reasonable and should be accepted. The adjustment, using the O&M Growth Factor is more representative of Kentucky-American's historical cost trends than applying a CPI inflationary adjustment.

<u>Contracted Services Expense</u> – Kentucky-American proposed an increase to its base period level of Contracted Services Expense in the amount of $111,261 to arrive at its forecasted test year Contracted Services Expense of $1,728,444.[33] Kentucky-American stated that the forecasted level of its Contracted Services Expense was based on the utilization of the O&M Growth Factor Adjustment.[34] As noted above, the Attorney General objected to this adjustment.[35]

The Commission finds that Kentucky-American's Contracted Services Expense adjustment should be based on known and measurable changes to its agreements with

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[30] Application, Exhibit 37, Schedule D-2.

[31] Kentucky-American's Response to Staff's Third Request, Item 4.

[32] Defever Direct Testimony at 27.

[33] Application, Exhibit 37, Schedule C-1.

[34] Kentucky-American Response to Staff's Third Request, Item 1.

[35] Defever Direct Testimony at 27.

its contractors, rather than an inflation-based adjustment. As such, the Commission finds that the O&M Growth Factor adjustment should be removed from Kentucky-American's forecasted Contracted Services Expense. This adjustment will reduce Kentucky-American's forecasted Contracted Services Expense by $131,858 with a corresponding reduction to Kentucky-American's base revenue requirement of $132,683.

Building Maintenance and Services Expense – Kentucky-American proposed an increase to its Building Maintenance and Services Expense in the amount of $104,831 to arrive at a test year expense level of $1,628,524.[36] Kentucky-American stated that this increase reflected the utilization of Kentucky-American's Growth Factor Adjustment.[37] As noted above, the Attorney General objected to this adjustment.[38]

The Commission finds that the application of Kentucky-American's Growth Factor Adjustment to its Building Maintenance and Services Expense produces a reasonable forecasted expense while also being more indicative of Kentucky-American's cost trends than a CPI inflationary adjustment. For those reasons, the Commission finds that Kentucky-American's Building Maintenance and Services Expense should be accepted as filed.

Telecommunication Expense – Kentucky-American proposed an increase to Telecommunication Expense in the amount of $20,982 to arrive at a test year Telecommunication Expense of $325,955.[39] Kentucky-American stated that this increase

[36] Application, Exhibit 37, Schedule C-1.

[37] Application, Exhibit 37, Schedule D-2.

[38] Defever Direct Testimony at 27.

[39] Application, Exhibit 37, Schedule C-1.

reflected the utilization of Kentucky-American's Growth Factor Adjustment.[40] As noted above, the Attorney General objected to this adjustment.[41]

The Commission finds that the application of Kentucky-American's Growth Factor Adjustment to its Telecommunication Expense produces a fair, just and reasonable forecasted expense while also being more indicative of Kentucky-American's cost trends than a CPI inflationary adjustment. For those reasons, the Commission finds that Kentucky-American's Telecommunication Expense should be accepted as filed.

<u>Office Supplies and Services Expense</u> – Kentucky-American proposed an increase to its Office Supplies and Services expense in the amount of $40,940, to arrive at a test year expense of $342,626.[42] Kentucky-American stated that there were adjustments made to account for uniform expenses, software costs, and normalize credit line fees. In addition to these adjustments, Kentucky-American also applied its O&M Growth Factor adjustment to its base year level of expense to arrive at its test year expense.[43] In response to discovery, Kentucky-American stated that after performing further analysis of the Credit line fees forecast, it realized that the normalized adjustment of $8,333 was made in error and removed $8,333 from its test year level of expense, resulting in a forecasted test year amount of Office Supplies and Services expense of

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[40] Application, Exhibit 37, Schedule D-2.

[41] Defever Direct Testimony at 27.

[42] Application, Exhibit 37, Schedule C-1.

[43] Application, Exhibit 37, Schedule D-2.

$324,583.[44] As noted above, the Attorney General objected to Kentucky-American's O&M Growth Factor Adjustment.[45]

The Commission finds that both adjustments that Kentucky-American made: (1) to apply Kentucky-American's Growth Factor Adjustment to its Office Supplies and Services Expense, and (2) to account for uniform expenses, software costs, and normalize credit fees produces a reasonable forecasted expense while also being more indicative of Kentucky-American's cost trends than a CPI inflationary adjustment. For those reasons, the Commission finds that Kentucky-American's Office Supplies and Services Expense should be accepted as filed.

Employee-Related Expense – Kentucky-American proposed an increase to its Employee Related Expense in the amount of $41,074, to arrive at a test year Employee Related Expense of $236,418.[46] Kentucky-American stated that it made an adjustment to incorporate a three-year average of its relocation expense in addition to applying the O&M Growth Factor Adjustment to the base period of expense to arrive at its test year expense.[47] As noted above, the Attorney General objected to Kentucky-American's O&M Growth Factor Adjustment.[48]

The Commission finds that both adjustments that Kentucky-American made: (1) to apply Kentucky-American's Growth Factor Adjustment to its Employee-Related Expense, and (2) to incorporate a three-year average of its relocation expense, produces a fair, just

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[44] Kentucky-American's Response to Staff's Third Request, Item 20.

[45] Defever Direct Testimony at 27.

[46] Application, Exhibit 37, Schedule C-1.

[47] Application, Exhibit 37, Schedule D-2.

[48] Defever Direct Testimony at 27.

and reasonable forecasted expense while also being more indicative of Kentucky-American's cost trends than a CPI inflationary adjustment. For those reasons, the Commission finds that Kentucky-American's Employee Related Expense should be accepted as filed.

Miscellaneous Expenses – Kentucky-American proposed to increase its Miscellaneous Expense in the amount of $19,512, to arrive at a test year Miscellaneous Expense of $1,161,823.[49] Kentucky-American stated that the adjustment to its Miscellaneous Expense was to remove charitable contributions in addition to applying the O&M Growth Factor Adjustment to the base period level of expense to arrive at its test year expense.[50] As noted above, the Attorney General objected to Kentucky-American's O&M Growth Factor Adjustment.[51]

The Commission finds that both adjustments Kentucky-American made: (1) to apply Kentucky-American's Growth Factor Adjustment to its Miscellaneous Expense, and (2) to remove charitable contributions, produces a reasonable forecasted expense while also being more indicative of Kentucky-American's cost trends than a CPI inflationary adjustment. Further, Kentucky-American's removal of charitable contributions follows prior Commission precedent.[52] For those reasons, the Commission finds that Kentucky-American's Miscellaneous expense should be accepted as filed.

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[49] Application, Exhibit 37, Schedule C-1.

[50] Application, Exhibit 37, Schedule D-2.

[51] Defever Direct Testimony at 27.

[52] Case No. 2023-00191, (Ky. PSC, May 3, 2024), final Order at 22.

Rent Expense -- Kentucky-American proposed an increase to Rent Expense in the amount of $4,282, to arrive at a test year Rent Expense of $66,516.[53] Kentucky-American stated that the forecasted level of its Rent Expense included a base year adjustment to normalize the base year expense.[54] After the normalization adjustment, Kentucky-American applied it's O&M Growth Factor Adjustment to its Rent Expense in the base period to forecast the expense in the test year.[55] As noted above, the Attorney General objected to this adjustment.[56]

The Commission finds that Kentucky-American's normalization adjustment should be accepted as filed, as the amounts of Rent expense in the Base Period included negative amounts. The Commission finds that Kentucky-American's Rent Expense adjustment should be based on known and measurable changes to its rental contracts, rather than an inflation-based adjustment. As such, the Commission finds that the growth factor adjustment should be removed from Kentucky-American's forecasted Rent Expense. This adjustment will reduce Kentucky-American's forecasted Rent Expense by $5,075 with a corresponding reduction to Kentucky-American's base revenue requirement of $5,108.

Other Customer Accounting Expense – Kentucky-American proposed an increase to its Other Customer Accounting Expense in the amount of $7,734, to arrive at a test year Other Customer Accounting expense of $120,150.[57] Kentucky-American stated that

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[53] Application, Exhibit 37, Schedule C-1.

[54] Application, Exhibit 37, Schedule D-2.

[55] Application, Exhibit 37, Schedule D-2.

[56] Defever Direct Testimony at 27.

[57] Application, Exhibit 37, Schedule C-1.

it included two adjustment to its base period level of Other Customer Accounting expense: (1) to normalize the projected base year expense and (2) to apply its O&M Growth Factor Adjustment.[58] As noted above, the Attorney General objected to Kentucky-American's O&M Growth Factor Adjustment.[59]

In response to discovery, Kentucky-American stated that it believed that the 2024 level of its Other Customer Accounting expense, adjusted for an anticipated decline in bank service charges, was a better representation of the forecasted test year and applied a reduction to its Other Customer Accounting expense of $33,308 in the test year to arrive at a forecasted expense level of $86,842.[60]

The Commission finds that Kentucky-American's adjustment to base its Other Customer Accounting expense on its 2024 level of expense and make adjustments for the anticipated decline in bank service charges produces a reasonable level of expense and is more indicative of Kentucky-American's cost trends than a CPI inflationary adjustment or applying Kentucky-American's O&M Growth Factor adjustment. For those reasons, the Commission finds that Kentucky-American's updated adjustment to its Other Customer Accounting expense, provided in response to discovery,[61] should be accepted as filed. Further, for the same reasons listed above, the Commission finds that Kentucky-American's original adjustment, to normalize the base period expense and apply its O&M Growth Factor Adjustment, should be rejected.

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[58] Application, Exhibit 37, Schedule D-2.

[59] Defever Direct Testimony at 27.

[60] Kentucky-American's Response to the Attorney General's First Request, Item 80.

[61] Kentucky-American's Response to the Attorney General's First Request, item 80.

Maintenance Supplies and Services Expense – Kentucky-American proposed an increase to its Maintenance Supplies and Services Expense of $265,741, to arrive at a test year Maintenance Supplies and Services expense of $2,991,634.[62] Kentucky-American stated that the adjustment is based on forecasted amortization schedules for Amortized Deferred Maintenance and additional contracted services due for safety mandates and preventative plans, in addition to applying its O&M Growth Factor adjustment.[63] As noted above, the Attorney General objected to Kentucky-American's O&M Growth Factor Adjustment.[64]

The Commission finds that Kentucky-American's application of the O&M Growth Factor adjustment, as well as its adjustment to account for Amortized Deferred Maintenance and additional contracted services for safety mandates and preventative plans, produces a reasonable forecasted expense while also being more indicative of Kentucky-American's cost trends than applying a CPI inflationary adjustment. For these reasons, the Commission finds that the adjustments made to Kentucky-American's forecasted Maintenance Supplies and Services expense should be accepted as filed.

Payroll Adjustments – Kentucky-American proposed $9,528,061 for its Payroll Expense and approximately $708,794 for related Payroll Tax Expense.[65] Kentucky-American stated that its labor expense was based on an assumed full-staffing level with reductions to its overtime, temporary employee, and contractor expenses, accordingly.[66]

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[62] Application, Exhibit 37, Schedule C-1.

[63] Application, Exhibit 37, Schedule D-2.

[64] Defever Direct Testimony at 27.

[65] Application, Exhibit 37, Schedule G-1.

[66] Kentucky-American's Brief at 7.

Kentucky-American identified 168 full-time employees as the appropriate staffing level for its operations.[67]

The Attorney General/LFUCG argued that it cannot be assumed that Kentucky-American will spend the amounts it budgets for payroll due to Kentucky-American consistently having had vacancy issues.[68] The Attorney General/LFUCG noted that Kentucky-American has averaged 5.5 vacancies during the period of 2020 through 2024,[69] and in that same time period, was under budget by an average of 6.05 percent.[70] The Attorney General/LFUCG calculated Kentucky-American's vacancies for the years 2020 through 2024 as 3.6 percent, and recommended not including the labor cost of unfilled positions in the revenue requirement by reducing Payroll Expense by 3.6 percent, or $610,390.[71] Alternatively, the Attorney General/LFUCG recommended that, if the Commission rejected its recommended reduction of 3.6 percent based on vacancies, then the Commission should reduce Kentucky-American's payroll expense by 6.5 percent based on Kentucky-American's historical record of overbudgeting.[72]

In its post-hearing brief, Kentucky-American stated that, for ratemaking purposes, Kentucky-American has historically forecasted its labor expense based on the salaries and wages owed to the number of employees required to complete its work, instead of forecasting how much potential overtime or contracted labor expenses may result from

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[67] Application, Exhibit 10, Direct Testimony of William A. Lewis (Lewis Direct Testimony) at 35.

[68] Defever Direct Testimony at 7.

[69] Defever Direct Testimony at 8.

[70] Defever Direct Testimony at 7.

[71] Defever Direct Testimony at 9.

[72] Defever Direct Testimony at 9.

an unknown number of vacant employee roles.[73] Further, Kentucky-American stated that it did not include increased expenses for overtime, temporary employees, or contractor expenses when calculating its forecasted labor expense.[74]

In response to post-hearing discovery, Kentucky-American stated that its current collective bargaining agreement (CBA) expired on October 31, 2025, and that negotiations for a new contract would begin on October 13, 2025.[75] In that response, Kentucky-American stated that the existence of a new contract in place as soon as the current contract expires is immaterial because the forecasted test period wages were projected using the most-recent increase from the current contract.[76] However, in a supplemental response to post-hearing discovery, Kentucky-American stated that negotiations with the union were successful and the union ratified a new CBA on November 19, 2025.[77] The Commission notes that Kentucky-American did not ask for the application or test year revenue requirement to be amended as a result of the successful negotiations with the union and the ratification of a new CBA. However, when the Commission reviewed the new CBA, the adjustment made to include the updated CBA terms and conditions would be greater than the amount that resulted from the originally forecasted wage increase for union workers to arrive at the forecasted test year amount. The Commission found that the updated CBA increased Kentucky-American's

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[73] Kentucky-American's Brief at 6.

[74] Kentucky-American's Brief at 7.

[75] Kentucky-American's Response to Staff's First Post-Hearing Request, Item 12.

[76] Kentucky-American's Response to Staff's First Post-Hearing Request, Item 12.

[77] Kentucky-American's Supplemental Response to Staff's First Post-Hearing Request (filed Nov. 26, 2025) , Item 12.

test year union wage increases by 0.25 percent from its originally filed position,[78] increased Kentucky-American's initial and subsequent meal allowances from $10 to $15,[79] increased Kentucky-American's Safety Shoe allowance from $159 to $250 plus applicable taxes,[80] and included a new $500 annual clothing credit, issued each January, for Kentucky-American's union employees.[81] Due to the timing of the filing of the updated CBA, as well as the fact that Kentucky-American did not request to update its revenue requirement based on the updated CBA, the Commission made no adjustments to Kentucky-American's payroll expenses to account for the updated CBA. The Commission further recognizes that, should Kentucky-American file another base rate case before the updated CBA expires, the Commission will recognize these adjustments as fair, just, and reasonable, as they constitute the binding contract between Kentucky-American and its partnered union.

The Commission finds that both adjustments proposed by the Attorney General/LFUCG are unreasonable and should be denied. The Commission has consistently found that unfilled positions be included as Kentucky-American is actively seeking to fill those positions. The vacancies are not an unreasonable amount, and the Attorney General/LFUCG's adjustment does not account for an increase in overtime,

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[78] (1) Kentucky-American's Supplemental Response to Staff's First Post-Hearing Request, Item 12, Attachment A at 11; (2) Kentucky-American's Supplemental Response to Staff's First Post-Hearing Request, Item 12, Attachment A at 15.

[79] Kentucky-American's Supplemental Response to Staff's First Post-Hearing Request, Item 12, Attachment A at 25.

[80] Kentucky-American's Supplemental Response to Staff's First Post-Hearing Request, Item 12, Attachment A at 23.

[81] Kentucky-American's Supplemental Response to Staff's First Post-Hearing Request, Item 12, Attachment A at 24.

contractor labor, or temporary employee labor to offset unfilled positions.[82] Kentucky-American filed information about the vacancies as well as the efforts to fill those positions and throughout the case updated current vacancy status.[83] The Commission notes that, while Kentucky-American's total payroll expenses are increasing in the test period, Kentucky-American has demonstrated a lower forecasted amount of overtime, contractor labor, and temporary employee labor expenses in the test period as a result of assuming a full staffing level. This bilateral adjustment to assume full staffing levels and reduce related expenses that would otherwise increase as staffing levels decrease follows prior Commission precedent, and the Commission finds Kentucky-American's forecasted level of Payroll Expense should be accepted.

Incentive Compensation – Kentucky-American's incentive compensation plan is composed of an Annual Performance Plan (APP), which all full-time employees participate in, and a Long-Term Performance Plan (LTPP), for which eligibility is limited to certain exempt employees.[84] Kentucky-American included $3,171,584 in the forecasted test period for its total incentive compensation plan.[85]

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[82] Case No. 2024-00092, *Electronic Application of Columbia Gas of Kentucky, Inc. for an Adjustment of Rates ; Approval of Depreciation Study; Approval of Tariff Revisions; and Other Relief* (Ky. PSC Dec. 30, 2024), Order at 30; Case No. 2024-00287, *Electronic Application of Big Sandy Rural Electric Cooperative Corporation for a General Adjustment of Rates* (Ky. PSC June 20, 2025), Order at 16; Case No. 2023-00191, (Ky. PSC May 3, 2024), Order at 15-16; Case No. 2018-00358, (Ky. PSC June 27, 2019), Order at 39-40.

[83] Kentucky-American's Response to Staff's First Post-Hearing Request, Item 10; Kentucky-American's Response to Staff's Fourth Request, Item 1; Kentucky-American's Response to Staff's Fourth Request, Item 2.

[84] Lewis Direct Testimony at 42.

[85] Kentucky-American's Response to the Attorney General First Request, Item 116.

The Attorney General/LFUCG recommended removing 50 percent of Kentucky-American's APP ($933,538) and 70 percent of Kentucky-American's LTPP ($913,156) that is driven by the financial performance of the company.[86] The Attorney General/LFUCG argued that the Commission has long-standing precedent of disallowing recovery of incentive compensation tied to financial goals, claiming that incentive compensation tied to fiscal measurements overwhelmingly benefit shareholders over customers, and customers should not bear the expense of those plans.[87]

Kentucky-American argued that the APP and LTPP benefit customers by enabling it to invest in its resources, both people and infrastructure, helping to ensure the efficient operation of the company, which, in turn, ultimately benefits its customers.[88] Kentucky-American further argued that, if its employees did not receive the portion of incentive compensation tied to the financial performance of Kentucky-American, they would receive compensation that is well below reasonable and competitive levels of market median total remuneration.[89]

While Kentucky-American contended that the total compensation of its employees, inclusive of its APP and LTPP, is market competitive, the Commission finds that the Attorney General/LFUCG's adjustment to remove incentive compensation based on financial performance metrics should be approved, consistent with Commission precedent. The Commission disallowed recovery of the cost of employee incentive

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[86] Defever Direct Testimony at 10.

[87] Case No. 2023-00191, (Ky. PSC May 3, 2024) Order at 17.

[88] Rebuttal Testimony of Robert Mustich (Mustich Rebuttal Testimony) at 4.

[89] Mustich Rebuttal Testimony at 6.

compensation plans tied to fiscal measurements in Case No. 2018-00358[90] and further reaffirmed that sentiment in Case No. 2023-00191.[91] In those cases the Commission explained financial performance measures do not benefit customers, and Kentucky-American's ratepayers should not bear the expense of those plans.[92] The evidence put forth in this case leads the Commission to a similar conclusion. The resulting revenue requirement impact is a reduction of $1,858,253. Further, the adjustments for Kentucky-American's Payroll Tax Expense flows through this adjustment to reduce the forecasted test year Payroll Tax Expense by $134,950, which would reduce the revenue requirement by $135,795.

Employee Stock Purchase Program – Kentucky-American stated that its employees have the option to participate in the Employee Stock Purchase Program (ESPP), in which they are able to purchase shares of American Water common stock at a 15 percent discount.[93] In this proceeding, Kentucky-American included the costs associated with the difference between the market price and the price paid by the employee through the ESPP in its revenue requirement, for a total increase of $61,961.[94]

The Attorney General/LFUCG, citing Case No. 2023-00191, argued that since ratepayers do not receive any benefits from this program, it is not reasonable for them to

[90] Case No. 2018-00358, *Electronic Application of Kentucky-American Water Company for an Adjustment of Rates*, (Ky PSC June 27, 2019) Order at 44.

[91] Case No. 2023-00191, (Ky. PSC May 3, 2024) Order at 17.

[92] Case No. 2023-00191, (Ky. PSC May 3, 2024) Order at 17.

[93] Prendergast Direct Testimony at 9.

[94] Kentucky-American's Response to the Attorney General's First Request, Item 92.

bear the costs associated with this program.[95] Kentucky-American stated that it included the ESPP discounts in the revenue requirement because it disagreed with the Commission's decision and basis for disallowance of ESPP Expense in its prior rate case.[96]

The Commission finds that Kentucky-American's ESPP Expense should be removed from the test year revenue requirement because it is unreasonable to recover this expense from ratepayers as they receive no benefit from the program, and Kentucky-American has not provided sufficient evidence to deviate from the Commission's prior Order in Kentucky-American's last base rate proceeding. Disagreement with the Commission is not sufficient evidence of a known and measurable change or a factual basis to support recovery from customers for this expense. This will reduce Kentucky-American's ESPP Expense by $61,961 with a corresponding reduction to Kentucky-American's revenue requirement $62,349.

<u>401(k) Contribution Expense</u> – Kentucky-American proposed an increase to its Other Benefits expense of $166,541 to arrive at a test year expense level of $811,569.[97] However, in response to discovery, Kentucky-American stated that it included $40,950 in retirement plan expense related to matching contributions made to employees' 401(k) retirement plans who are also participants in a defined benefit pension retirement plan for both its direct employees and expenses allocated from the service company.[98]

[95] Defever Direct Testimony at 14.

[96] Kentucky-American's Response to the Attorney General's Second Request, Item 30.

[97] Application, Exhibit 37, Schedule C-1.

[98] Kentucky-American's Response to the Attorney General's First Request, Item 96.

The Attorney General/LFUCG recommended reducing Kentucky-American's 401(k) expense by $40,950 based on precedent in which the Commission denied recovery of retirement expenses in which a utility made contributions to both a defined benefit pension plan and a 401(k) plan.[99] In Case No. 2018-00358, the Commission noted that permitting utility employees to participate in multiple pension plans simultaneously while many ratepayers have no pension plan at all, is not fair, just or reasonable.[100]

Kentucky-American disagreed with the Attorney General/LFUCG's characterization of this expense as duplicative, noting that the expense should be viewed as a cost associated with the pension's wind-down because it is representative of transitioning American Water's employees from Kentucky-American's locked pension to the 401(k) that now serves as Kentucky-American's standard retirement benefit.[101] In rebuttal, Kentucky-American claimed that only $30,815 of the total amount of expense in the test year is for employees enrolled in a non-frozen benefit plan.[102] Kentucky-American stated that, throughout the past two decades, it has modified retirement benefits to control costs, including closing the defined benefit plan to new hires in 2006, and eliminating the availability of retiree medical benefits for non-collective bargaining unit new hires in 2002 and collective bargaining unit new hires in 2006.[103]

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[99] Defever Direct Testimony at 23.

[100] Case No. 2018-00358, (Ky. PSC June 27, 2019), Order at 46.

[101] Rebuttal Testimony of Robert Prendergast (Prendergast Rebuttal Testimony) at 6.

[102] Prendergast Rebuttal Testimony at 7.

[103] Prendergast Rebuttal Testimony at 7.

The Commission finds that the test year level of Kentucky-American's 401(k) Expense should be reduced by $40,950 to reflect 401(k) matching contributions made by Kentucky-American to its employees who are also eligible for the defined benefit pension program and has not had their benefit frozen. As the Commission has stated previously, allowing recovery for two separate retirement plans is not reasonable. This adjustment reduces Kentucky-American's base revenue requirement by $41,206.

Healthcare Expense – Kentucky-American forecasted its Healthcare Expense for the test year by determining its cost share through collective bargaining with its unionized workforce.[104] Kentucky-American argued that these agreements are legally binding, are negotiated every five years, and cannot be unilaterally changed by Kentucky-American.[105] Further, Kentucky-American stated that it applies the same contribution cost share levels to its non-union employees.[106]

The Attorney General/LFUCG proposed reducing Kentucky-American's forecasted test year healthcare expense by $315,000 to remove the costs of healthcare above the most current United States Bureau of Labor Statistics' (BLS) averages for single and family coverage.[107] Citing Case No. 2021-00407, the Attorney General/LFUCG argued that applying the BLS average to a utility's healthcare expenses in the test year helps mitigate benefit expenses.[108]

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[104] Kentucky-American's Response to the Attorney General's First Request, Item 41.

[105] Kentucky-American's Response to the Attorney General's First Request, Item 41.

[106] Prendergast Rebuttal Testimony at 16.

[107] Defever Direct Testimony at 27.

[108] Defever Direct Testimony at 27.

In response, Kentucky-American explained that, although it factors in BLS and other benchmarking data, its employee verses employer cost share is negotiated through its union contract, with non-union benefits matching the contract.[109] The Commission finds that Kentucky-American's Healthcare Expense should be accepted as filed, as the amounts are known and measurable. The expense is negotiated as part of a collective bargaining agreement, and the Commission has consistently allowed for the utility to recover for the full amount of an arms length negotiated agreement with its employee union.

Rate Case Expense – Kentucky-American proposed a two-year amortization period for estimated rate case expense of $1,218,404, for a test year expense of $609,202.[110] In addition to the amortization of rate case expense for this proceeding (2025 Rate Case Expense), Kentucky-American also included $332,246 in rate case expense in the test year to reflect the unamortized balance from Kentucky-American's most recent general rate case, Case No. 2023-00191, (2023 Rate Case Expense) for a total test year rate case expense of $941,449.[111]

The Attorney General/LFUCG argued that Kentucky-American was expected to amortize the balance of $996,740 for 2023 Rate Case Expense over three years and, since Kentucky-American filed for an adjustment of rates in only two years, it is requesting the remaining amount in the forecasted test period.[112] Further, the Attorney

[109] Kentucky-American's Response to the Attorney General's First Request, No. 41

[110] Application, Exhibit 37, Schedule D-2 at 5.

[111] Kentucky-American's Response to Staff's First Request, Item 1, KAWC 2025 Rate Case – Regulatory Expense Exhibit (W/P 3-6).

[112] Defever Direct Testimony at 19.

General/LFUCG argued that, if the full amount of $332,246 is not amortized over an additional three years, then the full amount will be collected every year until Kentucky-American's next rate case and Kentucky-American will begin over-collecting in the second year.[113]

Kentucky-American argued that the extension of the amortization for the 2023 Rate Case Expense would not align with the approved amortization period in that case.[114] Further, in justifying a two-year amortization period for the 2025 Rate Case Expense, Kentucky-American argued that the timing between its last rate case and its current rate case does not align with the three-year amortization period normally utilized by the Commission in its Orders.[115]

The Commission finds that the Attorney General/LFUCG's recommendation to amortize the remaining 2023 Rate Case Expense for an additional three years is reasonable and should be accepted because, if the full unamortized balance of Kentucky-American's 2023 Rate Case Expenses is recovered in the test year, then Kentucky-American would be authorized to recover that amount each year until its next base rate case, and would ultimately begin over-collecting it's 2023 Rate Case Expense from its customers.

Further, the Commission finds that Kentucky-American's 2025 Rate Case Expense should be reduced to $713,791. Following the evidentiary hearing, Kentucky-American provided an update to its 2025 Rate Case Expense, which the utility calculated

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[113] Defever Direct Testimony at 20.

[114] Degrazia Rebuttal Testimony at 5.

[115] Degrazia Rebuttal Testimony at 5.

as $813,240, and provided the accompanying invoices.[116] The Commission notes that the total of the accompanying invoices was $99,449 less than Kentucky-American's calculated total, with the largest discrepancies relating to Rate of Return and Support Services Study consulting services and Miscellaneous expenses. The Commission finds only the expenses with supporting invoices reasonable for recovery. Undocumented expense cannot be examined for reasonableness and prudency.

Finally, the Commission finds that the Attorney General/LFUCG's recommendation to amortize the 2025 Rate Case Expense over three years should be accepted as the time period reflects the time period normally between general rate adjustment applications.

The total effect of the Commission's adjustments is a reduction of $592,770 to Rate Case Expense and a reduction of $596,480 to Kentucky-American's revenue requirement.

<u>Business Development, Government Affairs, and Regulatory Policy Expense</u> – Kentucky-American included $615,734 in its forecasted test year for its Business Development, Government Affairs, Regulatory Policy, and Lobbying Expenses, of which $213,516 is attributed to Kentucky-American's shared services that its service company provides.[117]

In this proceeding, the Attorney General/LFUCG argued that, in Kentucky-American's last rate case, the Commission disallowed the shared services business development expenses finding the shared service business development expenses were

[116] Kentucky-American's Supplemental Response to Attorney General's Second Request (filed Oct. 27, 2025), Item 16.

[117] Kentucky-American's Response to Attorney General's First Request Item 56.

not specifically justified, and allocated business development expenses are not specific to Kentucky-American's development efforts.[118] The Attorney General/LFUCG recommended disallowing the shared services portion of Kentucky-American's business development expenses as it follows prior Commission precedent.[119]

In its post-hearing brief, Kentucky-American asserted that it has specifically explained the composition and value of these costs, reiterating that there are direct and indirect benefits that customers receive as a result of the service company's business development activities.[120] Further, Kentucky-American explained that its service company business development activities allow for: (1) mitigation of the costs to be recovered per customer; (2) enhanced purchasing power; (3) the spurring of activities that contribute to local economies; and (4) allowing American Water and Kentucky-American to acquire new water and wastewater utilities and leverage economies of scale to make operational improvements.[121]

After reviewing the record, the Commission finds that the allocated portion of Kentucky-American's business development expenses should be disallowed for recovery. As with the Commission's previous decisions concerning business development costs, here the Commission determined that external affairs and public policy costs enhance shareholder value but do not benefit ratepayers. Therefore, the Commission finds that those costs are not reasonable and should not be borne by

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[118] Case No. 2023-00191, (Ky. PSC May 3, 2024), final Order at 22.

[119] Defever Direct Testimony at 22.

[120] Kentucky-American's Brief at 27.

[121] Kentucky-American's Brief at 27.

ratepayers. As such, the Commission finds that Kentucky-American's business development expenses should be reduced by $213,516 for an overall reduction to the revenue requirement of $214,852.

Membership Dues Expense – In response to a request for information from the Attorney General/LFUCG, Kentucky-American provided its Membership Dues Expense historical actuals from 2020 through May 2025 year-to-date.[122] Since Kentucky-American does not forecast its Membership Dues Expense at a detail vendor level,[123] the Attorney General/LFUCG used Kentucky-American's 2024 Membership Dues Expense to reflect its recommended adjustment to remove the costs associated with lobbying, advocacy, attempts to influence public opinion, and institutional or image building advertising.[124]

In its review of Kentucky-American's historical Membership Dues Expense, the Attorney General/LFUCG noted that, out of the 17 organizations listed for 2024, 14 engaged in lobbying and image building.[125] The Attorney General/LFUCG argued that lobbying and image building costs should be below the line, and not paid for by Kentucky-American's ratepayers.[126] Further, the Attorney General/LFUCG argued many of the organizations listed were chambers of commerce, which provide very little benefit to ratepayers.[127] In addition, the Attorney General noted that the Commission has repeatedly ruled that the utility has the burden of proof to establish that costs it seeks to

[122] Kentucky-American's Response to Attorney General's First Request, Item 89.

[123] Kentucky-American's Response to Attorney General's First Request, Item 89.

[124] Defever Direct Testimony at 29.

[125] Defever Direct Testimony at 30.

[126] Defever Direct Testimony at 31.

[127] Defever Direct Testimony at 31.

recover in rates for dues paid to various associations do not include prohibited costs for lobbying and political activity.[128]

In response to requests for information, Kentucky-American argued it provided a detailed breakdown of the lobbying activity of the respective organizations.[129] In this breakdown, Kentucky-American extracted the total membership dues paid to each organization and total lobbying expenses paid by such organization and calculated the percentage of lobbying expenditures by dividing reported lobbying expenses by total overall membership dues received from all members.[130] These percentages were averaged, resulting in a composite lobbying factor of 17.3 percent, which was applied to Kentucky-American's 2024 level of Membership Dues Expense to remove $7,154 from the forecasted test period.[131]

After reviewing the record, the Commission finds that dues paid to organizations who participate in lobbying and image building are not reasonable to be recovered from

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[128] Defever Direct Testimony at 31, citing to Case No. 2024-00276, *Electronic Application of Atmos Energy Corporation for an Adjustment of Rates*; *Approval of Tariff Revisions; and Other General Relief* (Ky. PSC Aug. 11, 2025), final Order at 26–27; Case No. 2021-00214, *Electronic Application of Atmos Energy Corporation for an Adjustment of Rates* (Ky. PSC May 19, 2022), final Order at 23–25; Case No. 2021-00185, *Electronic Application of Delta Natural Gas Company, Inc. for an Adjustment of Its Rates and a Certificate of Public Convenience and Necessity* (Ky. PSC Jan. 3, 2022), final Order at 8–9; Case No. 2020-00350, *Electronic Application of Louisville Gas and Electric Company for an Adjustment of Its Electric and Gas Rates, a Certificate of Public Convenience and Necessity to Deploy Advanced Metering Infrastructure, Approval of Certain Regulatory and Accounting Treatments, and Establishment of a One-Year Surcredit* (Ky. PSC June 30, 2021), final Order at 27–31; Case No. 2020-00349, *Electronic Application of Kentucky Utilities Company for an Adjustment of its Electric Rates, a Certificate of Public Convenience and Necessity to Deploy Advanced Metering Infrastructure, Approval of Certain Regulatory and Accounting Treatments, and Establishment of a One-Year Surcredit* (Ky. PSC June 30, 2021), final Order at 25–28; Case No. 2021-00183, *Electronic Application of Columbia Gas of Kentucky, Inc. for an Adjustment of Rates; Approval of Depreciation Study; Approval of Tariff Revisions; Issuance of a Certificate of Public Convenience and Necessity; and Other Relief* (Ky. PSC Dec. 28, 2021), final Order at 9–10.

[129] Kentucky-American's Response to Staff's Fourth Request, Item 3.

[130] Kentucky-American's Response to Staff's Fourth Request, Item 3.

[131] Kentucky-American's Response to Staff's Fourth Request, Item 3.

ratepayers. The Commission finds that the Attorney General/LFUCG's adjustment to remove the amount that Kentucky-American spent in 2024 for the 14 organizations that included costs for lobbying and image building is reasonable. This adjustment, in totality, will reduce Kentucky-American's forecasted Membership Dues Expense by $41,178 and will reduce Kentucky-American's revenue requirement by $41,436.

Unaccounted-For Water Loss Expenses – The expense to produce water includes the Purchased Water Expense, Chemical Expense, Fuel and Power Expense and Waste Disposal Expense. Kentucky-American proposed a forecasted Chemicals Expense of $4,632,446, forecasted Purchased Water Expense of $201,875, forecasted Fuel and Power Expenses of $6,040,520 and forecasted Waste Disposal Expense of $714,836 in its test year,[132] with no adjustment to reduce each expense in accordance with 807 KAR 5:066, Section 6(3).[133] For purposes of recovery in rates, a utility may not recover more than 15 percent of its unaccounted for water loss expense.

The Attorney General/LFUCG argued that Kentucky-American's unaccounted-for water loss expenses should be reduced for purposes of recovery in rates.[134] The Attorney General/LFUCG calculated an unaccounted-for water loss percentage of 18.40 percent, claiming that this percentage was calculated in the same manner as the Commission's adjustment in Kentucky-American's last base rate proceeding, Case No. 2023-00191.[135] This adjustment would reduce Kentucky-American's forecasted Chemicals Expense,

[132] Application, Exhibit 37, Schedule C-1.

[133] 807 KAR 5:066.

[134] Defever Direct Testimony at 17.

[135] Defever Direct Testimony at 17.

Purchased Water Expense, Fuel and Power Expense, and Waste Disposal Expense by a total of $394,049, which would reduce Kentucky-American's base revenue requirement by $396,515.[136]

Attorney General's Proposed Reduction to Account for Unaccounted-for Water Loss in Excess of Fifteen Percent

Total Water Loss	Purchased Water	Fuel and Power	Chemicals	Waste Disposal	Total
Pro Forma Purchases	$ 201,875	$ 6,040,520	$ 4,632,446	$ 714,836	$ 11,589,677
Water Loss Percent	18.4000%	18.4000%	18.4000%	18.4000%	18.4000%
Total Water Loss	$ 37,145	$ 1,111,456	$ 852,370	$ 131,530	$ 2,132,501

Disallowed Water Loss	Purchased Water	Fuel and Power	Chemicals	Waste Disposal	Total
Pro Forma Purchases	$ 201,875	$ 6,040,520	$ 4,632,446	$ 714,836	$ 10,874,841
Water Loss in Excess of 15%	3.4000%	3.4000%	3.4000%	3.4000%	3.4000%
Disallowed Water Loss	$ 6,864	$ 205,378	$ 157,503	$ 24,304	$ 394,049

In its rebuttal testimony, Kentucky-American argued that the Attorney General/LFUCG inadvertently calculated a non-revenue water percentage, as opposed to the unaccounted-for water loss percentage, which is the basis for making the adjustment to expenses to reflect water loss in excess of 15 percent.[137] Further, Kentucky-American calculated a nine-year average variance between its non-revenue water and unaccounted-for water loss percentages, and argued that an unaccounted-for water loss percentage of 17.24 is reasonable.[138] Utilizing this adjustment would reduce Kentucky-American's Chemicals Expense, Purchased Water Expense, Fuel and Power Expense, and Waste Disposal Expense by 2.24 percent, for a total reduction of $252,471.[139]

[136] Defever Direct Testimony at 17.

[137] Lewis Rebuttal Testimony at 16.

[138] Lewis Rebuttal Testimony at 17, Table 2.

[139] Prendergast Rebuttal Testimony at 10.

Having reviewed the workpapers and arguments, the Commission finds that an adjustment for expenses in excess of the 15 percent threshold for recovery should be made. However, in reviewing the calculations, the Commission notes that the Attorney General/LFUCG calculated Kentucky-American's non-revenue water percentage, as opposed to its unaccounted-for water loss percentage. The Commission notes that the non-revenue water percentage methodology is consistent with the final Order in Case No. 2023-00191, but it was not correct, although not a subject of the rehearing. As such, the Commission does not agree with implementing an adjustment based upon the non-revenue water percentage methodology. Further, the Commission is not persuaded by Kentucky-American's utilization of a nine-year average variance between its non-revenue water percentage and its unaccounted-for water loss percentage, which is not indicative of Kentucky-American's current water loss issues. The Commission finds that Kentucky-American's adjustment to reduce its Chemicals Expense, Purchased Water Expense, Fuel and Power Expense, and Waste Disposal Expense by 2.24 percent should be rejected. The methodology used to calculate an alternative level of unaccounted-for water loss is not reflective of Kentucky-American's current water loss issues.

In response to a post-hearing request for information, Kentucky-American provided its monthly unaccounted for water loss reports from August 2024 through August 2025.[140] The Commission used these water loss reports to calculate an alternative level of unaccounted-for water loss for Kentucky-American. As shown in the table below, the 12-month average of Kentucky-American's unaccounted-for water loss for the period of

[140] Kentucky-American's Response to Staff's Third Post-Hearing Request, Item 2.

September 2024 through August 2025 resulted in an unaccounted-for water loss percentage of 17.60 percent.

Kentucky American Water Unaccounted-for Water Loss by Month
From September 2024 Through August 2025

Year	Month	Percentage
2024	September	2.66%
2024	October	13.65%
2024	November	7.83%
2024	December	31.97%
2025	January	21.35%
2025	February	8.00%
2025	March	24.65%
2025	April	30.35%
2025	May	13.39%
2025	June	23.46%
2025	July	18.86%
2025	August	15.03%
Unaccounted-for Water Loss for Base Period		17.60%
	Amount Over 15%	2.60%

The Commission finds that the most reasonable unaccounted-for water loss percentage for Kentucky-American is 17.60 percent, as this amount is more reflective of Kentucky-American’s current water loss experience than utilizing a nine-year variance. Additionally, the percentage is supported by the most recent known and measurable information. The Commission further finds that, pursuant to Section 6 of 807 KAR 5:066, an adjustment to remove 2.60 percent from Kentucky-American’s unaccounted-for water loss expenses should be made, which equates to $293,047 and will reduce Kentucky-American’s base revenue requirement by $294,881. The adjustments to each expense included in the Commission’s unaccounted-for water loss expense calculation are discussed below.

Commission Approved Reduction to Account for Unaccounted-for Water Loss in Excess of Fifteen Percent

Total Water Loss	Purchased Water	Fuel and Power	Chemicals	Waste Disposal	Total
Pro Forma Purchases	$ 201,875	$ 5,721,873	$ 4,632,446	$ 714,836	$ 11,271,030
Water Loss Percent	17.6000%	17.6000%	17.6000%	17.6000%	17.6000%
Total Water Loss	$ 35,530	$ 1,007,050	$ 815,310		$ 1,857,890

Disallowed Water Loss	Purchased Water	Fuel and Power	Chemicals	Waste Disposal	Total
Pro Forma Purchases	$ 201,875	$ 5,721,873	$ 4,632,446	$ 714,836	$ 11,271,030
Water Loss in Excess of 15%	2.6000%	2.6000%	2.6000%	2.6000%	2.6000%
Disallowed Water Loss	$ 5,249	$ 148,769	$ 120,444	$ 18,586	$ 293,047

Chemicals Expense – As previously stated, Kentucky-American proposed a forecasted Chemicals Expense $4,632,446 in its test year.[141] In response to discovery, Kentucky-American stated that it did not reflect any reductions to its Chemicals Expense to account for having unaccounted-for water loss because that methodology was consistent with its previous rate case filings.[142]

The Commission finds that the most reasonable unaccounted-for water loss percentage for Kentucky-American is 17.60 percent, as calculated using the 12-month average of Kentucky-American's monthly unaccounted-for water loss reports for the period September 2024 through August 2025. As such, the Commission finds that Kentucky-American's forecasted Chemicals Expense should be reduced by 2.60 percent. This adjustment reflects a reduction to Kentucky-American's Chemicals Expense of $120,444 and will reduce Kentucky-American's base revenue requirement by $121,197.

[141] Application, Exhibit 37, Schedule C-1.

[142] Kentucky American's Response to the Attorney General's First Request, Item 173.

Purchased Water Expense – As stated previously, Kentucky-American forecasted a Purchased Water Expense of $201,875 in its test year,[143] with no reduction to account for having unaccounted-for water loss in excess of 15 percent.

Based on the Commission's above calculation of unaccounted-for water loss percentage of 17.60 percent, the adjustment to remove 2.60 percent from Kentucky-American's proposed Purchased Water Expense will reduce the expense by $5,249 and will reduce Kentucky-American's base revenue requirement by $5,282.

Fuel and Power Expense – As stated previously, Kentucky-American forecasted a Fuel and Power Expense of $6,040,520 in its test year,[144] with no reduction to account for having unaccounted-for water loss in excess of 15 percent. However, in response to discovery, Kentucky-American stated that it had erroneously applied an adjustment to both the base period and the forecasted test year to account for Kentucky Utilities' pending rate increase in the amount of 6.5 percent.[145] Kentucky-American further stated that the cumulative impact of the correction to only apply the 6.5 percent increase to the forecasted test year resulted in a reduction to its Fuel and Power expense by $318,647, to arrive at a forecasted test year expense level of $5,721,873.[146]

The Commission finds that the adjustment to remove the 6.5 percent escalation factor from the base period should be approved, as Kentucky Utilities' pending rate increase was not approved at any point during Kentucky-American's base period.

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[143] Application, Exhibit 37, Schedule C-1.

[144] Application, Exhibit 37, Schedule C-1.

[145] Kentucky-American's Response to the Attorney General's Second Request, Item 55.

[146] Kentucky-American's Response to the Attorney General's Second Request, Item 55.

Additionally, based on the Commission's above calculation of unaccounted-for water loss percentage of 17.60 percent, the adjustment to remove 2.60 percent from Kentucky-American's proposed Fuel and Power Expense should be made, which will reduce the Fuel and Power Expense by $148,769 and will reduce Kentucky-American's base revenue requirement by $149,700.

Waste Disposal Expense – As stated previously, Kentucky-American forecasted a Waste Disposal Expense of $714,836, with no reduction to account for having unaccounted-for water loss in excess of 15 percent.

Based on the Commission's above calculation of unaccounted-for water loss percentage of 17.60 percent, the adjustment to remove 2.60 percent from Kentucky-American's proposed Waste Disposal Expense will reduce the Waste Disposal Expense by $18,586 and will reduce Kentucky-American's base revenue requirement by $18,702.

Income Tax Expense – Kentucky-American proposed a state income tax expense of $478,685 and a federal income tax expense of $2,545,779 in its forecasted test year.[147] The total effect of the Commission's adjustments to Kentucky-American's proposed Operations and Maintenance Expenses is a $3,362,000 reduction to Kentucky-American's Operations and Maintenance Expenses.[148]

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[147] Application, Exhibit 37, Schedule C-1.

[148] As discussed above, the Commission made adjustments to the following expense categories that affect the calculation of income tax: Incentive Compensation; Employee Stock Purchase Plan Discount; Unaccounted-For Water; Rate Case Expense; Business Development Expense; 401(k) Expense; Growth Factor; Membership Dues; and Payroll Tax.

Commission Operating Income Adjustments

Description		Forecasted Test Period
Updated Operating Income per Kentucky-American	$	32,700,367
Adjustments:		
Incentive Compensation	$	(1,846,694)
Employee Stock Purchase Plan Discount	$	(61,961)
Unaccounted For Water	$	(293,047)
Rate Case Expense	$	(592,770)
Business Development Expense	$	(213,516)
401(k) Expense	$	(40,950)
Growth Factor	$	(136,934)
Membership Dues	$	(41,178)
Payroll Tax	$	(134,950)
Subtotal: Operating Income Adjustments	$	(3,362,000)

As a result of reducing Kentucky-American's Operations and Maintenance Expenses, Kentucky-American's operating income, and, in turn, its income taxes, increase. The Commission finds that, after the reduction to Kentucky-American's Operations and Maintenance Expenses, Kentucky-American's proposed federal income tax expense will increase by $670,719, and Kentucky-American's proposed state income tax expense will increase by $168,100, for a total increase of $838,819 to Kentucky-American's Income Tax expense.

Interest Synchronization Expense – Kentucky-American proposed a forecasted Interest Synchronization Expense of $15,103,004 based on the forecasted capital structure, the weighted cost of debt and the weighted dividend rate on the preferred stock.[149] As shown in the table below, the Commission has recalculated this expense to be $14,940,662 based on the rate base and weighted cost rates found reasonable herein

[149] Application, Exhibit 37, Schedule E-1.3.

resulting in a reduction of $162,342 to Kentucky-American's Interest Synchronization Expense.

	Weighted Cost of Debt	Rate Base	Interest Synchronization
Short-Term Debt	0.05%	$ 666,993,852	$ 333,497
Long-Term Debt	2.16%	$ 666,993,852	$ 14,407,067
Preferred Stock	0.03%	$ 666,993,852	$ 200,098
Interest Synchronization			$ 14,940,662

Rate Base

Advanced Metering Infrastructure (AMI)

Kentucky-American proposed capital expenditures for meter replacements of $10,538,425 for the forecasted test period.[150] Kentucky-American has a pending application for a Certificate of Public Convenience and Necessity (CPCN) in Case No. 2024-00240[151] requesting to implement AMI. The Attorney General/LFUCG argued that it is not clear from the record that any of the AMI capital expenditures are included in the forecasted test period meter replacement expense and requested that no AMI expense be included in the forecast period unless the Commission grants the CPCN.[152]

In response to Commission Staff's Fourth Request, Kentucky-American stated that the capital expenditures presented in this Application are not affected by the metering technology implementation.[153] Kentucky-American further stated it does not anticipate

[150] Kentucky American's Response to the Attorney General's Second Request, Item 73.

[151] Case No. 2024-00240, *Electronic Application of Kentucky-American Water Company for a Certificate of Public Convenience and Necessity for Installation of Advanced Metering Infrastructure*, Application (filed June 11, 2025).

[152] Attorney General's Brief at 28.

[153] Kentucky-American's Response to Commission Staff's Fourth Request, Item 7.

material changes to capital expenditures in the base or forecasted test periods if it receives approval to implement AMI technology instead of automated meter reading Automated Meter Reading (AMR) technology.[154]

The Commission finds that the capital expenditures for meter replacements of $10,538,425 for the forecasted test period filed in Kentucky-American's application is reasonable given the responses from Kentucky-American. The Commission cautions Kentucky-American to be mindful of expending funds for projects not yet approved by the Commission. However, the Commission recognizes that using newer meter technology replacements when a meter has reached the ends of its useful life may be necessary and reasonable.

Qualified Infrastructure Program (QIP)

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.[155] The Commission approved the implementation of the QIP Rider finding that smaller, more gradual rate increases are reasonable, opposed to shock from large increases due to rate recovery for several years of capital investment to replace aging infrastructure was reasonable.[156] With the approval of the QIP Rider, the Commission established a filing schedule, calculation methodology, and filing contents. These requirements stated that QIP applications were to be filed on an annual basis on or before April 2, have a 90-day review period that can be extended for good

[154] Kentucky-American's Response to Commission Staff's Fourth Request, Item 7.

[155] Case No. 2018-00358, (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.

[156] Case No. 2018-00358 (Ky. PSC June 27, 2019), Order at 81.

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.[157] However, in Case No. 2023-00300, at Kentucky-American's request, the QIP filing schedule was changed to a calendar year, as shown below, pursuant to Kentucky-American's assertion it would be more beneficial.[158]

Filing	Filing Date	QIP Period Start / Rates Effective	QIP Period End	Balancing Adjustment
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.

In this rate case, Kentucky-American requested to roll its QIP into base rates and reset the QIP rider to zero.[159] Kentucky-American requested to include all QIP eligible projects in the forecasted test period revenue requirement, instead of flowing these eligible projects through the QIP rider.[160]

The Attorney General/LFUCG recommended denying Kentucky-American's request to roll its QIP into base rates and reset the QIP charge to zero.[161] The Attorney General repeated the Commission's statement in the final Order for Case No. 2023-00191 about the QIP charge that having "a separate line item on customer bills allows for

[157] Case No. 2018-00358, (Ky. PSC June 27, 2019), Order at 84.

[158] Case No. 2023-00300, *Electronic Application of Kentucky-American Water Company for a Balancing Adjustment for its QIP Charge* (Ky. PSC Aug. 12, 2024), Order at 6.

[159] Degrazia Direct Testimony at 9, 20-21.

[160] Direct Testimony of Robert Burton at 4-5; Degrazia Direct Testimony at 20.

[161] Defever Direct Testimony at 36-38.

transparency."[162] The Attorney General went on to argue that by requiring the QIP charge to be on a separate line item on the customers' bills, it not only allows for greater transparency to the customers, but it also acts as an incentive for the Company to control QIP costs in order to maintain a reasonable charge.[163] The Attorney General's second argument is that embedding the QIP eligible projects in the forecasted test period revenue requirement in the pending case will provide less transparency to the customers and create more confusion.[164] The Attorney General was unable to provide a monetary adjustment to remove the QIP eligible projects from the forecast test period.[165]

When Kentucky-American proposed the QIP, the utility argued that, among other benefits, it would reduce regulatory costs, while increasing rates on a more gradual basis than a general rate case and providing regulatory certainty that attracts debt and equity capital at reasonable costs, all of which lower the rate impact on customers.[166]

As of its 2023 rate case, Kentucky-American made a clear designation between its QIP eligible projects and the other capital investments it included in its revenue requirement. However, Kentucky-American has filed two rate cases since January 2023. Kentucky-American did not designate any QIP projects for its QIP 7 filing.[167] Due to the timing of the QIP filings, as illustrated in the chart above, this will result in the QIP not

[162] Attorney General's Brief at 29.

[163] Attorney General's Brief at 29.

[164] Attorney General's Brief at 30.

[165] Attorney General's Brief at 30. The Attorney General stated it was unable to quantify a recommended monetary adjustment for these proposals because they did not exist in the record at the time of his expert witness's testimony filing.

[166] Case No. 2018-00358, (Ky. PSC June 27, 2019) final Order at 74-75.

[167] HVT of the September 23, 2025 Hearing, Robert Burton at 09:23:57-09:24:32.

being utilized for the entire calendar year of 2026. As seen in this proceeding, Kentucky-American has chosen instead to request recovery for its QIP eligible projects in the forecasted test period revenue requirement.[168] When granting the QIP mechanism to Kentucky-American, the Commission noted that it should lower regulatory lag and allow for a timelier recovery of capital investments.[169] However, Kentucky-American's inclusion of its QIP eligible projects in its rate case appears to be effectively allowing recovery at the same rate of recovery, negating the purpose of the QIP.

Based on the evidence in this case, the Commission finds the QIP program no longer serves Kentucky-American's initial intended purpose of facilitating recovery for the approved capital expenditures while reducing the frequency of rate cases.[170] The timing of Kentucky-American's rate cases and the failure to include any new projects for 2026 in the QIP charge supports termination of the QIP rider. As noted by the Commission when the QIP rider was established, the same statutory authority[171] that permits the Commission to authorize a QIP also grants the authority to terminate or limit the QIP.[172] The Commission finds that, given the frequency of rate cases, as well as Kentucky-

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[168] Burton Direct Testimony at 4-5; Degrazia Direct Testimony at 20; HVT of the September 23, 2025 Hearing, Robert Burton at 09:23:57-09:24:32.

[169] Case No. 2018-00358, (Ky. PSC June 27, 2019), final Order at 65.

[170] Case No. 2018-00358, (Ky. PSC June 27, 2019), final Order at 74-75.

[171] Case No. 2018-00358, (Ky. PSC June 27, 2019), final Order at 80. The Commission discussed its authority to establish the QIP rider, and stated "It is well established that KRS 278.030 and KRS 278.040 expressly grant the Commission plenary ratemaking authority to regulate and investigate utilities and to establish fair, just, and reasonable rates. In the absence of any statute that requires a particular procedure to determine whether rates are fair, just, and reasonable, the Commission has the authority to consider and decide ratemaking issues such as the infrastructure replacement surcharge proposed by Kentucky-American."

[172] Case No. 2018-00358, (Ky. PSC June 27, 2019), final Order at 82; Case No. 2023-00191, (Ky. PSC May 3, 2024), final Order at 53, citing *Public Serv. Comm'n v. Commonwealth ex. Rel. Jack Conway, 324 S.W .3d 373, 383* (Ky. 2010).

American's failure to utilize the QIP rider consistently, the QIP mechanism should be terminated effective December 31, 2025. The Commission finds that Kentucky-American's request to roll QIP into base rates and reset the QIP rider to zero is approved given that the QIP rider is being terminated. Kentucky-American may file a request for a new rider mechanism at some point in the future for the intended purpose and use.

Cash Working Capital (CWC)

In its application, Kentucky-American included $2,788,000 in CWC for the forecasted test year based upon a lead/lag study with an average day interval between date expenses are incurred and date of payment of 32.87 days.[173] Kentucky-American's base period update included $2,772,000 in CWC for the forecasted test year based upon the updated lead/lag study an average day interval between date expenses are incurred and date of payment of 32.89 days.[174]

The Attorney General/LFUCG argued Kentucky-American's lead/lag study does not comply with long-standing Commission precedent[175] to exclude all noncash items and balance sheet adjustments.[176] The Attorney General/LFUCG cited the final Order in Case No. 2021-00183, where the Commission stated that it, "places Columbia Kentucky and all other utilities on notice that in any future rate cases, a lead/lag study is to be performed

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[173] Application, Exhibit 37, Schedule B 5.2.

[174] Base Period Update, Exhibit 37, Schedule B 5.2.

[175] Case No. 2024-00276, *Electronic Application of Atmos Energy Corporation for an Adjustment of Rates; Approval of Tariff Revisions; and Other General Relief* (Ky. PSC Aug. 11, 2025), final Order at 19; 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, 2024), final Order at 9; Case No. 2021-00214, *Electronic Application of Atmos Energy Corporation for an Adjustment of Rates* (Ky. PSC May 19, 2022), final Order at 20.

[176] Defever Direct Testimony at 39.

and shall exclude noncash items and balance sheet adjustment."[177] The second argument that Attorney General/LFUCG made is that Kentucky-American included negative 4.2 lag days for Service Company charges and that those lag days should be set to the same amount as other outside providers – after the services have been provided.[178] The Attorney General/LFUCG points to the final Order in Case No. 2023-00191, where the Commission stated that Kentucky-American, "has not provided any reasoning for service company expenses to be collected in revenues from customers and paid before the actual service is performed. The Commission finds that the Attorney General/LFUCG's adjustment to CWC included in rate base is reasonable and should be accepted."[179] The impact of the Attorney General/LFUCG's adjustments to CWC are a $8.223 million CWC reduction, which is a reduction of $11.011 million to the Kentucky-American's request of $2.788 million. This recommendation results in a reduction to the revenue requirement of $1.063 million after the gross up.[180]

The Commission agrees with both of the Attorney General/LFUCG's proposed adjustments to CWC however the Commission made additional adjustments to expenses mentioned in this order. The Commission has historically disallowed the inclusion of non-cash items from the lead/lag study. The Commission also disallowed the inclusion of negative lag days for Kentucky-American's service company in its last rate case because customers should not pay for services before actual services have been performed. The

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[177] Defever Direct Testimony at 39.

[178] Defever Direct Testimony at 40-42.

[179] Defever Direct Testimony at 41.

[180] Defever Direct Testimony at 42.

Commission calculated its own CWC, which it finds reasonable here, using Kentucky-American's base period update, lead lag study and expense adjustments discussed in this order. The adjustment to rate base for removing non-cash items[181] and setting Kentucky-American's Service Company lag days[182] to the same amount as other outside contracted services is a reduction of $7,247,395 to CWC. This results in a reduction to the revenue requirement of $710,327 after gross up.

Capital Structure

Kentucky-American's proposed capital structure based on the projected 13-month average balances for the forecasted test period and the costs assigned to each capital component is shown in the table below:[183]

Class of Capital	13-Month Average Net Carrying Amount	Ratio	JDITC	Adjusted Capital	Cost Rate	13-Month Average Weighted Cost
Short-Term Debt	$ 8,914,663	1.31%	$ 0	$ 8,914,663	4.158%	0.050%
Long-Term Debt	314,752,544	46.10%	0.30	314,752,545	4.696%	2.160%
Preferred Stock	2,245,974	0.33%	0	2,245,974	8.500%	0.030%
Common Equity	356,818,465	52.26%	0.33	356,818,465	10.750%	5.620%
Total	$ 682,731,646		$ 0.64	$ 682,731,647		7.860%

When submitting its Base Period Updates, Kentucky-American submitted an updated forecasted capital structure and assigned cost rates; however, there was no

[181] Kentucky-American's Updated Forecasted Test Period Rate Base $674,241,247 - $7,247,395 = $ 666,993,852

[182] Moving Kentucky- American's Service Company Lag Days from -4.2 to 50.7.

[183] Application, Exhibit 37, Schedule J-1.

material change as a result of the update.[184] Kentucky-American's revised forecasted capital structure and assigned cost rates are shown in the table below:[185]

Class of Capital	13-Month Average Net Carrying Amount	Ratio	JDITC	Adjusted Capital	Cost Rate	13-Month Average Weighted Cost
Short-Term Debt	$ 8,914,663	1.31%	$ 0.01	$ 8,914,663	4.158%	0.050%
Long-Term Debt	314,753,047	46.10%	0.30	314,753,048	4.690%	2.160%
Preferred Stock	2,245,974	0.33%	0.00	2,245,974	8.500%	0.030%
Common Equity	356,818,465	52.26%	0.33	356,818,465	10.750%	5.620%
Total	$ 682,732,150		$ 0.64	$ 682,732,150		7.860%

In response to a post-hearing request for information, Kentucky-American provided an update to its capital structure and cost rates due to a September 15, 2025 transaction[186] in which Kentucky-American received $19 million, which differed from the $13 million it originally projected.[187] However, Kentucky-American stated that it is not seeking to recover the additional debt and cost of long-term debt in this proceeding, even though the additional long-term debt leads to a corresponding change to the projected balance of short-term debt and an increased Rate of Return.[188] As such, the update resulted in no change to the Rate of Return presented in Kentucky-American's base period update.[189]

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[184] Kentucky-American's Response to Staff's First Post-Hearing Request, Item 6a.

[185] Kentucky-American's Response to Staff's First Post-Hearing Request, Item 6a.

[186] See Case No, *2024-00018, Electronic Application of Kentucky-American Water Company for Issuance of Indebtedness and Continued Participation with American Water Capital Corp.* (Ky. PSC Mar. 25, 2024), Order in which the Commission approved (1) Kentucky-American's request for authority to issue indebtedness in an aggregate principal amount, not to exceed $60 million, through December 31, 2025, and (2) Kentucky-American's request for continued participation in its borrowing program with American Water Capital Corporation.

[187] Kentucky-American's Response to Staff's First Post-Hearing Request, Item 2.

[188] Kentucky-American's Response to Staff's First Post-Hearing Request, Item 2.

[189] Kentucky-American's Response to Staff's First Post-Hearing Request. Item 2.

Upon review of the record and being otherwise sufficiently advised, the Commission finds Kentucky-American's revised capital structure reasonable and that it accurately projects the test-year capitalization requirements. The Commission notes that, in Kentucky-American's last base rate proceeding, the Commission put Kentucky-American on notice regarding its increasing common equity ratio,[190] and acknowledges the decrease in Kentucky-American's equity ratio since its last base rate proceeding. The Commission expects Kentucky-American to continue to exercise prudent control over the amount of equity that is issued so that it maintains a balanced capital structure that more closely reflects an equal amount of debt and equity, and places less of a burden on its ratepayers due to the higher cost of equity.

<u>Return on Equity</u>

Kentucky-American proposed a Return on Equity (ROE) using the Discounted Cash Flow Model (DCF), Capital Asset Pricing Model (CAPM), and the Empirical CAPM.[191] In its models, Kentucky-American utilized a proxy group which included water and natural gas distribution utilities (Combination Proxy Group).[192] Kentucky-American requested an ROE of 10.75 percent based upon a range of 10.25 percent to 11.25 percent.[193]

Kentucky-American stated that it did not limit its proxy group to water utilities, but rather, it included a broader group of utilities that face similar risk to Kentucky-

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[190] Case No. 2023-00191, (Ky. PSC May 3, 2024), Order at 28.

[191] Application, Exhibit 10, Direct Testimony of Ann E. Bulkley (Bulkley Direct Testimony) at 2.

[192] Bulkley Direct Testimony at 17.

[193] Bulkley Direct Testimony at 5.

American.[194] Kentucky-American argued that a proxy group composed only of water utilities would result in a small group of companies for which data is limited.[195] Additionally, Kentucky-American stated that its recommendation takes into consideration its relative business and regulatory risk as compared with the proxy group, as well as its proposed capital structure as compared with the capital structures of the operating utilities of the companies contained in the proxy group.[196] Kentucky-American noted it also considered the effect of current and prospective capital market conditions on the cost of equity estimation models and on investors' return requirements, and noted that its analyses rely on forward-looking inputs and assumptions.[197] The table below summarizes the range of Kentucky-American's ROE estimates:[198]

[194] Bulkley Direct Testimony at 2.

[195] Bulkley Direct Testimony at 2.

[196] Bulkley Direct Testimony at 2.

[197] Bulkley Direct Testimony at 3 - 4. Kentucky-American noted specifically that the forward-looking analyses are the projected analyst growth rates in the DCF model, forecasted risk-free rate, and market risk premium in the CAPM analysis.

[198] Bulkley Direct Testimony, Exhibit AEB-1 at 1.

Method	Low Growth Rate	Average Growth Rate	High Growth Rate
DCF			
Median Results			
30-Day Average	9.42%	10.63%	11.36%
60-Day Average	9.51%	10.92%	11.46%
180-Day Average	9.36%	11.17%	11.59%
Average	9.43%	10.91%	11.47%

	30-Year Treasury Bond Yield		
	Current 30-day Average	Near-Term Projected	Longer-Term Projected
CAPM			
Current Value Line Beta	11.57%	11.56%	11.53%
Current Bloomberg Beta	10.59%	10.57%	10.52%
Long-Term Average Beta	10.65%	10.62%	10.57%
ECAPM			
Current Value Line Beta	11.82%	11.81%	11.79%
Current Bloomberg Beta	11.09%	11.07%	11.03%
Long-Term Avg. Value Line Beta	11.13%	11.11%	11.07%

The Attorney General/LFUCG provided an ROE analysis that employed the DCF and CAPM using historical and forecasted market risk premiums as well as publicly available estimates of market risk premiums from other sources.[199] The Attorney General/LFUCG stated that it used two sets of proxy groups including the Combination Proxy Group proposed by Kentucky-American, as well as a proxy group consisting of six investor-owned water utilities from the Value Line Investment Survey (Value Line) (Water

[199] Attorney General's Direct Testimony (filed Aug. 13, 2024), Direct Testimony of Richard Baudino (Baudino Direct Testimony) at 3.

Proxy Group).[200] The Attorney General/LFUCG's DCF analyses were based on the standard growth form of the model and employed four different growth rate forecasts from Value Line, S&P Capital IQ Pro, and Zacks.[201] The Attorney General/LFUCG's CAPM analyses used both historical and forward-looking data.[202] The Attorney General/LFUCG recommended an ROE of 9.50 percent, which it argued provides a fair return to investors on a relatively low-risk regulated water utility investment such as Kentucky-American.[203]

In regard to its DCF model, the Attorney General/LFUCG employed the average dividend yield and earnings growth rates, and calculated DCF estimates using two methods.[204] The first applied average growth rates and the second, median growth rates.[205] The Attorney General/LFUCG noted that, in the past, it used Yahoo! Finance to obtain consensus analysts' earnings growth forecasts; however, at the time the Attorney General/LFUCG prepared its testimony, Yahoo! Finance was not available so it instead used Value Line, Zacks, and S&P Capital IQ Pro.[206] The average growth rates ROE estimates ranged from 7.98 percent to 10.38 percent for the Combination Proxy Group and 8.97 percent to 9.56 percent for the Water Proxy Group, and the median growth rates ROE estimates ranged from 7.75 percent to 10.29 percent for the Combination Proxy Group and 8.80 percent to 9.31 percent for the Water Proxy Group, with the average of

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[200] Baudino Direct Testimony at 3.

[201] Baudino Direct Testimony at 13.

[202] Baudino Direct Testimony at 13.

[203] Baudino Direct Testimony at 3.

[204] Baudino Direct Testimony at 17-18.

[205] Baudino Direct Testimony at 20-21.

[206] Baudino Direct Testimony at 18.

the two methods being 9.73 percent and 8.87 percent for the Combination Proxy Group and Water Proxy Group, respectively.[207]

For its CAPM model, the Attorney General/LFUCG used three approaches to estimate the market risk premium (MRP).[208] The first approach used the expected return on the market and was forward-looking, the second approach employed three historical MRPs based on actual stock and bond returns, and the third approach used four published sources that estimate the current investor-required MRP.[209] In determining its risk-free rate, the Attorney General/LFUCG considered a six-month average of the 30-year Treasury Bond yield from February through July 2025, however, the Attorney General/LFUCG stated that it chose to use the most recent three-month average of 4.90 percent, given the rise in the 30-year Treasury yield over the three months prior.[210] To calculate its beta value used in the CAPM, the Attorney General/LFUCG used two sources.[211] First, the Attorney General/LFUCG obtained and averaged the beta values for the companies in the proxy groups from the most recent Value Line reports at the time its testimony and analyses were prepared.[212] Second, the Attorney General/LFUCG averaged the adjusted beta values from S&P Capital IQ.[213] Ultimately, the Attorney General/LFUCG averaged the two beta value sources in its CAPM analysis, which was

[207] Baudino Direct Testimony at 20-21.

[208] Baudino Direct Testimony at 25.

[209] Baudino Direct Testimony at 25.

[210] Baudino Direct Testimony at 30.

[211] Baudino Direct Testimony at 31.

[212] Baudino Direct Testimony at 31.

[213] Baudino Direct Testimony at 31-32.

0.78 for the Combination Proxy Group and 0.79 for the Water Proxy Group.[214] The following table summarizes the Attorney General/LFUCG's results:[215]

Method	Average
DCF	
Combination Proxy Group	
Average Growth Rates	
High	10.38%
Low	7.98%
Average	9.73%
Median Growth Rates	
High	10.29%
Low	7.75%
Average	9.23%
Water Proxy Group	
Average Growth Rates	
High	9.56%
Low	8.97%
Average	9.26%
Median Growth Rates	
High	9.31%
Low	8.49%
Average	8.87%
CAPM	
Forward-looking Market Return	9.55%
Historical Risk Premium	
Arithmetic Mean	10.59%
Supply Side MRP	9.77%
Supply Side less WWII Bias	9.03%
Kroll MRP	9.18%
KMPG MRP	8.98%
IESE MRP Survey	9.18%
Damodaran MRP	8.23%

[214] Baudino Direct Testimony at 32.

[215] Baudino Direct Testimony at 33, Table 1.

The Attorney General/LFUCG recommended an ROE range of 9.25 percent to 9.75 percent, and noted that the lower end of the range is consistent with the average ROE for the Water Proxy Group and the median ROE for the Combination Proxy Group, and that the upper end of the range is consistent with the average ROE for the Combination Proxy Group.[216] Additionally, the Attorney General/LFUCG noted that the DCF ROE for the Water Proxy Group is lower than the ROE for the Combination Proxy Group and explained that including gas distribution utilities in the Combination Proxy Group increased the DCF ROE substantially. However, the Attorney General/LFUCG argued that this is consistent with the Commission's concerns in its Order in Kentucky-American's last base rate case,[217] and that its ROE recommendations appropriately considered the lower DCF ROE from the Water Proxy Group as part of its recommended ROE range.[218]

With regard to Kentucky-American's DCF analysis, the Attorney General/LFUCG argued that the approaches had much in common including that the same Combination Proxy Group was used, that both employed six-month averages of stock prices, and both used the same three sources for growth rates and the same method of calculating the expected dividend yield.[219] However, the Attorney General/LFUCG noted that evaluating the Water Proxy Group is a necessary part of any DCF analysis used in this case, and that its DCF analysis for the Water Proxy Group revealed lower analysts' expected

[216] Baudino Direct Testimony at 34.

[217] Baudino Direct Testimony at 34.

[218] Baudino Direct Testimony at 34.

[219] Baudino Direct Testimony at 42.

earnings growth forecasts for investor-owned water utilities compared to gas distribution utilities.[220] The Attorney General/LFUCG argued that failing to take these factors into account and omitting forecasted dividend growth contributed to a significant overstatement of Kentucky-American's DCF results.[221]

With regard to Kentucky-American's CAPM analysis, the Attorney General/LFUCG noted that Kentucky-American only used one source to estimate its recommended MRP, which it argued led to an MRP range that is overstated and led to an overestimation of the CAPM ROE.[222] Additionally, the Attorney General/LFUCG argued that the main issue with Kentucky-American's CAPM analysis is the sole reliance on a forward-looking market return for the S&P 500.[223] The Attorney General/LFUCG argued that the projected market return of 12.58 percent is overstated due to reliance on an average Value Line long-term projected growth rate of 11.15 percent, which it argued is unsustainable in the long run.[224] The Attorney General/LFUCG argued that Kentucky-American's earnings growth forecast is not supportable when further consideration is given to both historical and forecasted gross domestic product (GDP) growth for the United States.[225] In addition, the Attorney General/LFUCG argued that the ECAPM is designed to account for the possibility that the CAPM understates the ROE for companies with betas less than 1.0 and that the argument that an adjustment factor is needed to "correct" the CAPM results for companies

[220] Baudino Direct Testimony at 42-43.

[221] Baudino Direct Testimony at 43.

[222] Baudino Direct Testimony at 43.

[223] Baudino Direct Testimony at 43.

[224] Baudino Direct Testimony at 43.

[225] Baudino Direct Testimony at 44.

with betas less than 1.0 is further evidence of the lack of accuracy inherent in the CAPM itself, and with beta in particular.[226] The Attorney General/LFUCG also argued that Kentucky-American provided no evidence that investors favor this version of the ECAPM over the standard CAPM.[227]

In response to the consideration of specific risk factors, the Attorney General/LFUCG noted specific risks Kentucky-American presented that it believes should be considered in setting the allowed cost of equity for Kentucky-American including its capital expenditure program, regulatory risks, and flotation costs.[228] The Attorney General/LFUCG argued that the Commission should not increase Kentucky-American's ROE in consideration of its capital expenditure program, and that it is Kentucky-American's responsibility to prudently manage its expenditures and the timing of its rate cases to ensure that it collects its reasonable costs of providing service to its ratepayers while maintaining a competitive return on its investments.[229] In addition, the Attorney General/LFUCG noted that Kentucky-American does have a significant projected capital expenditure program and that Kentucky-American has control over the amount and timing of its program, and argued that Kentucky-American's use of a future test year and its QIP both help mitigate the risk of the program.[230] The Attorney General/LFUCG also argued that the Commission should not consider flotation costs in its allowed ROE for Kentucky-American, as the Commission's consistent past precedent is not to allow flotation costs

[226] Baudino Direct Testimony at 46.

[227] Baudino Direct Testimony at 46-47.

[228] Baudino Direct Testimony at 47.

[229] Baudino Direct Testimony at 47.

[230] Baudino Direct Testimony at 47.

in the allowed ROE for regulated utilities in Kentucky, and argued that Kentucky-American has provided no new evidence that should change this practice.[231] The Attorney General/LFUCG opined that it is likely that flotation costs are already accounted for in current stock prices and that adding an adjustment for flotation costs amounts to double counting, and a DCF model using current stock prices should already account for investor expectations regarding the collection of flotation costs.[232] Additionally, the Attorney General/LFUCG disagreed with Kentucky-American's conclusion that it has a greater than average regulatory risk than the proxy group, although it noted that Kentucky-American did not include a specific adjustment for regulatory risk in its recommended ROE.[233] Finally, the Attorney General/LFUCG noted the Commission's ruling in Kentucky-American's previous rate case in which the Commission ruled that Kentucky-American's argument to factor in Kentucky-American's capital expenditure program, environmental risks, and regulatory risk when determining a fair ROE was not persuasive, as Kentucky-American has control over the amount and timing of its capital expenditure program and many other factors are mitigated through the use of a forecasted test year and Kentucky-American's QIP, which allow for lower regulatory lag and a more timely recovery of capital investments.[234]

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[231] Baudino Direct Testimony at 48, *citing* Case No. 2023-00191, (Ky. PSC May 3, 2024), Order, at 38-39; Case No. 2022-00372, *Electronic Application of Duke Energy Kentucky, Inc. for (1) An Adjustment of Electric Rates; (2) Approval of New Tariffs; (3) Approval of Accounting Practices to Establish Regulatory Assets and Liabilities; and (4) All Other Required Approvals and Relief* (Ky. PSC Oct. 12, 2023), Order at 41; Case No. 2021-00214, *Electronic Application of Atmos Energy Corporation for an Adjustment of Rates* (Ky. PSC May 19, 2022), Order at 48.

[232] Baudino Direct Testimony at 48.

[233] Baudino Direct Testimony at 48-49.

[234] Baudino Direct Testimony at 49.

In rebuttal, Kentucky-American disagreed with the following aspects of the Attorney General/LFUCG's analysis: (1) the use of a water only proxy group; (2) the use of DPS growth rates in the constant growth DCF model; (3) the application of the constant growth DCF model to the proxy group; (4) the market risk premium relied on to estimate the CAPM analysis; (5) the relevance of the ECAPM analysis; and (6) the effect of company-specific risks on the cost of equity for Kentucky-American.[235] Kentucky-American opined that the fundamental issue with the Attorney General/LFUCG's analysis is that its ROE recommendation of 9.50 percent is directionally inconsistent with the ROE authorized by the Commission in Kentucky-American's last rate proceeding relative to the changes in market conditions since that time that are indicative of an increase in the cost of equity.[236] Kentucky-American argued that the Attorney General/LFUCG's methodology for determining its ROE recommendation based on the results of its cost of equity models in the current proceeding is inconsistent with the methodology it relied on in Kentucky-American's last rate proceeding.[237] Additionally, Kentucky-American argued that the Commission should disregard the results of the Attorney General/LFUCG's analyses that rely on the Water Proxy Group.[238] Kentucky-American stated that it believes it is appropriate to include natural gas utilities in the proxy group used to estimate the cost of equity for a water utility because of the small size of the proxy group due to consolidation in the water industry, there are significant similarities between the business

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[235] Kentucky-American Rebuttal Testimony, Rebuttal Testimony of Ann E. Bulkley (Bulkley Rebuttal Testimony) (filed Sept. 15, 2025) at 13.

[236] Bulkley Rebuttal Testimony at 4.

[237] Bulkley Rebuttal Testimony at 4.

[238] Bulkley Rebuttal Testimony at 4.

and operating risks of water and natural gas distribution companies, the consideration of the results of a combination proxy group by several regulatory commissions, and historical annual average authorized ROEs for water and gas utilizes which are indicative that these utilities are reasonably comparable to one another.[239] Finally, Kentucky-American maintained its conclusion that Kentucky-American has greater regulatory risk relative to the proxy group because: (1) the proxy group companies had more timely cost recovery than Kentucky-American had in Kentucky, and (2) Kentucky-American has underearned its authorized ROE over the past seven years.[240]

In response to post-hearing discovery, Kentucky-American provided an update to its ROE analysis using data as of July 31, 2025. The results of the updated analysis are summarized in the table below:[241]

[239] Bulkley Rebuttal Testimony at 15.

[240] Bulkley Rebuttal Testimony at 56.

[241] Kentucky-American's Response to Staff's First Post-Hearing Request, Item 1.

Method	Low Growth Rate	Average Growth Rate	High Growth Rate
DCF			
Median Results			
30-Day Average	9.74%	10.39%	11.10%
60-Day Average	9.78%	10.43%	11.15%
180-Day Average	9.80%	10.45%	11.17%
Average	9.77%	10.42%	11.14%
Mean Results			
30-Day Average	8.92%	9.37%	10.08%
60-Day Average	8.94%	9.39%	10.02%
180-Day Average	8.95%	9.40%	9.98%
Average	8.94%	9.39%	10.03%

	30-Year Treasury Bond Yield		
	Current 30-day Average	Near-Term Projected	Longer-Term Projected
CAPM			
Current Value Line Beta	11.46%	11.42%	11.37%
Current Bloomberg Beta	10.94%	10.89%	10.83%
Long-Term Average Beta	11.27%	11.23%	11.17%
ECAPM			
Current Value Line Beta	11.93%	11.90%	11.87%
Current Bloomberg Beta	11.54%	11.50%	11.46%
Long-Term Avg. Value Line Beta	11.79%	11.76%	11.72%

In its brief, the Attorney General argued that, if the Commission approved Kentucky-American's proposed ROE of 10.75 percent, it would cause rates to increase to an unreasonable level and harm ratepayers.[242] As such, the Attorney General requested that the Commission adopt its recommendation of a 9.50 percent ROE for Kentucky-American, which would reduce Kentucky-American's requested rate increase

[242] Attorney General's Brief at 44.

by approximately $5,239,999.[243] Additionally, the Attorney General argued that Kentucky-American's QIP ROE should be 10-basis points less than the awarded ROE for its regulatory rate base.[244]

In its post-hearing brief, Kentucky-American argued that its proposed ROE of 10.75 percent creates a reasonable opportunity for capital investors to earn a risk-comparable return, allows Kentucky-American to maintain its financial integrity, and enables Kentucky-American to attract necessary capital investment for the benefit of its customer.[245] Additionally, Kentucky-American argued that its proposed ROE recognizes existing and expected capital market conditions, while the Attorney General's proposed ROE is unreasonably low and should be rejected.[246]

In evaluating the ROE for Kentucky-American, the Commission must evaluate and review each model and all parties' positions and balance the financial integrity of the utility with the interest of the consumer and the statutory obligation that rates be fair, just, and reasonable. The Commission has discussed, in recent cases including 2024-00276[247] and 2024-00354,[248] why it is appropriate for utilities to present, and for the Commission to evaluate, multiple methodologies to estimate ROEs. Each approach has its own

[243] Attorney General's Brief at 44.

[244] Attorney General's Brief at 47.

[245] Kentucky-American's Brief at 43.

[246] Kentucky-American's Brief at 43-44.

[247] Case No. 2024-00276, *Electronic Application of Atmos Energy Corporation for An Adjustment of Rates; Approval of Tariff Revisions; And Other General Relief* (Ky. PSC Aug. 11, 2025), Order at 35-36.

[248] Case No. 2024-00354, *Electronic Application of Duke Energy Kentucky, Inc. For: 1) An Adjustment of The Electric Rates; 2) Approval of New Tariffs; 3) Approval of Accounting Practices to Establish Regulatory Assets and Liabilities; And 4) All Other Required Approvals and Relief* (Ky. PSC Oct. 2, 2025), Order at 50-51.

strengths and limiting assumptions. As demonstrated in the respective ROE testimonies in this proceeding, considerable variation exists in both data and application within each modeling approach, which can lead to very different results. The Commission's role is to conduct a balanced analysis of all presented models, while giving weight to current economic trends and conditions.

The Commission cautions all parties against unreasonably removing or ignoring "outlier" data due to a subjective perception of being "too high" or "too low." As demonstrated in the case record, there are multiple actions that can be and were taken into account for "outlier" or "unreasonable" data. Result-oriented exclusions of data that are not beyond the realm of reasonableness are inappropriate. Results based upon excluded data without adequate support will be given less weight in future Commission determinations.

The Commission is not persuaded by Kentucky-American's argument that a 10.75 percent ROE is reasonable. The Commission reiterates that it continues to reject the use flotation cost adjustments, financial risk adjustments, and size adjustments in the ROE analyses. Although Kentucky-American's final cost of equity results did not include an adjustment for flotation cost recovery, the estimated effect of flotation cost on the cost of equity was considered in identifying its recommended ROE within the range of cost of equity estimates from the various models.[249] The Attorney General/LFUCG argued that the Commission should not consider flotation costs in its allowed ROE for Kentucky-American.[250] The Commission agrees with the Attorney General/LFUCG's argument

[249] Bulkley Direct testimony at 47-48.

[250] Baudino Direct Testimony at 47-48.

regarding flotation cost adjustments, and finds that Kentucky-American has not established that flotation costs should be considered in the determination of an allowed ROE. Additionally, the Commission notes that Kentucky-American's argument regarding its capital expenditure program, environmental risk, and regulatory risks are factors that should be considered when determining a fair ROE is not persuasive. Kentucky-American has control over the amount and timing of its capital expenditure program and many other factors are mitigated through the use of a forecasted test year, which lowers regulatory lag and allows for a timelier recovery of capital investments. The Commission does acknowledge that, under normal circumstances, the termination of a program such as the QIP would potentially be cause for consideration in determining a fair ROE, as such mechanisms typically also lower regulatory lag and allow for a timelier recovery of capital investments. However, the Commission notes that, as discussed above, since Kentucky-American has not proposed any new QIP projects in its QIP 7, the change in Kentucky-American's risk profile due to the termination of the QIP mechanism, if any, will likely be immaterial. The Commission will reevaluate this determination in a subsequent proceeding, once any effects of the termination of the QIP mechanism are evident and justifiable.

The Commission continues to acknowledge that gas and electric utilities assume and absorb far more financial, environmental, and regulatory risk than a water utility, and that the argument that those types of utilities possess similar operating and financial risk to that of Kentucky-American is flawed. However, the Commission also understands Kentucky-American's argument that the results of an analysis based on such a consolidated sample size as the proxy group for water utilities may also be flawed. As such, the Commission appreciates the Attorney General/LFUCG's inclusion of both a water and combination utility proxy group in its analysis, the results of which present the Commission with a comparable view of the nuances with each scenario.

Therefore, the Commission expresses its preference in future rate proceedings for investor-owned water utilities such as Kentucky-American, both a water only proxy group and combination gas and water proxy group be utilized in ROE analyses, and will be given an appropriate weight in the Commission's consideration of a fair, just and reasonable return for the utility. The Commission also notes that the utility should consider that the use of gas utilities in the proxy group may skew the results of the analysis upwards. If the utility chooses to utilize a combination water and gas utility proxy group in a subsequent proceeding, it should scrutinize the companies' comparability to the utility and provide substantial evidence that each company in the proxy group is a relevant proxy.

For the reasons set forth above, the Commission finds that a ROE of 9.70 percent is fair, just, and reasonable and appropriately balances the needs of Kentucky-American and its customers and addresses the current economic state of the capital markets.

Rate of Return Summary

Applying the cost rates of 4.70 percent for long-term debt, 4.16 percent for short-term debt, 8.50 percent for preferred stock, and 9.70 percent for common equity, the capital structure percentages consisting of 46.10 percent, 1.31 percent, 0.33 percent, and 52.26 percent, respectively, produce an overall weighted cost of capital of 7.31 percent.

	Percent of Total	Cost Rate	Weighted Avg. Cost
Short-Term Debt	1.31%	4.16%	0.05%
Long-Term Debt	46.10%	4.69%	2.16%
Preferred Stock	0.33%	8.50%	0.03%
Common Equity	52.26%	9.70%	5.07%
Total Capital	100.00%		7.31%

AUTHORIZED INCREASE IN REVENUE REQUIREMENT

The effect of the Commission's adjustments is a total revenue requirement increase of $18,200,097, as shown in Appendix A, which includes the ROE discussed above. This reflects a $8,736,243 decrease of Kentucky-American's requested revenue increase of $26,936,340.

Operating Revenues at Present Rates	$ 135,872,961
Less: Total Expenses	100,689,918
Present Rate Operating Income	$ 35,183,043
Net Rate Base	$ 666,993,852
Rate of Return	7.31%
Operating Income Required	48,757,251
Less: Present Rate Operating Income	35,183,043
Gross Revenue Conversion Factor	1.3408
Required Revenue Increase	$ 18,200,097

COST OF SERVICE STUDY (COSS)

Kentucky-American filed a COSS using the base-extra capacity method as outlined in the American Water Works Association (AWWA), "Principles of Water Rates, Fees and Charges," (AWWA M1 Manual).[251] The Commission notes that it previously accepted the use of this methodology for cost allocation and development of water service

[251] Application, Exhibit 10, Direct Testimony of Max McClellan (McClellan Direct Testimony) at 3.

rates in Kentucky-American's previous two rate cases.[252] However, the Commission is concerned with Kentucky-American's utilization of advance metering infrastructure (AMI) data from its Missouri-American Water Company's St. Louis County service territory as a proxy for maximum daily consumption values and peaking factors within the proposed COSS.[253]

In the formal hearing, Kentucky-American witness Max McClellan stated that the reason for using the Missouri AMI usage data was because the territory recently had a large AMI meter roll out, and such, that the AMI usage data, being more granular, produced better results.[254] Although the Commission supports the use of more granular data, when possible, the Missouri AMI usage data used as a proxy in this case cannot be verified to accurately represent what Kentucky-American's AMI usage data would be. The Commission acknowledges that subjective decisions can be made within the development of a COSS but Kentucky-American has service territory usage information. The Commission finds that data from within the service territory only should be utilized in future rate case filings.

Kentucky-American provided its Kentucky usage data in response to a post-hearing request for information.[255] The table below compares the results of the COSSs using Missouri AMI data and Kentucky data:

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[252] Case No. 2018-00358, (Ky. PSC June 27, 2019) ,Order at 67-68. Case No. 2023-00191, (Ky. PSC May 03, 2024), Order at 41.

[253] McClellan Direct Testimony at 8.

[254] HVT of the September 23, 2025 Hearing, Max McClellan at 01:33:14–01:33:52.

[255] Kentucky-American's Response to Staff's Third Post-Hearing Request, Item 1A, Attachment, KAW_R_PSCHDR3_NUM001_102725_Attachment.

Customer Class	Revenues at Present Rates	Cost of Service (proposed)	Percent Allocation	Cost of Service (modified)	Percent Allocation
Residential	$74,139,687	$77,457,275	48.09%	$79,215,550	49.18%
Commercial	$35,279,904	$39,693,592	24.65%	$39,620,725	24.60%
Industrial	$3,324,989	$4,402,340	2.73%	$3,997,046	2.48%
Other Public Authority	$8,983,234	$11,883,679	7.38%	$10,952,675	6.80%
Sales for Resale	$1,881,729	$3,443,132	2.14%	$3,646,214	2.26%
Public Fire	$5,687,531	$16,810,345	10.44%	$16,449,044	10.21%
Private Fire	$4,862,671	$7,207,362	4.47%	$7,004,830	4.35%
Misc.	$114,793	$163,358	0.10%	$173,467	0.11%
Total	$134,304,528	$161,061,083	100.00%	$161,059,550	100.00%

As shown in the table above, when the Kentucky usage data is inserted into the proposed COSS, the results vary slightly. Therefore, due to only slight differences in the results, the Commission finds the proposed COSS to be acceptable in allocating the revenue increase granted herein. However, in Kentucky-American's next rate case, the Commission expects the use of its Kentucky service territories usage data only in the development of maximum daily consumption values and peaking factors for each customer class.

REVENUE ALLOCATION AND RATE DESIGN

For all general water service, Kentucky-American separates customers by classification. Kentucky-American currently charges a monthly meter charge that is differentiated by meter size and applied uniformly to all customers groups, and a volumetric rate for each customer class.[256] Kentucky-American proposed to increase the

[256] McClellan Direct Testimony at 14-15.

monthly meter charges by approximately 11 percent, and the volumetric charges based upon their respective class cost to serve.[257]

Kentucky-American proposed to increase private and public fire charges towards their respective class cost to serve, with revenue increase not exceeding 125 percent of the overall revenue increase percentage.[258] The table below illustrates the present and proposed rates by Kentucky-American:[259]

	Present Meter Charge	Proposed Meter Charge	Percent Increase
Meter Size			
5/8" Meter	$17.55	$19.45	11%
3/4" Meter	$26.20	$29.00	11%
1" Meter	$43.60	$48.30	11%
1 1/2" Meter	$87.30	$96.80	11%
2" Meter	$139.70	$154.80	11%
3" Meter	$261.90	$290.30	11%
4" Meter	$436.60	$483.90	11%
6" Meter	$873.00	$967.50	11%
8" Meter	$1,396.80	$1,548.00	11%
	Present Volumetric Charge	Proposed Volumetric Charge	Percent Increase
Customer Class			
Residential	$6.7291	$9.4567	41%
Commercial	$6.0875	$8.1129	33%
Industrial	$5.0324	$6.8779	37%
Public Authorities	$5.6070	$7.8187	39%
Sales for Resale	$4.9527	$6.9266	40%
Bulk	$4.0000	$6.1736	54%

The monthly meter charges supported by the COSS slightly differ from the proposed rates. In most meter sizes, the COSS supports a lower monthly meter charge than proposed by Kentucky-American. Notably, the 5/8" meter, which services primarily

[257] McClellan Direct Testimony at 16.

[258] McClellan Direct Testimony at 16.

[259] McClellan Direct Testimony at 17, Table 4 and Table 5.

residential customers, is the only monthly meter charge at its COSS-supported rate. Kentucky-American's COSS supports the following monthly meter charges:[260]

Meter Size	COSS Meter Charge
5/8" Meter	$19.45
3/4" Meter	$26.65
1" Meter	$42.96
1 1/2" Meter	$79.35
2" Meter	$124.47
3" Meter	$239.69
4" Meter	$369.89
6" Meter	$730.92
8" Meter	$1,165.10

The Attorney General/LFUCG did not present any evidence as to the COSS. However, the Attorney General stated that the proposed monthly meter charge increase of 11 percent, coupled with the proposed volumetric charge of $9.4567, an approximate 41 percent increase, could pose financial hardship on customers who are already struggling to make ends meet.[261] Additionally, the Attorney General stated that the proposed increases violate the principle of gradualism.[262] The Attorney General also stated that since Kentucky-American's commercial and residential monthly service charges are proposed to be the same, and the commercial volumetric charge is less than that of the residential class, then it awarding such a rate design may lead to an inequitable result.[263]

[260] Kentucky-American's Response to Staff's First Request, Item 3, KAW_R_PSCDR1_NUM003_Attachment.xlsx, "Meter Charge Calc" Tab.

[261] Attorney General's Brief at 48.

[262] Attorney General's Brief at 48.

[263] Attorney General's Brief at 48-49.

LFUCG stated that Kentucky-American's proposed rates are unreasonable and should be denied.[264]

The Commission acknowledges the arguments of LFUCG and the Attorney General. The Commission agrees with the Attorney General that the residential class should not be charged more than that of a commercial customer. The Commission gives substantial weight to the evidence from the COSS and acknowledges the importance of gradually moving towards the cost-based rates. The Commission must weigh these factors and strike a balance between the customers' financial interest and the utility's ability to provide adequate, reliable service. Therefore, the Commission finds that Kentucky-American's proposed allocation is reasonable with modifications.

Utilizing the Commission's approved revenue increase of $18,200,097, or 13.33 percent, the Commission will allocate this percentage increase across-the-board to all monthly meter charges ranging from 5/8" to 8". For example, for the residential customer using a 5/8" size meter, the monthly meter charge will increase from $17.55 to $19.89, or 13.33 percent. The residential volumetric rate will increase from $6.7291 per 1,000 gallons to $7.8656 per 1,000 gallons. The increase in rates results in a monthly increase of $6.82, or 14.31 percent, from $44.08 to $50.90, for a residential customer utilizing approximately 3,942 gallons per month.

Similarly to Kentucky-American's proposal, Fire Protection and Hydrant monthly rates will increase across-the-board by approximately 35 percent. Volumetric rates were adjusted to be closer to cost-of-service.

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[264] LFUCG's Post-Hearing Brief (filed Oct. 27, 2025) at 1.

The Commission notes that it does not support a rate design where the commercial class is charged less than that of a residential customer. Therefore, the commercial volumetric charge will increase from $6.0875 per 1,000 gallons to $8.0066 per 1,000 gallons or 31.53 percent. All other rates approved by the Commission are fair, just, and reasonable, and are reflected in Appendix B to this Order.

IT IS THEREFORE ORDERED that:

1. The rates and charges proposed by Kentucky-American are denied.

2. The rates and charges, as set forth in Appendix B to this Order, are approved as fair, just and reasonable rates for Kentucky-American, and these rates and charges are approved for service rendered on and after the date of the entry of this Order.

3. Kentucky-American's proposed roll in of current QIP expenditures into base rates is granted.

4. Kentucky-American's QIP rider is terminated effective December 31, 2025.

5. In its next base rate proceeding, Kentucky-American shall forecast its operating expenses based on its internal budgeting process on an individual expense basis, rather than applying a uniform adjustment to a number of its operating expenses.

6. 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 reflecting that they were approved pursuant to this Order.

7. This case is closed and removed from the Commission's docket.

PUBLIC SERVICE COMMISSION

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Chairman

____
Commissioner

____
Commissioner

ATTEST:

Linda Bridwell RP
____
Executive Director

ENTERED
DEC 16 2025
AD
KENTUCKY PUBLIC
SERVICE COMMISSION

APPENDIX A

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE COMMISSION IN CASE NO. 2025-00122 DATED DEC 16 2025

Overall Financial Summary - Including QIP

Description	Forecasted Test Period Application	Difference	Forecasted Test Period Updated	Difference	Forecasted Test Period Commission
Rate Base	$ 674,394,979	$ (153,732)	$ 674,241,247	$ (7,247,395)	$ 666,993,852
Requested Rate of Return	7.86%	-	7.86%	-0.55%	7.31%
Required Operating Income	53,007,445	(12,083)	52,995,362	(4,238,111)	48,757,251
Less: Adjusted Operating Income	32,917,472	(217,105)	32,700,367	2,482,676	35,183,043
Income Deficiency / (Sufficiency)	20,089,973	205,022	20,294,995	(6,720,787)	13,574,208
Gross Revenue Conversion Factor	1.3408	-	1.3408	-	1.3408
Revenue Increase	$ 26,936,340	$ 274,890	$ 27,211,230	$ (9,011,133)	$ 18,200,097
Percent Increase	19.72%		20.03%		13.33%

Kentucky-American Water Requested Rate Increase	$ 26,936,340
Kentucky-American Water Base Period Update Adj	274,890
	$ 27,211,230
Adjustments:	
O&M Adjustments	
Incentive Compensation	(1,858,253)
Employee Stock Purchase Plan Discount	(62,349)
Unaccounted For Water	(294,881)
Rate Case Expense	(596,480)
Business Development Expense	(214,852)
401(k) Expense	(41,206)
Growth Factor	(137,791)
Membership Dues	(41,436)
Payroll Tax	(135,795)
Interest Synchronization	54,308
Rate Base Adjustments	(710,327)
Rate of Return Adjsutment	(4,972,070)
Rate Increase	$ 18,200,097
Percent Rate Increase	13.33%

APPENDIX B

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE COMMISSION IN CASE NO. 2025-00122 DATED DEC 16 2025

The following rates and charges are prescribed for the customers in the area served by Kentucky-American Water Company. All other rates and charges not specifically mentioned herein shall remain the same as those in effect under the authority of the Commission prior to the effective date of this Order.

Monthly Service Charge

Meter Size	
5/8" – Meter	$19.89 Minimum Bill
3/4" – Meter	$29.75 Minimum Bill
1" – Meter	$49.45 Minimum Bill
1 1/2" – Meter	$98.95 Minimum Bill
2" – Meter	$158.40 Minimum Bill
3" – Meter	$296.85 Minimum Bill
4" – Meter	$494.85 Minimum Bill
6" – Meter	$989.40 Minimum Bill
8" – Meter	$1,583.05 Minimum Bill

Volumetric Charge

Service Type	
Residential	$0.0078656 per Gallon
Commercial	$0.0080066 per Gallon
Industrial	$0.0070849 per Gallon

Other Public Authority	$0.0080347 per Gallon
Sales for Resale	$0.0083091 per Gallon

Monthly Public or Private Fire Connections

Size of Service	
2” Diameter	$14.00 per Month
4” Diameter	$56.00 per Month
6” Diameter	$125.55 per Month
8” Diameter	$223.00 per Month
10” Diameter	$348.25 per Month
12” Diameter	$521.25 per Month
14” Diameter	$502.00 per Month
16” Diameter	$891.50 per Month

Hydrant Charge

Public Hydrant	$75.00 per Month
Private Hydrant	$120.00 per Month

Bulk Sales

Rate per 50 Gallons	$3.2946
Rate per 100 Gallons	$5.5892

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