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October 4, 2000

Rex Carpenter
General Manager
Nebraska Rural Electric Association
800 South 13th St.
Box 82048
Lincoln, NE 68501

Re: Merger/Rates

Dear Rex:

You have asked me to comment on whether the surviving public power district "District A," in a proposed consolidation or merger with another public power district "District B," can charge higher rates to the former customers of District B, based on the pre-existing debt of District B?

As I understand the facts, District A has no debt and lower rates than District B. District B has higher rates because of a preexisting debt. It is proposed that after the consolidation or merger, the customers of District A would constitute a separate rate class or classes, and the Customers of District B would constitute a separate rate class or classes. The former customers of District B would be allocated the pre-existing debt service and continue to pay the higher rate until the debt is paid in full. The rates proposed after the merger would be the current rates that District A and District B are now charging its respective customers.

Neb. Rev. Stat. § 70-655 requires a public power district board to fix adequate rates "which rates, tolls, rents and charges shall be fair, reasonable, nondiscriminatory, and so adjusted as in a fair and equitable manner to confer and distribute among the users and consumers of commodities and services furnished or sold by the district the benefits of a successful and profitable operation and conduct of the business of the district."

The legal question presented is whether separate classes of rates for customers of District A and District B after the merger is fair, reasonable and nondiscriminatory. A similar question was presented in *McGinley v. Wheat Belt Public Power District,* 214 Neb. 178, 332 N.W.2d 915 (1983). In *Wheat Belt,* the power district attempted to pass along to new customers the higher cost of a new power source. The power district's reasoning was that it had to obtain a more costly power source in order to provide service to the new customers and the existing customers should not have to pay for the new power source. The Nebraska Supreme Court rejected the power district's rate classification as being discriminatory, and stated among other things, the following:

1. Persons receiving similar service under similar circumstances cannot be charged for such service in an arbitrary, designed, dissimilar manner.

2. A dissimilar rate may not be imposed for similar service solely on the basis that the additional source of power or energy is more costly that previous sources. All of the sources must properly be blended into a rate which results in all customers obtaining the same service under the same conditions being charged the same rate.

3. While it is true than an entire class may be charged a rate other or different than another class, if indeed the increased cost of providing the service can be identified with that class, the class itself may not be subdivided dependent solely upon the date on which the service was provided.

In light of the decision in *Wheat Belt,* the question to be analyzed here is whether the former customers of District B, after the merger and at the time that District A begins providing service to both the customers of District A and District B, would be customers receiving similar service under similar circumstances as the former customers of District A. If the answer is yes, then the separate rate classifications are discriminatory.

There is an argument that serving the former customers of District B is more costly after the merger because of the pre-existing debt service associated with the former customers of District B. However, I am not certain that this is a change in circumstances sufficient to warrant a separate rate classification.

On the other hand, there is the argument that the customers of former District A and District B, after the merger, are receiving the same service under the same circumstances and it is unreasonable and discriminatory to charge the debt service to the former customers of District B since District A and District B are now the same entity. A Court might well say that the total costs of the two districts should be blended into a rate apportioned equally among all of the customers of the District. This is the rational that the Court followed in *Wheat Belt.* It seems to me, that charging an increased rate to new customers based on a more costly power supply is very similar to charging an increased rate to one class of customers based on pre-existing debt. In *Wheat Belt,* the power district argued that the new customers were receiving service under different circumstances, i.e. the higher cost of power. The Court rejected this argument. In the case here, although the facts are somewhat different, a merger vs. new customers, essentially the same argument would have to be made. The argument is that the former customers of District B would be receiving service under different circumstances, i.e. the pre-existing debt service. It

cannot be said with certainty that a Court would find that the pre-existing debt service is a circumstance that warrants a higher rate to former customers of District B.

An additional problem is the language in *Wheat Belt* that states "the class itself may not be subdivided dependent solely upon the date on which the service was provided." As I understand the facts, District A would propose to subdivide the class on the date that the merger became effective, which appears to be contrary to this language.

Because of the uncertainty as to whether subdividing the customers into different classes for rate purposes based on the pre-existing debt of District B would be permissible under *Wheat Belt,* I would advise against it.

Sincerely,

FOR THE FIRM

Steven G. Seglin

SGS:rrk