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September 7, 2005

Jay Holmquist, General Manager
Nebraska Rural Electric Association
800 South 13th Street
P.O. Box 82048
Lincoln, NE 68501

Re: Conditions on Irrigation Service

Dear Jay:

INTRODUCTION

Because of the rising costs of diesel fuel and natural gas, many farmers who are presently using these types of fuel are evaluating whether to change to electric power.

If a public power district decides to serve a large number of the farmers who wish to change to electric power, it may require a significant expenditure of district funds in order to upgrade their electric systems to handle the increased electrical load.

QUESTION PRESENTED

You have asked what conditions, if any, may be imposed on new electric irrigation services in light of the significant cost expenditures required to be made by public power districts in order to upgrade their electric systems to accommodate the increase in the electrical load. Specifically, may these customers be

1. Charged a higher rate;

2. Required to have their electric load controlled; or

3. Required to pay for the extension of the electric system to their irrigation service.

BRIEF ANSWER

New customers may not be charged a higher rate than existing customers if they are in the same rate classification. New customers may not be required to control their electric loads, unless all customers in the same class are required to control their loads. New customers may be required to pay for the extension of the electric system to their irrigation service, if all customers in the same class are required to pay for line extensions.

ANALYSIS

Neb. Rev. Stat. § 70-655 requires public power districts to set rates that are "fair, reasonable and non-discriminatory." In *McGinley v. Wheat Belt P .P. Dist.,* 214 Neb. 178, 184, 332 N.W. 2d 915 (1983) the Nebraska Supreme Court affirmed the fair, reasonable and non-discriminatory standard for setting rates by a public power district's board of directors. In *Bard v. Cox Cable of Omaha, Inc.,* 226 Neb. 880, 885, 416 N.W. 2d 4 (1987) the Nebraska Supreme held that courts have the power to review legislatively set rates to determine whether they are so arbitrary and unreasonable as to be confiscatory and thus unconstitutionally take property without due process of law.

In *Reimer v. City of O'Neill,* 189 Neb. 151, 153, 201 N.W.2d 706 (1972) the Court held that a public power district may classify users for rate purposes if the classification is reasonable and not unjustly discriminatory. The Court has also held in *Erickson v. Metropolitan Utilities Dist.,* 171 Neb. 654, 107 N.W.2d 324 (1961) that a water district which furnishes water to the public at large may classify users and charge different rates to different classes provided that the charges are reasonable and not discriminatory. The court also stated that those engaged in serving water to the public generally may not unreasonably or unjustly discriminate either in service or rates among patrons.

The Court's analysis of the facts in *McGinley v. Wheat Belt P. P. Dist., supra,* are particularly pertinent to answering the questions presented here. Wheat Belt is one of the then 25 members of Tri-State Generation & Transmission Association ("Tri-State"), a multi-state wholesale distributor of electric energy. Due to increasing load growth of its members caused primarily by the increased use of seasonal irrigation, Tri-State constructed a peak generating facility that would provide energy during periods of high seasonal demand. In February of 1975, Tri-State informed Wheat-Belt that a surcharge or ratchet would be charged all customers of Tri-State including Wheat-Belt and Wheat-Belt would be assessed on the basis of its summer peak demand. Wheat-Belt considered three alternatives to deal with the imposed ratchet:

(1) Refuse to add new irrigation;

(2) Allocate the ratchet equally among all irrigation customers; or

(3) Create two classes of irrigation customers based on the date the customer request service.

Wheat-Belt chose the last alternative based on the notion that the new customers were causing the increased summer peak demand thereby causing the imposition of the ratchet.

The new class of customers sued claiming that the increased rate for them was discriminatory on the ground that they were receiving the same service as the other irrigation customers who paid a lower rate.

The court analyzed the plaintiffs' claim of unjust discrimination by stating the following:

> While it is true that an entire class may be charged a rate other or different than another class, the class itself may not be subdivided dependent solely upon the date on which the service was provided. Were this to be otherwise, then a utility could impose upon a single, newly constructed building the entire cost of obtaining a new source of energy required by reason of the addition of the building to the service, even though the nature of the service is in all respects identical to all other commercial customers in the community. Such a rate formula is beyond comprehension. In *Erickson v. Metropolitan Utils. Dist.,* 171 Neb. 654, 667-68, 107 N.W.2d 324, 331, (1961), we said: 'The rule forbidding unjust discrimination has been variously expressed: The charges must be equal to all for the same service under like circumstances. . .'
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> This is not a case in which Wheat Belt has been compelled to expend capital funds to extend service to customers not previously receiving service. . . For purposes of allocating the cost of replacing original facilities, it is arbitrary and irrational to distinguish between old and new users, all of whom bear the expense of the old plant and all of whom will use the new plant. . . Courts which have been called upon to review this matter have made a distinction between the cost of providing service not previously provided and source of service. (Citations omitted.) This is not to say that in a proper case a customer may not be charged for the additional cost of extending the service to a point where the service had not previously been provided.

Id. at 185-87.

CONCLUSION

If a wholesale supplier of a public power district is required to add more generation capacity to serve an increase in customer demand, the new customers may not be charged more for their service that the old customers, assuming they are in the same rate classification. By the same token, if a public power district needs to upgrade its electric system to accommodate new irrigation customers because of an increased load, new customers may not be charged for the cost of upgrading the system. This is so because both the old and the new customers are

receiving the same service, they are the same class of customer, and they will both be using the upgraded facilities. In light of the foregoing, it would be arbitrary to place the cost of upgrading the system on the new irrigation customers.

Similarly, it would be arbitrary to required new irrigation customers to control their electrical loads, without placing the same restriction on old irrigation customers. A district could amend an existing policy to require all irrigation customers, both old and new, to control their electrical load.

However, if a public power district incurs additional costs in extending its electric system to new irrigation customers, these new customers may be charged with the cost of such extension or a portion of the cost of the extension, so long as all new customers in this class are likewise charged for such extensions at the same incremental cost. The cost of line extension may change from time to time based on the cost of materials and changes in policy on whether the entire cost or a portion of the cost will be passed on to the customer. The amendment of existing line extension polices or even creating a new policy is not discriminatory so long as all new or future customers in the same rate class are treated the same.

Very truly yours,

CROSBY GUENZEL LLP

By Steven G. Seglin

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