

E-100, Sub 37a

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Attn: Jo Anne Sanford, Chair, North Carolina Utilities Commission

Chairman's Office

MAR 6 2001

Members of the North Carolina Utilities Commission:

This letter is in response to a request from the North Carolina Utilities Commission (the "Commission") to Bob Koger, President of North Carolina Advanced Energy Corporation ("AEC"), for information regarding certain actions taken by AEC subsequent to the Commission's approval on February 8, 2000, of two amendments to AEC's Articles of Incorporation (the "Charter"). Specifically, the Commission requested information of any actions taken by AEC, which may be similar to those taken by MCNC in the establishment and sale of its spin-off company, Cronos Integrated Microsystems, Inc. ("Cronos"). In addition, the Commission requested information on any plans that AEC may have to own and distribute shares of stock in other entities to AEC's employees.

As you know, On February 8, 2000, the Commission approved two amendments to AEC's Charter. The first amendment allows AEC to invest funds in entities including privately held for-profit companies. Previously AEC could only invest its surplus cash in "interest bearing federally insured bank accounts or certificates of deposit, direct obligations of the United States government or obligations guaranteed by either the government of the United States or any of its agencies or by the State of North Carolina or any of its agencies or subdivisions." AEC requested this amendment so that it could (i) qualify for certain federal grant funds by forming for-profit subsidiaries and, (ii) obtain equity interests in small start-up companies for which AEC was willing to provide funds.

The ability to form for-profit subsidiaries provides AEC with additional means in which to bring research funds into North Carolina. Start-up companies are often eligible to apply for various federal grants such as federal Small Business Innovative Research grants, which typically

require that the applicant be a "for-profit" entity. Qualifying grantees are required to be for-profit entities so that the government may recover all or part of its grant through various wage, income and other taxes levied on those grantees that are successful. As a result of the Charter amendment, AEC now has the ability to establish a requisite for-profit entity in the event that AEC feels it appropriate to do so in order to qualify for various funding programs.

Although AEC may now form a "for-profit corporation, to date it has not done so. This is in contrast to MCNC, which forms, and serves as, an incubator for small companies that are involved in emerging technologies. These companies include, among others, Cronos, which designs and manufactures microelectromechanical systems and Unitive Electronics, Inc. ("Unitive"), which has developed an innovative soldering technology that is used in the manufacturing and assembly of integrated circuits. When these companies are sufficiently mature to attract private capital, they are spun out of MCNC, with MCNC retaining a significant equity interest. The equity interest is received in exchange for the intellectual property and other assets contributed by MCNC. MCNC's intent is to use this equity interest to (i) to fund additional start-up companies; and (ii) provide an incentive to MCNC employees, which may have participated in the creation and incubation of the various start-ups. At this time AEC has neither created any for-profit subsidiaries nor does it have plans to create any for-profit subsidiaries in the future.

In addition to forming for-profit subsidiaries, the first Charter amendment also allows AEC to receive an equity interest in exchange for its grant to, or investment in, a privately held company. Prior to the amendment, in the event that AEC worked with privately held entities in the furtherance of AEC's corporate purpose and decided to assist such entities in their research and development efforts, AEC was limited to making grants and contributions in-kind. For example, AEC made a grant to Southern Produce to further its research of the feasibility of an "Iceberg Underground Cooling Storage System" and to Sea Sun Power Systems to provide further development of the "Energy Cycle". Now, however, as result of the first Charter amendment and in addition to any results of research and development efforts that will be available to the citizens of North Carolina, AEC may receive an equity interest in exchange for such grants or contributions in-kind.

At the time AEC proposed this Charter amendment, AEC discussed with the Commission the possibility of AEC investing in a small, privately held and locally owned startup fuel cell company, Microcell Corporation ("Microcell"). Subsequent to the Charter amendment, and after due consideration and analysis, the Advanced Energy Board of Directors unanimously approved a \$150,000 investment in Microcell in exchange for Microcell Series A Preferred Stock. Microcell's primary focus is in developing more efficient and economical electric power sources, and AEC believes that the results of Microcell's research and development efforts may directly benefit the citizens of North Carolina and that any development grants obtained by Microcell may lead to continued and future research in the area of electric power use and conservation in

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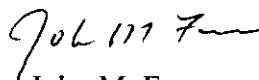
the state of North Carolina. Prior to the Charter amendment, AEC would have been limited to making a \$150,000 grant to Microcell as its only funding option.

The second Charter amendment that was approved on February 8, 2000, allows AEC to permit its employees to own stock in companies in which AEC either establishes or invests, including both for-profit wholly-owned subsidiaries (in the event that AEC ever establishes such an entity) or privately held companies in which AEC has made an investment. This particular Charter amendment was sought so that AEC could, if it desired, create a plan that would allow AEC to distribute shares of stock that it held to employees so that the AEC employees could share in any return on an investment made by AEC. Although AEC did investigate the costs required to set up such a plan, all efforts in this area were abandoned when it was discovered that the total cost to establish a plan could approach \$200,000 and that the annual costs to monitor and maintain a plan were not inconsequential. Due to the prohibitively high costs to implement and maintain an employee incentive program, the AEC Board voted to abandon its efforts in this area. To date AEC has not transferred any of the equity interests held by it to employees, directors or any other third parties it has no plans to do so in the future.

This contrasts to a plan implemented and maintained by MCNC under which its employees are eligible to receive equity interests in companies which MCNC has spun-off, such as Cronos and Unitive. In addition, MCNC has also sold part of its retained equity stake in a company to its directors.

In summary, AEC has not formed, and has no present intent to form, any for-profit subsidiaries. AEC has taken a small equity position in Microcell and has retained, and plans to retain, all such interest. It has no plans to transfer any of its shares to employees, directors or any other third party. At this time, AEC does not anticipate that it will make any investments in any companies this year. Thank you for the opportunity to bring you up-to-date on this matter. Please feel call me if you need additional information or have any questions regarding this letter.

Sincerely,



John M. Fuscoe

cc: Robert H. Bennick, Jr., General Counsel, North Carolina Utilities Commission  
Robert P. Gruber, Executive Director of the Public Staff, North Carolina Utilities Commission  
Robert K. Koger, President, North Carolina Advanced Energy Corporation