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June 5, 1997

VIA HAND DELIVERY

Mossou PL

Lila Jaber, Esquire
Division of Legal Services
Florida Public Service Commission
2540 Shumard Oak Boulevard
Tallahassee, Florida 32399

Re: Aloha Utilities, Inc. and Florida Waterworks Association v.
Florida Public Service Commission (Audits)
Our File No. 26038.22

Dear Lila:

Attached is an outline of our proposal for settlement which we have formulated in order to avoid litigation on this rule challenge while addressing to a certain extent both parties' concerns.

One item that came up during our recent conversations was a concern expressed by Ms. Tricia Merchant that Aloha had high authorized rates of return for its systems. This is not true. While the rates of return for the Aloha Gardens water and sewer systems and Seven Springs water and sewer systems were set sometime ago and in different cases, the authorized rates of return for these systems as set in the company's last rate proceedings are as follows:

ACK _____
AFA _____
APP _____ Aloha Gardens - Water - 10% rate of return; Order No. 9526
CAF _____ Seven Springs - Water and Sewer - 10.18% rate of return; Order
CMU _____ 9278
CTR _____ Aloha Gardens - Sewer - 10.85% rate of return; Order PSC-92-
EAG _____ 0578-POF-SU
LEG _____
LIN _____ These are all lower than the most recently authorized return
in the Utility's reuse case of 11.0%.
OPC _____
RCH _____ The Utility's authorized AFUDC rate is relatively high and we
have proposed to reduce that as part of any settlement.
SEC 1 _____
WAS _____
OTH _____

DOCUMENT NUMBER-DATE

05602 JUN-56

FPSC-RECORDS/REPORTING

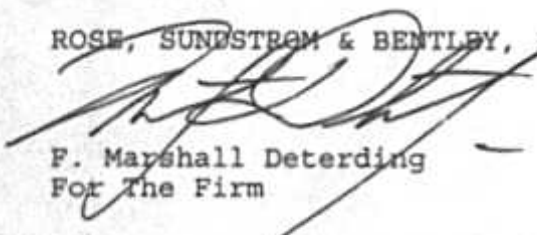
Lila Jaber, Esquire
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Ms. Merchant also expressed a concern with the earnings level for the Utility. The annual report shows that such concern is unfounded. Ms. Merchant mentioned that the recently filed annual report showed one system substantially overearning. The one she is referring to is the Aloha Gardens water system which showed an 88% return. However, in the recently adopted settlement proposal in Commission Docket No. 961419-WS, Aloha has agreed to reduce rates for this system by an annualized total of \$17,700. This will bring the rate of return on this system down to approximately 4%. In addition, the dollars involved in the alleged overearning were immaterial. The only reason such a high percentage for achieved rate of return was reflected was because of the very small rate base for this system. The other systems are within or substantially below the range of their authorized returns. Overall, the Utility in its total combined operations; or in its combined water or sewer operations; or in its combined Aloha Gardens or Seven Springs systems is underearning significantly. Anyway you view this, the Utility is not in an overearning situation.

In light of these facts and the benefits that can be gained from settlement for both sides and for the industry from establishment of rules, I would request that you consider carefully the attached proposal and let us know your position no later than Monday, June 9, 1997, at noon. If the Staff can agree to this settlement proposal, then we are willing to seek a continuance of the rule challenge proceedings until such time as the Commission as a whole has a chance to consider the settlement. Please let us know your position as soon as is possible so that we can draft the appropriate formal proposal.

Sincerely,

ROSE, SUNDBROM & BENTLEY, LLP



F. Marshall Deterding
For The Firm

FMD/lts
Enclosure

cc: Ms. Blanca Bayo
Richard Bellak, Esquire
Bobbie Reyes, Esquire

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Tricia Merchant, CPA
Ms. Billie Messer
Mr. Steve Watford
Robert Nixon, CPA

UNDOCKETED AUDIT AND RULE CHALLENGE
SETTLEMENT PROPOSAL

Under the settlement which we discussed, the parties would have the following responsibilities:

Aloha Obligations

1. Withdraw rule challenge petition currently pending at DOAH upon acceptance of the settlement proposal by the Commission.
2. Aloha will provide information to allow the Public Service Commission to calculate and adjust its AFUDC rate to one based on current capital and equity costs. This new rate will then be utilized on a prospective basis.
3. Aloha will provide, informally, responses to any questions which the Staff wishes to pose concerning the 1996 Annual Report and related specifically to any issues raised therein which suggest the possibility of overearnings for those systems.

PSC Obligations

1. The PSC will immediately proceed to rulemaking on the procedures and criteria for conducting audits of regulated water and wastewater utility companies with involvement by the Florida Waterworks Association, Aloha and all other interested parties. Such rule making shall include, at a minimum, the procedures governing: the ordering of an audit, the conduct of an audit, and the use of audit once completed.
2. The Commission will cancel its current informally scheduled audit of the 1996 Annual Report of Aloha Utilities, Inc. To the extent after receipt of the 1997 or 1998 Annual Reports, the Commission still believes it is appropriate and necessary to audit the books and records of Aloha, the Commission will arrange an audit based upon the 1997 or 1998 calendar year anytime after receipt of the annual report for those years or after the finalization of the rulemaking as outlined in Paragraph 1. above, whichever comes later. The decision to undertake such an audit and the procedure for any such audit shall be based upon application of such new rule as adopted.
3. The Commission Staff will issue a recommendation to the Commission for adoption of this settlement proposal and advocate for full acceptance of the settlement proposal.

Proposed Delays Pending Acceptance of Settlement Proposal

The parties have already agreed as to the following delays:

1. Delay in the response to the discovery due on June 4, 1997, until June 9, 1997 thereby giving the Commission Staff the opportunity to review this proposal for settlement and accept or reject it. If during this period, the proposal for settlement is accepted by the PSC Staff, the discovery due date will be held in abeyance pending Commission approval and the matter will be presented to the Public Service Commission at its June 24, 1997 Agenda Conference. If the proposal for settlement is accepted by the Commission, the parties will move forward with their obligations hereunder.

If the proposal for settlement is rejected by the Commission, the currently pending discovery will be due two days after the date of the Commission's decision at the June 24, 1997 Agenda Conference and any subsequent discovery will be due in accordance with the hearing officer's previously entered orders.

2. Aloha agrees to request a 21 day delay in the proposed hearing date on the rule challenge while the Commission Staff takes a recommendation before the full Commission to accept this proposal for settlement.

If the Commission rejects the proposed settlement, the rule challenge proceeding will immediately be reactivated in conformance with the strict timetables outlined by the hearing officer and applicable rules and statutes.

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