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June 25, 2007

RECEIVED

JUN 27 2007

PUBLIC SERVICE  
COMMISSION

Public Service Commission  
ATTN: Ms. Beth O'Donnell, Executive Director  
211 Sower Boulevard  
P.O. Box 615  
Frankfort, Kentucky 40601

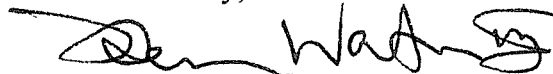
Re: Case No. 2006-00403

Dear Ms. O'Donnell:

Enclosed is an original Exception and ten (10) copies for filing in the above referenced case. I have also enclosed an extra copy for you to stamp file and return to this office in the self addressed stamped envelope.

Thank you for your cooperation in this matter. Please do not hesitate to contact me should you have any questions, and thank you for your kind and prompt attention.

Sincerely,

  
Henry Watson III

HW/lmh

Enclosures

Cc: City of Falmouth

COMMONWEALTH OF KENTUCKY  
BEFORE THE PUBLIC SERVICE COMMISSION

RECEIVED  
JUN 27 2007  
PUBLIC SERVICE  
COMMISSION

In the Matter of:

PROPOSED ADJUSTMENT OF THE )  
WHOLESALE WATER SERVICE ) CASE NO. 2006-00403  
RATES OF THE CITY OF FALMOUTH)

**EXCEPTIONS**

Comes now the City of Falmouth, by counsel, and notes for the record its Exceptions to the Staff Report in City of Falmouth Case, PSC No. 2006-00403, as set forth in the Commission's Order of May 11, 2007.

**SUBJECT MATTER JURISDICTION**

The City of Falmouth denies that the PSC has subject matter jurisdiction over the contract between the City of Falmouth and the Pendleton County Water District, based on the fact that the Pendleton County Water District has another source of supply, has relied upon same, and the parties are not in a "monopoly-dependent" relationship. See PSC Case No. 2004-00318. The finding of the Kentucky Supreme Court in the seminal case of *Simpson County Water District v. City of Franklin*, 872 S.W.2d 460 (Ky., 1994), (from a deeply divided Court), indicates that the rationale behind the decision was the necessary regulation of a supplier, when the entity being supplied was clearly and statutorily regulated by the Public Service Commission, and the fact that a monopoly existed leaving the supplied utility with no other avenue of supply.

The essential rationale for any price regulation of economic activity in a free market society is monopoly.

Additionally, it should be pointed out that the Kentucky General Assembly has taken no action on the statutory scheme involving the regulation of municipals since the decision of the Kentucky Supreme Court in 1994, nor has there been a single Kentucky Administrative Regulation proposed by the Public Service Commission addressing in any way the differences between the provision of retail and wholesale water service by a Kentucky Municipality and those utilities which provide services, either on a non-profit or a profit making basis.

The same regulatory scheme and approach to the regulation of profit making monopolies should not necessarily extend to Kentucky's cities, without taking into account the nature and operation of local government in the Commonwealth, and the reasons cities have taken it upon themselves, over time, to provide essential urban services such as potable water. Without a source of supply, most of which are municipalities, Kentucky's Water Districts and Water Associations would not exist, and the people of rural Kentucky would be without affordable potable water.

For the foregoing reasons, the City of Falmouth urges that this Commission is without subject matter jurisdiction over its rates with the Pendleton County Water District.

## **STAFF STUDY**

It is the understanding of the City of Falmouth that the rates that were applied for by the City in August of 2006 became effective as a matter of law on June 23, 2007, based on the provisions of KRS 278.190. It also appears from the record that the Staff Study in question was never finalized by the Public Service Commission in reaching any decision regarding these rates, and that the Study, as such, is not only irrelevant to this case, but to any future proceeding before this body or in any Court of competent jurisdiction.

The City of Falmouth objects to any use of the Staff Study as outlined above.

## **SPECIFIC EXCEPTIONS**

The Staff reduced from seventeen (17) to fourteen (14) the number of employees to be considered in the budget for the cost of service study. Additionally, the number of “employee equivalents” was thus reduced, also objected to.

Certain *pro forma* chemical expenses were adjusted by the Staff, and the City of Falmouth objects to the adjustments.

In examining costs allowable for depreciation the Staff relied upon an industry standard for depreciation of equipment, including meters, deciding that Falmouth’s depreciation schedule of 8.5 years was disallowed. It is respectfully submitted that reliance upon an industry standard, without resort to the actual testing or other methods utilized to establish life expectancy of equipment,

including meters, is arbitrary and capricious, and that proof should be heard on the issue of depreciation of equipment, as same adjusted the factors going into the Staff Study's cost of service, and use of such depreciation schedules is objected to by the City of Falmouth.

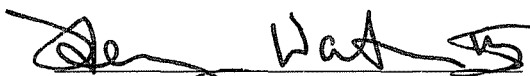
Respectfully submitted,



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Counsel for the City of Falmouth

#### CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing Exceptions was served upon the Commonwealth of Kentucky Public Service Commission by facsimile message at 502-564-3460, attention J.R. Goff, Esq., and by first class mail at 211 Sower Building, P.O. Box 615, Frankfort, Kentucky 40602-0615, upon William T. Jones, Manager, Pendleton County Water District, by mailing him a copy at P.O. Box 232, Falmouth, Kentucky 41040, and upon Wayne Lonaker, Manager, East Pendleton County Water District, by mailing him at copy at 600 Woodson Road, P.O. Box 29, Falmouth, Kentucky 41040, all on this the 25<sup>th</sup> day of June, 2007.

  
Henry Watson III