



Public Service Commission

CAPITAL CIRCLE OFFICE CENTER • 2540 SHUMARD OAK BOULEVARD
TALLAHASSEE, FLORIDA 32399-0850

-M-E-M-O-R-A-N-D-U-M-

DATE: SEPTEMBER 10, 1998

TO: DIRECTOR, DIVISION OF RECORDS AND REPORTING (BAY) *BAY*

FROM: DIVISION OF WATER AND WASTEWATER (JOHNSON, REDEMANN) *REDEMANN*
DIVISION OF LEGAL SERVICES (FLEMING) *FLEMING*

RE: DOCKET NO. 971456-WS - APPLICATION FOR TRANSFER OF
CERTIFICATE NOS. 524-W AND 459-S IN PASCO COUNTY FROM
B.D.C., INC. D/B/A TIMBERWOOD UTILITIES TO ARBOR OAKS I,
LLC AND ARBOR OAKS II, LLC BOTH DELAWARE LIMITED LIABILITY
COMPANIES D/B/A TIMBERWOOD UTILITIES.
COUNTY: PASCO

AGENDA: 9/22/98 - REGULAR AGENDA - PROPOSED AGENCY ACTION FOR
ISSUES NOS. 3, 4 AND 5 - INTERESTED PERSONS MAY
PARTICIPATE

CRITICAL DATES: NONE

SPECIAL INSTRUCTIONS: NONE

FILE NAME AND LOCATION: S:\PSC\WAW\WP\971456.RCM

CASE BACKGROUND

Timberwood Utilities, (Timberwood, Seller, or utility) is a Class C utility which provides water and wastewater service in Pasco County. According to the utility's 1997 Annual Report, it serves 160 water customers and 158 wastewater customers. In 1997, the utility had annual operating revenues of \$12,266 for water and \$24,532 for wastewater. The net operating losses were (\$17,701) and (\$10,409) for water and wastewater, respectively. The utility's facilities consist of one water treatment plant, one water transmission and distribution system, one wastewater treatment plant, and one wastewater collection system.

On November 5, 1997, Timberwood Utilities filed an application to transfer Certificates Nos. 524-W and 459-S from Timberwood Utilities to Arbor Oaks I, LLC and Arbor Oaks II, LLC of the

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FPSC-RECORDS/REPORTING

DOCKET NO. 971456-WS

DATE: SEPTEMBER 10, 1998

Delaware Limited Liability Companies (Arbor Oaks or Buyer) pursuant to Section 367.071, Florida Statutes. Arbor Oaks purchased the Arbor Oaks Mobile Home Park which included the water and wastewater utility assets. The purchase price for the property, including the Timberwood Utilities was \$3,510,000.

Section 367.071, Florida Statutes, states in part that no utility shall sell, assign, or transfer its certificate of authorization, facilities or any portion thereof, or majority organizational control without approval of the Commission. According to the application, the parties closed on the sale of the utility on or before October 15, 1997, which is discussed further in Issue 1. The following is staff's recommendation regarding the requested transfer.

DOCKET NO. 971456-WS

DATE: SEPTEMBER 10, 1998

DISCUSSION OF ISSUES

ISSUE 1: Should Timberwood Utilities be ordered to show cause, in writing within 21 days, why it should not be fined for violation of Section 367.071, Florida Statutes?

RECOMMENDATION: No. Show cause proceedings should not be initiated. (FLEMING)

STAFF ANALYSIS: As stated in the case background, Timberwood is in apparent violation of Sections 367.071, Florida Statutes, which states, in part, "No utility shall sell, assign, or transfer its certificate of authorization, facilities or any portion thereof . . . without determination and approval of the commission that the proposed sale, assignment, or transfer is in the public interest." Timberwood and Arbor Oaks entered into a Bill of Sale on October 15, 1997, whereby Arbor Oaks gained operational control of the facilities of the utility. Arbor Oaks has been operating the system providing water and wastewater service to customers of the utility since that time.

Section 367.161(1), Florida Statutes, authorizes the Commission to assess a penalty of not more than \$5,000 for each offense, if a utility is found to have knowingly refused to comply with, or have willfully violated, any provision of Chapter 367, Florida Statutes. Timberwood appears to have violated Section 367.071(1), Florida Statutes, by failing to obtain the approval of the Commission before transferring to Arbor Oaks. While staff does not have reason to believe that the utility intended to violate this statute, its act was "willful" in the sense intended by Section 367.161, Florida Statutes. See Order No. 24306, issued April 1, 1991, in Docket No. 890216-TL titled In Re: Investigation Into The Proper Application of Rule 25-14.003, F.A.C., Relating To Tax Savings Refund for 1988 and 1989 For GTE Florida, Inc., the Commission, having found that the company had not intended to violate the rule, nevertheless found it appropriate to order it to show cause why it should not be fined, stating that "'willful' implies an intent to do an act, and this is distinct from an intent to violate a statute or rule." *Id.* at 6. Utilities are charged with the knowledge of the Commission's rules and statutes. Additionally, "[i]t is a common maxim, familiar to all minds that 'ignorance of the law' will not excuse any person, either civilly or criminally." Barlow v. United States, 32 U.S. 404, 411 (1833).

DOCKET NO. 971456-WS

DATE: SEPTEMBER 10, 1998

Timberwood failed to obtain Commission approval before entering into the Bill of Sale and turning the system over to Arbor Oaks to operate. However, the Bill of Sale does make the closing of the sale contingent upon Commission approval of the sale and issuance of certificates to Arbor Oaks. Failure of Timberwood to obtain prior approval of the Commission appears to be due to its belief that because the sale had not closed, it was not in violation of Section 367.071, Florida Statutes.

Staff has reviewed the application and the sales agreement and, although Arbor Oaks is operating the utility, closing of the sale is conditioned upon Commission approval. Therefore, staff does not believe that the apparent violation of Section 367.071, Florida Statutes, rises in these circumstances to the level of warranting initiation of show cause proceedings. Staff recommends that the Commission not order Timberwood to show cause for failing to obtain Commission approval prior to the transfer to Arbor Oaks. This recommendation is consistent with Order Nos. PSC-98-0514-FOF-SU, issued April 15, 1998 in Docket No. 951008-SU, PSC-98-0371-FOF-WS, issued March 6, 1998 in Docket No. 961014-WS, and PSC-98-0024-FOF-WU, issued January 5, 1998 in Docket No. 970762-WU.

DOCKET NO. 971456-WS

DATE: SEPTEMBER 10, 1998

ISSUE 2: Should the transfer of Water Certificate No. 524-W and Wastewater Certificate No. 459-S from Timberwood Utilities to Arbor Oaks be granted?

RECOMMENDATION: Yes, the transfer of Certificate Nos. 524-W and 459-S from Timberwood Utilities to Arbor Oaks should be approved. (JOHNSON, REDEMANN)

STAFF ANALYSIS: As stated in the case background, Arbor Oaks applied for a transfer of Water Certificate No. 524-W and Wastewater Certificate No. 459-S in Pasco County to Arbor Oaks on November 5, 1997. Except as previously discussed in Issue 1 the application is in compliance with the governing statute, Section 367.071, Florida Statutes, and other pertinent statutes and administrative rules concerning an application for transfer. The application contains \$750, which is the correct filing fee pursuant to Rule 25-30.020, Florida Administrative Code.

Rule 25-30.037(2)(q), Florida Administrative Code, requires a utility to provide proof of ownership of the land upon which its facilities are located. The application contained a Warranty Deed that covers the entire Mobile Home Park. The owners of the Mobile Home Park also own the utility.

In addition, the application contains proof of compliance with the noticing provisions set forth in Rule 25-30.030, Florida Administrative Code, including notice to the customers of the system being transferred. A description of the territory served by the utility is appended to this memorandum as Attachment A.

Arbor Oaks has indicated that it has the technical and financial ability to operate the system. With regard to the purchaser's technical ability, Arbor Oaks is a Limited Liability Company owned by Mr. and Mrs. Kurt Wallach, who have over twenty years of experience in owning and managing mobile home communities. The company will have a licensed operator for the utility. Regarding the purchaser's financial ability, Arbor Oaks supplied a closing financial statement to staff which shows that it has cash invested (equity) in the project equal to \$1,249,738. The statement indicates that approximately 36% of the company's total acquisition costs was paid by Arbor Oaks. While staff does have some concerns about the liquidity of Arbor Oaks, we believe the owners possess the overall financial ability to operate the utility. As stated previously, the annual report for 1997 shows that the consolidated annual operating revenue for the system was \$36,798. Staff believes that the assets of the new owner should be adequate to insure the continued operations of the utility.

DOCKET NO. 971456-WS

DATE: SEPTEMBER 10, 1998

The application states that the Company's representative has performed a reasonable investigation of the Timberwood utility systems. The facilities appear to be in satisfactory condition and in compliance with all applicable standards set by the Florida Department of Environmental Protection (DEP). Staff has contacted the DEP and learned that there are no outstanding notices of violation against the utility.

The application contains a copy of the Bill of Sale and Assignment Agreement which includes the purchase price, terms of payment, and a list of the assets purchased and the liabilities assumed. According to the application, the purchase price of the utility is included in the purchase price paid for the Arbor Oaks Mobile Home Park, which was purchased for the sum of \$3,510,000 cash. Arbor Oak's has allocated \$629,200 of the purchase price for the utility system. The Utility constitutes approximately 20% of the purchase price. The Buyer financed the purchase with cash and proceeds for a first mortgage loan from Heller Financial, Inc., for the amount of \$2,360,000. This mortgage loan will encumber the real and personal property within the community, including the water and wastewater utility facilities. Based on the application, there are no developer agreements which the buyer is obligated to assume or fulfill. Also, the utility's 1997 regulatory assessment fees and annual report have been filed. Since ownership of the mobile home park was transferred to Arbor Oaks on October 15, 1997, it will be responsible for the 1998 regulatory assessment fees. By letter dated September 8, 1998, Arbor Oaks confirmed that it would be responsible for the 1998 regulatory assessment fees and the filing of the 1998 annual report. In addition, there are no customer deposits, guaranteed revenue, contracts, developer agreements, customer advances, or debts of the utility independent of the first mortgage loan that will be placed upon the property in connection with the purchase.

Based on the application the transfer is in the public interest for the following reasons: (1) the Buyer has a continuing interest in the system due to the joint ownership of the Arbor Oaks Mobile Home Park and utility, (2) the Buyer will continue to employ a licensed operator for the utility and the Buyer will continue to utilize the name Timberwood Utilities, so that from the customer perspective, no changes in the operation of the system will be readily apparent, and (3) the Buyer has the financial resources to provide real and significant benefits to the utility customers as the utility's capital or operational needs demand. Therefore, staff recommends that the transfer of Timberwood Utilities Water Certificate No. 524-W and Wastewater Certificate No. 459-S is in the public interest and should be approved to serve the territory described in Attachment A.

DOCKET NO. 971456-WS
DATE: SEPTEMBER 10, 1998

ATTACHMENT A

TIMBERWOOD UTILITIES

PASCO COUNTY

TERRITORY DESCRIPTION

WATER AND WASTEWATER SERVICE AREA

The following described lands located in a portion of Section 9, Township 26 South, Range 21 East, Pasco County, Florida:

Section 9

The SW 1/4 of the NE 1/4 of the NW 1/4 and the S 1/2 of the SE 1/4 of the NE 1/4 of the NW 1/4 and the N 1/2 of the N 1/2 of the SE 1/4 of the NW 1/4.

DOCKET NO. 971456-WS

DATE: SEPTEMBER 10, 1998

ISSUE 3: What is the rate base of Timberwood Utilities, at the time of transfer?

RECOMMENDATION: The rate base, which for transfer purposes reflects the net book value, is \$6,254 for the water and \$69,681 for wastewater system as of January 31, 1998. (JOHNSON)

STAFF ANALYSIS: According to the company, the net book value of the system was \$7,314 for the water and \$68,502 for wastewater system as of January 31, 1998. Rate base for the water and wastewater system was last established in Docket No. 900749-WS, which was a staff assisted rate case. According to Order No. 24640 issued on June 10, 1991 in that docket, rate base for the water system was \$9,229 and for the wastewater system was \$92,836, as of November 30, 1990.

Staff conducted an audit of the books and records of the utility to determine the rate base (net book value) as of January 31, 1998. The rate base was determined from the company's historical records and supporting source documentation. The utility's books and records were maintained in substantial compliance with Commission directives. The audit report contained three audit exceptions that primarily related to overstated plant and unsupported plant additions. Arbor Oaks, purchased the mobile home community along with the utility assets and allocated \$629,200 as the recorded price for the utility. Based upon the actions of the utility not filing a response to the audit report, staff is assuming the utility is in agreement with the finding in audit report. The following adjustments were made by staff as a result of the audit.

UTILITY PLANT IN SERVICE

Staff is recommending that water plant in service should be reduced by a total of (\$1,820) and wastewater plant in service should be increased by a total of \$1,754. The total reduction to the related accumulated depreciation is \$760 for water and the wastewater is increased by \$575. Staff recommends that the following adjustments should be made.

The first adjustment involves the overstatement of the plant account. The Arbor Oaks Company is composed of three operating divisions, which are Timberwood Water, Timberwood Wastewater, and Arbor Oaks Mobile Home Park. All three divisions share office space and office equipment in a small room located in the mobile home community's clubhouse. The company allocates telephone and

DOCKET NO. 971456-WS

DATE: SEPTEMBER 10, 1998

wastewater collections services equally among all three operating divisions. The allocation of costs to all operating divisions and non-utility affiliates that use the facilities is consistent with Commission Order PSC-92-1197-FOF-EI, which required the allocation of company assets when the non-utility affiliates use of such assets is substantial. According to the utility's records, \$8,225 in additions for office equipment was allocated equally between the water and wastewater divisions (\$4,113 each). Because there is equal access and use of the office and equipment, the \$8,225 for office equipment should be allocated equally among the three operating divisions. Therefore, the utility should reduce the office equipment accounts by \$1,371 for each of the systems. Additionally, the utility should reduce the respective accumulated depreciation accounts by \$549.

In addition, the plant account was overstated due to missing office furniture. Some of the utility plant in service assets identified as being transferred in the sales contract were located by the Staff Auditor. The seller stated that all assets were being transferred, that were listed in the application. Because the missing assets were never located, the company should retire the assets by reducing the plant by \$449 and the respective accumulated depreciation accounts by \$449. The combined adjustment for correcting overstated plant results in a total decrease of \$1,820 to each; the water plant and the wastewater plant account and a total reduction of \$998 for the related accumulated depreciation accounts.

The second adjustment involves unsupported wastewater plant and supported plant not recorded. In 1991, the utility recorded \$426 for additional treatment and disposal equipment. By January 31, 1998, this plant had depreciated with an accumulated depreciation of \$173. The utility was unable to provide invoices for the this equipment. The wastewater plant account should be reduced by \$426, to remove unsupported plant and the related accumulated depreciation of \$173. The auditor found an invoice for \$4,000 for a chlorine contact chamber that wasn't recorded in the utility's books. Because there is support for this equipment, it should be recorded by increasing the wastewater plant account by \$4,000 and the related accumulated depreciation by \$156. The net affect of removing the unsupported plant and recording the supported plant is a total increase of \$3,574 to the wastewater plant account and a reduction of \$17 for the related accumulated depreciation.

The third adjustment is necessary because the utility did not follow prior Commission Order No. 24640, issued November 30, 1990, which established the balances for organization cost, plant account

DOCKET NO. 971456-WS

DATE: SEPTEMBER 10, 1998

354-structures and improvements, accumulated amortization, and accumulated depreciation and the prescribed depreciation rates for the accounts. The utility used lower depreciation rates than was required by that order. The Commission authorized the prescribed rate of 3.17 for the amortization of Account 304-organization cost and a prescribed rate of 3.70 for the depreciation of Account 354-structures & improvements. Because the utility did not follow Commission Order No. 24640, issued November 30, 1990, it is in violation of the Rule 25-30.140 (4)(b) that requires all utilities to maintain depreciation rates as prescribed by the Commission. Staff recommends that the utility increase its accumulated amortization balance for account 301(Organization costs) by (\$238) and its accumulated depreciation balance for account 354 (structures and improvements) by (\$1,590).

ACCUMULATED DEPRECIATION

Accumulated depreciation was recalculated for water and wastewater to correspond to the audit adjustments to utility plant in service discussed above. The total recommended adjustment to accumulated depreciation is \$760 decrease for the water system and \$575 increase for the wastewater system.

RATE BASE

Staff's calculation of rate base for water and wastewater is shown on Schedules Nos. 1 and 3, respectively. Adjustments to rate base are itemized on Schedules Nos. 2 and 4, for water and wastewater, respectively. Based on the adjustments set forth herein, staff recommends that rate base for Timberwood Utilities be established as \$6,254 for the water system and \$69,681 for the wastewater system as of January 31, 1998. This rate base calculation is used purely to establish the net book value of the property being transferred and does not include the normal ratemaking adjustments of working capital calculations and used and useful adjustments.

DOCKET NO. 971456-WS
DATE: SEPTEMBER 10, 1998

TIMBERWOOD UTILITIES

SCHEDULE OF WATER RATE BASE

As of January 31, 1998

<u>DESCRIPTION</u>	<u>BALANCE PER UTILITY</u>	<u>STAFF ADJUSTMENTS</u>	<u>BALANCE PER STAFF</u>
Utility Plant in Service	\$ 65,883	(\$1,820)	(1) \$64,063
Land	0	0	0
Plant Held for Future Use	0	0	0
Accumulated Depreciation	(20,148)	760	(2) (19,388)
Contributions-in- aid-of-Construction	(53,583)	0	(53,583)
CIAC Amortization	<u>15,162</u>	<u>0</u>	<u>15,162</u>
TOTAL	<u>\$ 7,314</u>	<u>\$(1,060)</u>	<u>\$ 6,254</u>

DOCKET NO. 971456-WS
DATE: SEPTEMBER 10, 1998

SCHEDULE NO. 2

TIMBERWOOD UTILITIES WATER SERVICE

SCHEDULE OF WATER RATE BASE ADJUSTMENTS

<u>EXPLANATION</u>	<u>ADJUSTMENT</u>
Utility Plant in Service	
A. Reduction to plant to reflect reallocated share	(\$1,371)
B. Reduction to reflect retired plant	<u>(\$449)</u>
TOTAL (1)	<u>(\$1,820)</u>
Accumulated Depreciation	
A. Adjustment related to reallocated plant cost	\$549
B. Adjustment related to retired plant	\$449
C. Adjustment related to retired plant	<u>(\$238)</u>
TOTAL (2)	<u>\$760</u>

DOCKET NO. 971456-WS
DATE: SEPTEMBER 10, 1998

SCHEDULE NO. 3

TIMBERWOOD UTILITIES

SCHEDULE OF WASTEWATER RATE BASE

As of January 31, 1998

<u>DESCRIPTION</u>	<u>BALANCE PER UTILITY</u>	<u>STAFF ADJUSTMENTS</u>	<u>BALANCE PER STAFF</u>
Utility Plant in Service	\$193,478	\$1,754 (1)	\$195,232
Land	10,152	0	2,610
Accumulated Depreciation	(71,903)	(575) (2)	(72,478)
Contributions-in- aid-of-Construction	(95,165)	0	(95,165)
CIAC Amortization	<u>31,940</u>	<u>0</u>	<u>31,940</u>
TOTAL	<u>\$ 68,502</u>	<u>\$ 1,179</u>	<u>\$69,681</u>

DOCKET NO. 971456-WS
DATE: SEPTEMBER 10, 1998

SCHEDULE NO. 2

TIMBERWOOD UTILITIES

SCHEDULE OF WASTEWATER RATE BASE ADJUSTMENTS

<u>EXPLANATION</u>	<u>ADJUSTMENT</u>
Utility Plant in Service	
A. Reduction to plant to reflect reallocated share	(\$1,371)
B. Reduction to reflect retired plant	(\$449)
C. Reduction to reflect unsupported plant	(\$426)
D. Increase to reflect supported plant	<u>\$4,000</u>
TOTAL (1)	<u>\$1,754</u>
Accumulated Depreciation	
A. Adjustment related to reallocated plant	\$549
B. Adjustment related to retired plant	\$449
C. Adjustment related to unsupported plant	\$173
D. Adjustment related to supported plant	(\$156)
E. Adjustment to reflect the prescribe depreciation rate	<u>(\$1,590)</u>
TOTAL (2)	<u>(\$575)</u>

DOCKET NO. 971456-WS
DATE: SEPTEMBER 10, 1998

ISSUE 4: Should a positive acquisition adjustment be approved?

RECOMMENDATION: No, a positive acquisition adjustment should not be included in the calculation of rate base for transfer purposes. (JOHNSON)

STAFF ANALYSIS: An acquisition adjustment results when the purchase price differs from the rate base for transfer purposes. The acquisition adjustment resulting from the transfer of Timberwood Utilities would be calculated as follows:

Purchase Price:	\$ 629,200
Staff Calculated Rate Base:	<u>75,935</u>
Positive Acquisition Adjustment:	<u>\$553,265</u>

In the absence of extraordinary circumstances, it has been Commission practice that a subsequent purchase of a utility system at a premium or discount shall not affect the rate base calculation. The circumstances in this exchange do not appear to be extraordinary. Although there appears to be a substantial positive acquisition adjustment, the purchase price of the utility was an allocated amount of the total price for the entire mobile home park. Arbor Oaks estimated the utility to be valued at 20% of the total purchase price. However, upon further conversation with the utility's attorney it was stated that this was an arbitrary allocation and an estimate, and no justification for this allocation could be provided to staff. Further, an acquisition adjustment was not requested by the applicant. Also, field audit staff stated that they did not recommend an acquisition adjustment at this time. Therefore, staff recommends that a positive acquisition adjustment not be included in the calculation of rate base.

DOCKET NO. 971456-WS
DATE: SEPTEMBER 10, 1998

ISSUE 5: Should the rates and charges approved for this utility be continued?

RECOMMENDATION: Yes, the rates and charges approved for this utility system should be continued. The tariff reflecting the change in ownership should be effective for services rendered or connections made on or after the stamped approval date. (JOHNSON)

STAFF ANALYSIS: The utility's approved water and wastewater rates were effective February 1, 1997, in a administrative price index and pass through proceeding. The utility's approved rates and charges are as follows:

Monthly Service Rates for Water

Residential and General Service

Base Facility Charge:

Meter Size:

5/8" x 3/4"	\$ 3.07
1"	\$ 4.59
1 1/2"	\$ 7.66
2"	\$ 15.32
3"	\$ 24.51
4"	\$ 49.01
6"	\$ 76.58
8"	\$153.16
Gallagege Charge per 1,000 gallons	\$ 2.30

DOCKET NO. 971456-WS
DATE: SEPTEMBER 10, 1998

Miscellaneous Service Charges

Initial Connection Fee	\$ 15.00
Normal Reconnection Fee	\$ 15.00
Violation Reconnection Fee	\$ 15.00
Premises Visit Fee (in lieu of disconnection)	\$ 10.00

Service Availability Charges

Meter Installation Fee:	
5/8" x 3/4" Meter Size	\$100.00
1"	100.00
1 1/2"	100.00
2"	Actual Cost
Over 2"	Actual Cost
Customer Connection (Tap-in) Charge	Actual Cost

DOCKET NO. 971456-WS
DATE: SEPTEMBER 10, 1998

Monthly Service Rates for Wastewater

Residential

Base Facility Charge:

Meter Size:

5/8" x 3/4"	\$ 10.32
Full 3/4"	\$ 15.48
1"	\$ 25.79
1 1/2"	\$ 51.59
2"	\$ 82.54
3"	\$165.10
4"	\$257.96
6"	\$515.91

Gallon age Charge
per 1,000 gallons \$ 5.08
(capped At 6,000 Gallons)

General Service

Base Facility Charge:

Meter Size:

5/8" x 3/4"	\$ 10.32
Full 3/4"	\$ 15.48
1"	\$ 25.79
1 1/2"	\$ 51.59
2"	\$ 82.54
3"	\$165.10
4"	\$257.96
6"	\$515.91

Gallon age Charge
per 1,000 gallons \$ 6.09

DOCKET NO. 971456-WS
DATE: SEPTEMBER 10, 1998

Miscellaneous Service Charges

Initial Connection Fee	\$ 15.00
Normal Reconnection Fee	\$ 15.00
Violation Reconnection Fee	Actual Cost
Premises Visit Fee (in lieu of disconnection)	\$ 10.00

Rule 25-9.044(1), Florida Administrative Code, provides that:

In cases of change of ownership or control of a utility which places the operation under a different or new utility...the company which will thereafter operate the utility business must adopt and use the rates, classification and regulations of the former operating company (unless authorized to change by the Commission)...

The assignees have not requested a change in the rates and charges of the utility, and staff sees no reason to change them at this time. Accordingly, staff recommends that the utility continue operations under the existing approved rates and charges.

DOCKET NO. 971456-WS

DATE: SEPTEMBER 10, 1998

ISSUE 6: Should this docket be closed?

RECOMMENDATION: Yes, this docket should be closed if no timely protests are filed to the proposed agency action issues. (FLEMING)

STAFF ANALYSIS: If there are no timely protests filed by a substantially affected person to the proposed agency action issues (Issues Nos. 3, 4 and 5), no further action will be required and the docket should be closed.