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Rex Carpenter
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Re: Fuel Cells

Dear Rex:

You have asked me to comment on several questions regarding the proposed use of fuel cells by public power districts and cooperatives. It is my understanding that a fuel cell is an electrochemical device that converts commonly available fuels directly into electricity. In that respect, it is similar to a battery. With fuel cell technology, an electrochemical process generates the electricity. Many of the fuel cells under development use propane or natural gas as a fuel stock and therefore have some application for use in rural or remote locations. Fuel cells may be suited for providing power for farms or ranches, or for powering residences or multi-family dwellings in areas where utility rates are high or costly. Businesses can use fuel cells for standby or emergency use, or to run essential equipment such as computers during power outages. Utilities can use fuel cells as an alternative to building line extensions, or to correct voltage levels and improve load flow or reliability. They can also be used for peak shaving and limiting demand.

The questions that you have posed and my comments are as follows:

QUESTION 1: Under what conditions can a public power district (PPD) or a cooperative (Electric Cooperative (EC) or Electric Membership Association (EMA) sell energy from a fuel cell to a retail customer?

RESPONSE: Suppliers of electricity including a PPD, EC or EMA can only sell electric power at retail in their own service areas. *Neb. Rev. Stat. § 70-1002* requires suppliers of electricity serving customers at retail in adjoining service areas to enter into written agreements specifying the area or customers each shall serve with electric energy. The written agreements are required to be approved by the Nebraska Power Review Board (NPRB). Once the

agreements have been approved by the NPRB, the service area becomes certified (§ 70-1008) and no other electric supplier can serve within the certified serve area, without the consent of the certified supplier and the approval of the Power Review Board (*Neb. Rev. Stat.* § 70-1010).

QUESTION 2: What restrictions apply to non-utility marketers of fuel cells? For example, can a Farmer's Cooperative sell the electric output of a fuel cell?

RESPONSE: Non-utility marketers cannot sell electricity in a certified service area of a utility. Nonetheless, a non-utility marketer can probably sell or lease the fuel cells to the end user and supply the fuel, similar to a diesel powered generator.

QUESTION 3: Can a PPD buy propane or another fuel source solely for the purpose of using that fuel to generate power from a fuel cell?

RESPONSE: Yes, so long as the fuel cell is owned or controlled by the PPD, is a part of the PPD electric system, and the propane is purchased by the PPD for its own use.

QUESTION 4: Can a PPD sell propane for non-electric uses in the home (for example, home heating or cooking)?

RESPONSE: No, a PPD has no explicit statutory or implied authority to sell propane to a customer for any purpose. A PPD may purchase propane for its own use.

QUESTION 5: Can a PPD that owns a propane tank which stores propane for fuel cell operations, lease storage space in the tank to another entity which would sell the propane for heating and cooking purposes?

RESPONSE: If a storage tank has excess capacity, a PPD probably has the authority to lease the excess capacity to another entity. However, I do not think it would be a good practice to intentionally oversize a tank with the intention in mind to lease it to another entity.

QUESTION 6: What is the liability of a PPD for property damage or injury if the PPD owns or leases the fuel cell as opposed to the outright sale to the customer?

RESPONSE: If the PPD owns or leases the fuel cell, it has greater liability than if it sells the fuel cell to the customer. However, under either the ownership or sale, the purchase of liability insurance by either the PPD or the customer can protect both parties interest.

QUESTION 7: If a PPD decides to utilize fuel cells as a part of its electric system, will it be required to develop a new rate for customers utilizing this technology, or can a blended rate be utilized to keep the cost at a reasonable level?

RESPONSE: This question is difficult to answer and will depend on the specific facts of each case. In McGinley v. Wheat Belt P. P. Dist., 214 Neb. 178, 332 N.W. 2d 915 (1983), the Nebraska Supreme Court encountered a similar question regarding the addition of capacity to serve irrigation. In that case the Court held:

(1) Persons receiving similar service under similar circumstances cannot be charged for such service in an arbitrary or dissimilar manner.

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

(3) A discrimination may arise from a mere inequality in rates, but an overcharge arises only where the rate charged is unreasonable in and of itself, irrespective of the rate exacted of others, or when it is in excess of the rate established for the particular customer or business. In a suit for overcharges the rate paid by other is immaterial. It is only in suits for damages for discrimination that rates charged other are important.

In Wheat Belt, new irrigation customers were being charged a higher rate for electricity because Wheat Belt's power supplier had to obtain a new and more costly source of supply to meet the additional demand. The new irrigators were receiving the same service as existing customers. The only difference was that the new source of power was more costly. The court concluded that a dissimilar rate may not be imposed for similar service solely on the basis that the additional source of the power or energy is more costly than the previous sources. The court also recognized that in appropriate cases the additional cost of providing service not previously provided may be taken into consideration in establishing the cost of service.

In view of this decision it is difficult to answer the question posed with either a yes or no. It will depend on the specific facts in each case. If the only way to get service to a customer is by utilizing the fuel cell technology, it may be appropriate to offer a blended rate. Nonetheless, at least some of the cost of providing service to the customer should also be taken into consideration and perhaps passed along to the customer in the way of a contribution to construction. On the other hand, if the use of the fuel cell was to enhance the reliability of the power supply to a computer reliant business, then it would not seem appropriate to blend the rate with other less expensive sources of power.

QUESTION 8: Can a PPD invest in an independent cooperative entity that would sell propane to it for generation, but may also sell propane to individual homes and businesses for heating and cooking?

RESPONSE: No. A PPD can provide technical and management assistance to prospective, new, or expanding businesses, including home based businesses in order to promote economic development in rural areas of a PPD (*Neb. Rev. Stat. § 70-625(3)*). This does not include the authority to invest or provide capital. A PPD may provide technical and management assistance to an Electric Membership Cooperative (EMA) which in turn may sell propane to the PPD as fuel for fuel cells. However, the contribution of the technical and management assistance is the only contribution that a PPD is authorized to provide. In other words, the PPD may pay the salaries of PPD employees who in turn provide technical and management assistance to the EMA. The EMA may also sell propane to individual homes and businesses for heating and cooking, if authorized by its articles of incorporation. Creating two classes of memberships, one based on the sale of the propane to the PPD and the other based on the sale of

the propane for heating and cooking, does not in my opinion change the limitations on the PDD authority.

QUESTION 9. What contract restrictions do Tri-State and NPPD wholesale customers have to address when trying to use fuel cells?

RESPONSE: I assume that all PPDs, ECs, and EMAs are total wholesale requirements customers of either Tri-State or NPPD. If that is the case, they are required to purchase all of their electric power and energy needs from either Tri-State or NPPD. If any of these entities wanted to use fuel cells as a power source that would replace a purchase that would otherwise be required to be made under the contract, it would probably require a amendment to the power supply contract. In each case the contract would have to be examined to determine the restriction on the purchase of power from another source.

QUESTION 10: Can a fuel cell be classified as a "new" appliance under *Neb. Rev. Stat.* § 70-625 and then be sold or leased for a period of five years?

RESPONSE: I think it would be a stretch to call a fuel cell an electric appliance. PPD statutes do not define appliance. Webster's New World Dictionary (3d ed. 1984, 67) defines appliance as "a device or machine for performing a specific task, especially one that is worked mechanically or by electricity (stoves, irons, etc. are household appliances)." A fuel cell generates electricity and is not operated by using electricity. Therefore I do not believe that it is an appliance within the meaning of § 70-625.

QUESTION 11: Can a PPD own or lease fuel cells as a part of its electric system?

RESPONSE: Yes, if authorized in its Charter. *Neb. Rev. Stat.* § 70-626 provides in part "a district may own, construct, reconstruct, purchase, lease, or otherwise acquire, improve, extend, manage, use or operate any electric light and power plants, lines, and systems or ethanol production or distribution systems ...and may engage or transact business or enter into any kind of contract or arrangement with any person . . .for or incident to the exercise of any one or more of the forgoing powers, or for the generation, distribution, transmission, sale or purchase of electrical energy or ethanol for lighting, power, heating and every other useful purpose whatsoever, and for any and every service involving, employing , or in any manner pertaining to the use of electrical energy by whatever means generated or distributed . . ." The statute clearly authorizes a PPD to own or lease generation and engage in any business involving electricity by whatever means generated or distributed. A fuel cell is a tiny power plant or system and the PDD would be engaged in the business of the generation and sale of electrical energy and further would be providing a service involving the use of electrical energy. I think that a cogent argument can be made that a fuel cell may be reasonably necessary for the conduct of a PPD business, which is the test referred to in *Burnett v Central Neb. P.P. Dist.*, 147 *Neb.* 458, 23 *N.W.* 2d 661 (1946).

QUESTION 12: Is it necessary to amend a PPD charter and/or bylaws to authorize the ownership, use, lease or sale of fuel cells?

RESPONSE: Probably. Each district's charter and bylaws would have to be examined. At a minimum, the charter and bylaws should authorize the generation, transmission and distribution of electricity by any means including fuel cells.

QUESTION 13: Should PPD's introduce legislation that will limit or prohibit the sale of fuel cells by entities other than electric utilities with certified service area?

RESPONSE: It is difficult to predict in advance the wisdom of this type of legislation. However, as a practical matter, I would think that any legislation of this type would draw opposition from non-utilities who may be interested in marketing this type of technology. Furthermore, there may be an argument that this type of legislation is unconstitutional as a restraint of trade. In any event, I would not recommend any proposed legislation at this time.

QUESTION 14. Can a PPD legally enter into a franchise agreement whereby it purchases territory to market a commercial product? Can it enforce its rights under the franchise agreement if some other entity began selling the same product in its territory?

RESPONSE: A PDD pursuant to *Neb. Rev. Stat. § 70-626* has the authority to "enter into any kind of contract or arrangement with any person ... [pertaining to the operation of any electric light and power plants, lines and systems ... or distribution systems] ... for or incident to the exercise of any one or more of the foregoing powers, or for the generation, distribution, transmission, sale, or purchase of electrical energy or ethanol for lighting, power, heating, and any and every other useful purpose whatsoever, and for the use of electrical energy by whatever means, and for any and every service involving, employing, or in any manner pertaining to the use of electrical energy by whatever means generated or distributed . . ." Accordingly, I believe that a PPD can enter into a franchise agreement purchasing a territory to market a commercial product, so long as the product fits within the language of the above statute. I believe that a fuel cell fits within the language. So far as a PDD enforcing its rights under the franchise, including any provision for exclusivity, it depends upon the language in the contract. Generally, contracts which are clear and unambiguous in their terms are not subject to interpretation. See, e.g. Schrempp and Salerno v. Gross, 247 Neb. 685, 529 N.W.2d 764 (1995). The Nebraska Franchise Practices Act, *Neb. Rev. Stat. § 87-401 to 87-410*, is silent in so far as the enforcement of exclusivity provisions in a franchise is concerned.

QUESTION 15. Could the chartered territory of a PPD or Coop be expanded for the sole purpose of bringing municipalities into its chartered territory to allow it to market/sell, use, or lease fuel cells in those incorporated areas? What sort of agreements would be permissible under the Interlocal Cooperation Act?

RESPONSE: I doubt whether a PPD could acquire the right to serve a municipality at retail (sell electricity generated by fuel cells) by expanding the chartered territory of a PPD or Coop to include the municipality. Although it may be possible for municipalities which have a population of less than 1500 inhabitants to be added to the chartered territory of a PPD pursuant to *Neb. Rev. Stat. § 70-604.01*, in order to sell such inhabitants electricity, the inhabitants would

have to be included within the service area of a PPD or Coop. Merely adding such municipality to the chartered territory does not give the PPD the right to serve the municipality at retail. I further doubt that a PPD could acquire the right to serve by entering into an agreement with the municipality under the Interlocal Cooperation Act. In order to serve the municipality at retail, the PPD and the municipality would have to enter into a service area agreement approved by the Nebraska Power Review Board. Even if a PPD wanted to sell or lease the fuel cell rather than sell the electricity from the fuel cell, adding a municipality to the chartered territory would probably not give it that right, since adding a municipality to the chartered territory only gives the persons residing in the municipality the right to vote for director or run as a candidate for director (*Neb. Rev. Stat. § 70-610*).

QUESTION 16: What if any approval is needed by a PPD before a fuel cell could be put into service?

RESPONSE: Probably none. *Neb. Rev. Stat. § 70-1012* provides in part “[b]efore any electric generation facilities or any transmission lines or related facilities carrying more than seven hundred volts are constructed or acquired by any supplier, an application, filed with the [power review] board . . . shall be approved by the board. . .” I have been told that a fuel cell does not carry more than seven hundred volts. If it does, then power review board approval will have to be obtained unless the generation replaces a generating plant owned by an individual municipality with a capacity not greater than the one being replaced, generates less than 25,000 kilowatts, and will not be used to supply wholesale power outside of the applicant’s existing retail service area or chartered territory.

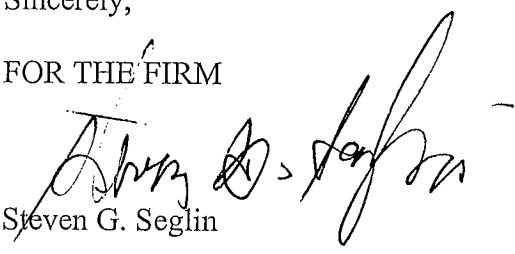
QUESTION 17: What legal options are available to PPDs to enhance the ability of PPDs to market fuel cells outside a PPDs retail service area.

RESPONSE: Because of the restrictive nature of the authority granted PPDs under their authorizing statutes, there is not much that can be done to enhance a PPDs ability to engage in marketing fuel cells outside a PPD retail service area. If the fuel cells are to be utilized as part of a PPD electric system and the power generated from the cells sold to customers, then the customers must be located in a PPD retail service area. If the fuel cells are to be marketed like a diesel generator, then they can probably be sold within a PPD operating territory which includes its wholesale service area. Otherwise, a PPD may provide technical and management assistance to prospective, new, or expanding businesses, including home based businesses in order to promote economic development in rural areas of a PPD (*Neb. Rev. Stat. § 70-625(3)*). This does not include the authority to invest or provide capital. A PPD may provide technical and management assistance to an Electric Membership Cooperative (Coop) which in turn may sell propane to the PPD as fuel for fuel cells. However, the contribution of the technical and management assistance is the only contribution that a PPD is authorized to provide. In other words, the PPD may pay the salaries of PPD employees who in turn provide technical and management assistance to the Coop. The Coop, if it is an Electric Membership Association, may also sell propane to individual homes and businesses for heating and cooking, if authorized by its articles of incorporation.

These comments are intended to give some overall guidance and not intended to give definitive advice on matters that are discussed in this letter. The areas covered in this letter are complex and in certain instances fact specific and if any PPD or Coop is interested in pursuing the fuel cell technology further, they should consult with their attorney.

Sincerely,

FOR THE FIRM


Steven G. Seglin

SGS:rrk