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ROBERT M. C. ROSE  
OF COUNSEL

October 10, 2001  
VIA HAND DELIVERY

OCT 10 PM 2:49  
COMMISSION CLERK

Ralph Jaeger, Esquire  
Division of Legal Services  
Florida Public Service Commission  
2540 Shumard Oak Boulevard  
Tallahassee, Florida 32399-0873

Re: Aloha Utilities, Inc.; PSC Docket No. 010503-WU  
Our File No. 26038.35

Dear Ralph:

Please replace the letter sent to you yesterday with the attached, as there were typographical errors in the version sent yesterday.

By copy of this letter, I am asking that everyone in receipt of this letter do the same. Should you have any questions in this regard, please let me know.

Sincerely,

ROSE, SUNDBSTROM & BENTLEY, LLP



F. Marshall Deterding  
For The Firm

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FMD\tms  
cc: Blanca S. Bayo, Director  
Bart Fletcher, Esquire  
Tricia Merchant, CPA  
Mr. Stephen G. Watford  
Robert C. Nixon, CPA  
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Re: Aloha Utilities, Inc.; PSC Docket No. 010503-WU  
Our File No. 26038.35

Dear Ralph:

Aloha Utilities, Inc., its management and its consultants have reviewed the staff recommendation on interim rates issued on October 4, 2001 and to be considered by the Commission at its October 16, 2001 agenda conference, and believe there are several errors, or issues raised therein, that need further discussion. We recognize that the Commission staff generally does not wish to engage in protracted discussions of issues arising out of interim recommendations. However, in this circumstance, we believe that the staff's proposed treatment of several issues for interim purposes and some not addressed within the staff recommendation, need to be addressed for interim purposes. Hopefully, the staff will take these matters into consideration when presenting their recommendation to the Commission and make appropriate adjustments orally at that time. We believe it is very important that these be not only presented to you, but also presented to the Commissioners. I have outlined the three major issues separately below:

1. Depreciation Expense - The staff has made a significant adjustment to depreciation expense for interim purposes, based upon a comparison of the accumulated depreciation account between June 30, 2000 and June 30, 2001. We do not believe this is appropriate. The change in A/D used by staff contained the effect of retirements backed in accordance with the NARUC and as such, does not represent the appropriate amount of depreciation expense. I am attaching hereto a brief discussion of this issue, prepared by Cronin, Jackson, Nixon & Wilson, which I believe demonstrates the inappropriateness of the adjustment made by the staff.
2. Income Tax Adjustment - The staff has made an adjustment to the proposed income tax provision presented by Aloha, which is not discussed anywhere within the staff recommendation. It is our understanding that this results from the staff's failure to recognize a deferred tax provision required by the provisions of Section 168 of the Internal Revenue Code. We do not understand why the staff has proposed to eliminate this deferred tax provision specifically required of the Utility by the Internal Revenue Code, and believe the staff should reconsider the conclusion to do so inherent in their recommendation to the Commissioners.

Ralph Jaeger, Esquire  
October 10, 2001  
Page 2

3. Corporate Undertaking - The staff has taken the position that the Utility cannot utilize a Corporate Undertaking as security for potential refund of interim rates, totaling \$192,139. It is interesting to note that the Commission has just recently finished an overearnings investigation in which the rates of all four of Aloha's systems were analyzed and allegedly compensatory rates set, and yet the Commission staff is recommending that the Utility does not have the financial viability to support \$192,000 Letter of Credit, despite authorized revenues of over \$5 million per year.

It should also be kept in mind that the Utility has debt service requirements which include debt coverage ratios. When the Utility is collecting revenues, to which it has no access, the bank will not allow those to be counted in calculating such ratios. As such, unnecessary escrow of revenues places the Utility in danger of default.

Attached is a copy of an analysis of the Utility's financial condition prepared by the Utility's accountants, that we believe demonstrates that the Utility is quite capable of supporting such a Corporate Undertaking, and that the staff analysis is at least dated, if not irrelevant to the issue of a Corporate Undertaking that this Utility can support.

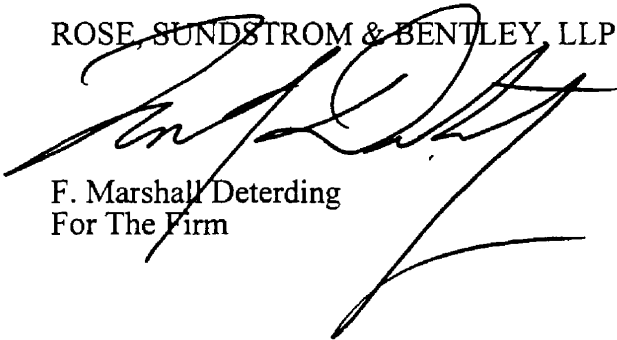
In addition, at a minimum, the Utility believes the Commission should authorize the use of some Corporate Undertaking to secure at least part of the interim rates, in order to minimize the costs relating to implementation of interim rates. The Utility could at least then utilize a Corporate Undertaking to the extent authorized, and some more costly method of security for the remainder.

To the extent the Utility ultimately utilizes an escrow as a method of securing some portion of the potential refunds, we believe the interim order should reflect that the interest that the Utility must pay on any subsequent refunds determined, must be only the amount of interest earned on that escrow account (since the Utility has no access to such funds), rather than the commercial paper rate as is generally applied to monies collected in interim and under a Corporate Undertaking, Bond, or Letter of Credit. We believe that issue should be addressed in the interim order and in the final order as well.

We appreciate the staff's taking into consideration these issues and presenting additional information to the Commission on this interim matter, after review of these additional factors. Please let me know if you need any further information with regard to any of these issues.

Sincerely,

ROSE, SUNDBSTROM & BENTLEY, LLP

  
F. Marshall Deterding  
For The Firm

FMD\tmg

cc: Blanca S. Bayo, Director  
Bart Fletcher, Esquire  
Tricia Merchant, CPA  
Mr. Stephen G. Watford  
Robert C. Nixon, CPA

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## ALOHA UTILITIES, INC.

Seven Springs Water

Interim Rates

Issue 3 - Guarantee

Since we are already into the 10<sup>th</sup> month of 2001, the relevance of the Company's liquidity, equity, profitability, and interest coverage factors at December 31, 1998 and 1999, and for the years then ended, appear to be of little relevance in determining whether Aloha today can financially support a corporate guarantee. As a result, we have looked at these factors at a more current date. We also want to advise you that the corporate guarantee in the amount of \$187,106 relating to the Aloha Gardens refund is no longer a concern since this refund was made to Aloha Gardens customers on September 24, 2001.

### Owners' Equity:

The net worth of the Company at December 31, 2000 represents an amount equal to 12.8 times the amount of the \$192,139 potential refund. This equity represents the financial strength of the utility and, in management's opinion, represents its ability to provide a corporate guarantee for this maximum potential refund amount. If in fact one-half of the total rate increase is deemed to be over earned the net worth of the Company covers this \$96,070 potential refund twenty-five times. Certainly such a potential refund would have an immaterial effect to the financial condition of the Company.

### Liquidity

The balance sheet at June 30, 2001, as shown on Page A-18, 1 of 2 in the MFR reflects a cash balance of \$703,507. This is an historically high balance and has prompted the Public Counsel in their first set of interrogatories to note that the Company has increased its cash balances to a high level as compared to previous cases. This high cash balance provides for liquidity to meet existing and potential liabilities. This cash balance covers the Staff's maximum refund calculation 3.6 times and if the refund totaled one-half of the maximum refund the June 30<sup>th</sup> coverage would be greater than 7 times.

### Profitability

There was a decrease in net income from 1999 to 2000. However, the \$1,077,337 annual increase in revenue requested in this rate case will return the utility to more profitable operations.

Based on the information explained above, management believes the utility is financially strong and sufficiently liquid to guarantee any potential refund with a corporate undertaking.

Aloha Utilities, Inc.  
Response to Staff's Recommendations  
Depreciation Expense  
Docket No. 010503-WU

For the purposes of calculating depreciation expense, using the group method, the net value of plant is depreciated using guideline rates, with additions and retirements depreciated using the half-year convention. For regulatory reporting, new assets are depreciated beginning July 1.

This method was followed for posting depreciation expense on a monthly basis.

The change in accumulated depreciation reflects not only the current period depreciation expense, but also reflects any NARUC retirements as well as any adjustments.

While using the change in accumulated depreciation to calculate the accuracy of depreciation expense is generally accurate, this method does not take into account other factors that affect the balance of accumulated depreciation that do not affect depreciation expense.

In this case, depreciation expense is not the only factor impacting accumulated depreciation. In this case, there were also retirements of assets recorded in July 2000 (half-year for this calendar company) resulting in a lower change in accumulated depreciation than depreciation expense would suggest.

Attached is a copy of Schedule A-10, revised to show the monthly change in accumulated depreciation. As shown on the Schedule, the change in accumulated depreciation from June 2000 to July 2000, was only \$1,093, while the average monthly change from August 2000, through June 2001 was \$24,682.

This average amount of \$24,682 more accurately reflects the change resulting from depreciation expense only, and should be used to calculate the reasonableness of depreciation expense. Therefore,  $\$24,682 \times 12 \text{ months} = \$296,184$ . When compared to the depreciation expense of \$291,237 included in net operating income, this appears reasonable.

We believe the adjustment to depreciation expense of \$18,641, reducing net depreciation to \$45,319 is not necessary and does not reflect the operating conditions of this utility.

Schedule of Water Accumulated Depreciation By Primary Account - Intermediate Period  
Beginning and End of Year Average

Florida Public Service Commission

Company: Aloha Utilities, Inc.; Seven Springs Water Division  
Docket No.: 010503-WU  
Schedule Year Ended: June 30, 2001  
Historic [X] Projected [ ]

Explanation: Provide the month ending balances and thirteen month average of accumulated depreciation for the prior year and the test year by primary account. Also show non-used & useful amounts by account.

Schedule: A-10(A)  
Page 1 of 1  
Preparer: C.JN & W

Recap Schedules: A-1, A-8

No.	(1) Line Account No. and Name	(2) through (13) Actual												(15) 13 Month Average	(16) Non-Used Useful %	(17) Non-Used Amount	
		(2) June 2000	(3) July 2000	(4) August 2000	(5) September 2000	(6) October 2000	(7) November 2000	(8) December 2000	(9) January 2001	(10) February 2001	(11) March 2001	(12) April 2001	(13) May 2001				(14) June 2001
1	INTANGIBLE PLANT																
2	301.1 Organization	\$ 51,478	\$ 51,814	\$ 52,151	\$ 52,487	\$ 52,824	\$ 53,160	53,497	53,833	54,169	54,505	54,841	55,177	55,513	53,400		
3	302.1 Franchises	1,103													85		
4	339.1 Other Plant & Misc. Equipment																
5	SOURCE OF SUPPLY AND PUMPING PLANT																
7	304.2 Structures & Improvements	25,897	26,982	26,268	26,453	26,639	26,824	27,010	27,195	27,380	27,565	27,750	27,935	28,120	27,009		
8	305.2 Collecting and Impounding Reservoirs																
9	306.2 Lake, River and Other Intakes																
10	307.2 Wells and Springs	153,184	151,340	153,420	155,500	167,580	159,059	161,738	163,788	165,834	167,882	169,930	171,978	174,026	161,989		
11	308.2 Infiltration Galleries and Tunnels																
12	309.2 Supply Mains	15,995	14,061	14,184	14,307	14,431	14,554	14,677	14,800	14,923	15,046	15,169	15,292	15,415	14,835		
13	310.2 Power Generation Equipment	604	613	622	631	640	650	659	668	677	686	695	704	713	659		
14	311.2 Pumping Equipment	26,099	26,333	26,567	26,801	27,035	27,269	26,434	25,729	26,024	26,319	26,614	26,909	27,204	26,487		
15	339.2 Other Plant & Misc. Equipment	26	27	27	27	27	28	28	28	28	28	28	28	28	28		
16	WATER TREATMENT PLANT																
18	304.3 Structures & Improvements	4,360	4,412	4,464	4,516	4,568	4,620	4,672	4,724	4,776	4,828	4,880	4,932	4,984	4,672		
19	320.3 Water Treatment Equipment	19,740	19,936	20,132	20,328	20,524	20,720	20,916	21,112	21,308	21,504	21,700	21,896	22,092	20,916		
20	339.3 Other Plant & Misc. Equipment	2,283	2,300	2,318	2,336	2,354	2,372	2,390	2,408	2,426	2,444	2,462	2,480	2,498	2,390		
21	TRANSMISSION AND DISTRIBUTION PLANT																
23	304.4 Structures & Improvements	63,470	63,755	64,042	64,328	64,614	64,901	65,187	65,473	65,759	66,045	66,331	66,617	66,903	65,187		
24	330.4 Distribution Reservoirs and Standpipes	116,494	105,365	105,880	106,395	106,909	107,424	107,939	108,452	108,965	109,359	109,831	110,304	110,777	108,767		
25	331.4 Transmission and Distribution Mains	759,317	767,280	777,259	787,238	797,217	807,195	817,174	827,153	838,232	848,761	858,290	869,819	880,348	818,218		
26	333.4 Services	52,748	53,888	55,051	56,202	57,353	58,504	59,644	60,795	61,946	63,097	64,248	65,399	66,550	59,648		
27	334.4 Meters and Meter Installations	453,015	457,031	461,058	465,085	469,112	473,139	477,165	481,208	485,251	489,294	493,337	497,380	501,423	477,192		
28	335.4 Hydrants	47,165	48,002	48,828	49,664	50,501	51,337	52,185	53,022	53,859	54,696	55,533	56,370	57,207	52,182		
29	339.4 Other Plant & Misc. Equipment	1,283	1,289	1,295	1,300	1,306	1,312	1,318	1,324	1,330	1,336	1,342	1,348	1,354	1,318		
30	GENERAL PLANT																
32	304.5 Structures & Improvements	1,039	461	711	961	1,210	1,460	1,709	2,201	2,693	3,185	3,677	4,169	4,661	2,184		
33	340.5 Office Furniture & Equipment	46,796	47,205	47,615	48,025	48,435	48,845	49,255	49,665	50,075	50,485	50,895	51,305	51,715	49,255		
34	340.5 Computer Equipment	7,623	8,181	8,740	9,298	9,856	10,415	10,973	11,531	12,090	12,648	13,206	13,765	14,323	10,973		
35	341.5 Transportation Equipment	144,195	146,912	149,629	152,345	155,062	157,779	160,496	163,213	165,930	168,647	171,364	174,081	176,798	160,496		
36	342.5 Stores Equipment																
37	343.5 Tools, Shop & Garage Equipment	12,181	10,592	10,767	10,942	11,117	11,292	11,467	11,642	11,817	11,992	12,167	12,342	12,517	11,704		
38	344.5 Laboratory Equipment	5,643	5,606	5,568	5,531	5,494	5,456	5,419	5,382	5,345	5,308	5,271	5,234	5,197	5,020		
39	345.5 Power Operated Equipment	13,199	13,324	13,449	13,575	13,700	13,825	13,951	14,076	14,201	14,326	14,451	14,576	14,701	13,950		
40	346.5 Communication Equipment	28,859	29,952	29,045	29,138	29,231	29,324	29,416	29,447	29,478	29,509	29,540	29,571	29,602	29,316		
41	347.5 Miscellaneous Equipment	608	634	659	684	710	735	761	786	811	836	861	886	911	760		
42	348.5 Other Tangible Plant																
43	TOTAL	\$ 2,054,303	\$ 2,055,396	\$ 2,079,869	\$ 2,104,337	\$ 2,128,809	\$ 2,153,279	\$ 2,175,679	\$ 2,200,882	\$ 2,226,086	\$ 2,251,289	\$ 2,276,492	\$ 2,301,696	\$ 2,326,899	\$ 2,179,618		\$ -
			\$ 1,093	\$ 24,473	\$ 24,468	\$ 24,472	\$ 24,470	\$ 22,400	\$ 25,203	\$ 25,204	\$ 26,203	\$ 25,203	\$ 25,204	\$ 25,203			

Company: Aloha Utilities, Inc.; Seven Springs Water Division  
 Docket No.: 010503-WU  
 Schedule Year Ended: June 30, 2001  
 Historic [X] Projected [ ]

Schedule: B-13 (A)  
 Page 1 of 1  
 Preparer: CJN & W  
 Recap Schedules: B-1

Explanation: Provide a schedule of test year non-used and useful depreciation expense by primary account

No.	(1) Line Account No. and Name	(2) Test Year 12/31/01	(3) Adjustments	(4) Adjusted Balance	(5) Non-Used & Useful %	(6) Non-Used & Amount
1	INTANGIBLE PLANT					
2	301.1 Organization	4,035		4,035		
3	302.1 Franchises	-				
4	339.1 Other Plant & Misc. Equipment	-				
5	SOURCE OF SUPPLY AND PUMPING PLANT					
6	303.2 Land & Land Rights					
7	304.2 Structures & Improvements	2,223		2,223		
8	305.2 Collect. & Impound. Reservoirs	-				
9	306.2 Lake, River & Other Intakes	-				
10	307.2 Wells & Springs	20,842		20,842		
11	308.2 Infiltration Galleries & Tunnels	-				
12	309.2 Supply Mains	1,714		1,714		
13	310.2 Power Generation Equipment	109		109		
14	311.2 Pumping Equipment	3,539		3,539		
15	339.2 Other Plant & Misc. Equipment	2		2		
16	WATER TREATMENT PLANT					
17	303.3 Land & Land Rights					
18	304.3 Structures & Improvements	624		624		
19	320.3 Water Treatment Equipment	2,352		2,352		
20	339.3 Other Plant & Misc. Equipment	215		215		
21	TRANSMISSION & DISTRIBUTION PLANT					
22	303.4 Land & Land Rights					
23	304.4 Structures & Improvements	3,433		3,433		
24	330.4 Distr. Reservoirs & Standpipes	5,675		5,675		
25	331.4 Transm. & Distribution Mains	121,031		121,031		
26	333.4 Services	13,802		13,802		
27	334.4 Meters & Meter Installations	48,408		48,408		
28	335.4 Hydrants	10,042		10,042		
29	339.4 Other Plant & Misc. Equipment	71		71		
30	GENERAL PLANT					
31	303.5 Land & Land Rights					
32	304.5 Structures & Improvements	3,622		3,622		
33	340.5 Office Furniture & Equipment	4,920		4,920		
34	340.5 Computer Equipment	6,700		6,700		
35	341.5 Transportation Equipment	32,603		32,603		
36	342.5 Stores Equipment	-				
37	343.5 Tools, Shop & Garage Equipment	2,339		2,339		
38	344.5 Laboratory Equipment	754		754		
39	345.5 Power Operated Equipment	1,502		1,502		
40	346.5 Communication Equipment	377		377		
41	347.5 Miscellaneous Equipment	303		303		
42	348.5 Other Tangible Plant					
42	TOTAL	291,237	-	291,237		-
43	LESS: AMORTIZATION OF CIAC	(227,277)	-	(227,277)		-
44	NET DEPRECIATION EXPENSE - WATER	\$ 63,960	\$ -	\$ 63,960		\$ -
45	Note: All plant is 100% used and useful					