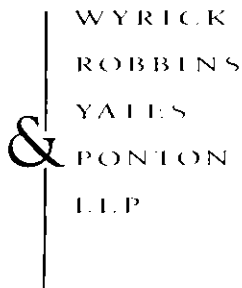


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Clerk's Office  
N.C. Utilities Commission

April 10, 2001

North Carolina Utilities Commission  
4325 Mail Service Center  
Raleigh, North Carolina 27699-4325  
Attn: Jo Anne Sanford, Chair, North Carolina Utilities Commission

Members of the North Carolina Utilities Commission:

This letter is in response to a letter from Jo Anne Sanford, dated March 29, 2001. In answer to the questions presented in that letter, please consider the following information.

To date, AEC has invested in only one independent for-profit entity, which is Microcell Corporation ("Microcell"). The amount invested was \$150,000 and the investment was made on February 17, 2000. The investment by AEC was conditionally approved by the AEC Board of Directors (the "AEC Board") in its meeting in December of 1999 and was further reviewed and approved by the AEC Executive Committee<sup>1</sup> (the "Executive Committee") on February 16, 2000. In addition, the Executive Committee, in its meeting on February 16, 2000, agreed to allow AEC employees to obtain a financial interest in Microcell.

The Executive Committee also determined that AEC's management would pursue and present to the AEC Board in April of 2000, a company-wide plan under which all AEC employees could obtain a financial interest in Microcell. At the time of this decision, the Executive Committee had been investigating an employee incentive/retention plan, similar to the plan adopted by MCNC, whereby AEC would be able to distribute to each AEC employee (at no cost to the employee) a small number of Microcell shares, or rights to such shares. Subsequent to this Executive Committee meeting, the AEC Board decided not to go forward with this

<sup>1</sup> Under Section 1104 of the Standing Rules and Procedures of the AEC Board of Directors, the Executive Committee may take actions on behalf of the AEC Board of Directors in significant areas where a decision must be taken prior to the next AEC Board meeting.

company-wide plan. Absent majority ownership of Microcell by AEC, it was determined that IRS regulations would make such a plan too costly to implement and administer.

Pursuant to the AEC investment in Microcell, AEC obtained the right to designate one person to serve as a director on the Microcell Board of Directors (the "Microcell Board"). Initially, Robert K. Koger was chosen by AEC to be its representative on the Microcell Board. In late February and early March of 2000, Mr. Koger, other AEC employees, and outside investors, were approached by Microcell regarding their potential purchases of Microcell stock. Mr. Koger was the only potential investor to indicate any interest but before making his investment, Mr. Koger discussed the matter with Gordon Blackwell, Chairman of the AEC Board. In a letter dated March 24, 2000, Mr. Koger advised the AEC Board of his intentions and agreed that he would resign as a director of the Microcell Board. Gordon Blackwell, a member of the AEC Board, was appointed to be AEC's representative on the Microcell Board.

It is important to point out that Mr. Koger, as President of AEC, has not been involved with any negotiations regarding Microcell. Although Mr. Koger is not a director of AEC, he attends the AEC Board meetings, reports on AEC activities, and may be called upon by the Board to participate in AEC Board discussions. Subsequent to his investment in Microcell, Mr. Koger has been diligent to ensure that he does not participate in any AEC Board discussions regarding any actions to be taken with respect to Microcell. In addition, Mr. Koger directed Maggy Inman, AEC Vice President of Administration, to negotiate a facilities lease of AEC space to Microcell. Ms. Inman used a simple pro rata allocation method based on the number of square feet leased to Microcell in order to arrive at the monthly rent for Microcell. Ms. Inman reported directly to the Board on the means of arriving at the dollar amount. Also, Mr. Koger never attended a Microcell Board meeting as a director as there were no Microcell Board meetings prior to his resignation. Thus, since his investment in AEC, Mr. Koger has not participated in any decisions involving AEC and Microcell, whether as an officer of AEC or as a shareholder of Microcell.

As pointed out by the Commission, without the approval of the AEC Board, no AEC employee shall have any financial interest in any concern or venture which is engaged in doing business with any electric utility supplier, AEC or any party or entity contracting with AEC (each referred to hereinafter as an "Affiliated Entity" and, collectively, as the "Affiliated Entities"). Since Microcell agreed to lease office and laboratory space from AEC, Microcell fell immediately into the category of an entity contracting with AEC. As of the date of this letter and except for the purchase of Microcell stock by Mr. Koger, the AEC Board has not approved any other purchase by an AEC employee of a financial interest in an Affiliated Entity.

AEC management is currently proposing that the following processes be put in place in order to ensure that the AEC Board carefully reviews any future AEC employee investment in an Affiliated Entity. First, AEC will distribute a memo to all employees informing them that AEC must be notified of and approve any employee acquisition of a financial interest in an Affiliated Entity. The memo will explain why this notification and approval is necessary, that this

notification process is a condition of employment, and how a conflict of interest may develop if this process is not observed. Also, each present employee will be asked for a current list of any investments (excluding mutual funds) he or she has in any regulated utility in the United States or with any entity doing business with AEC. This list will be provided to the Executive Committee of the AEC Board.

Second, with respect to Microcell, AEC is a member of the Microcell Board of Directors, and as such, must be notified of all securities sold by Microcell. Therefore, Microcell will not be able to grant or sell a financial interest to an AEC employee without proper notice being given to the AEC representative serving on the Microcell Board (currently, this representative is Gordon Blackwell). The AEC Board will inform Mr. Blackwell, and all future Microcell Board representatives, that AEC be notified immediately in the event that Microcell contemplates a sale of its securities or other financial interest to an AEC employee. In the event of such a notification, the AEC Board can then take the appropriate action.

Third, any future investment by AEC will only be made pursuant to a contractual commitment by the recipient of the investment, which prohibits the recipient from selling any financial interest to an AEC employee without the express written approval by the AEC Board of Directors. Finally, all members of the Board will receive a written memo by AEC's counsel outlining the duties of a director under North Carolina State law and common law. The memo will remind the directors that each proposed employee acquisition of a financial interest in an Affiliated Entity must be reviewed on a case by case basis, while paying careful attention to conflicts of interest and potential conflicts of interest. The memo will remind each director of his or her duties to AEC as set forth below.

Duty of Care. The first duty of directors requires them to make rational decisions based on adequate information, just as any other prudent person would, given similar circumstances. In North Carolina, case law precisely states: a director must in good faith perform his or her duties and make decisions in a manner in which he or she believes is in the best interests of the corporation. In so doing, the director is entitled to rely on information supplied by employees, legal counsel, independent accountants or committee reports, provided the director has a reasonable basis for believing the individual supplying the information. Courts interpret "reasonable" to mean the manner in which a normally prudent person would handle his or her own affairs. In legal parlance, the requirement that directors make reasonably informed, rational decisions is aptly called the "Duty of Care." See generally N.C.G.S. § 55-8-30.

Duty of Loyalty. The second duty of directors concerns the relationship between their interests and those of the corporation. Directors are prohibited from using their position within the company for personal advantage. The variety of situations in which conflicts of interest might arise is extensive. North Carolina imposes the "Duty of Loyalty" to ensure that directors serve the interests of the corporation and its shareholders before their own. North Carolina General Statutes Section 55-8-30(a)(3) states a director must act "in a manner he reasonably believes to be in the best interests of the corporation." The Duty of Loyalty proscribes

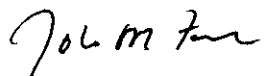
self-dealing and misappropriation of corporate property. A director self-deals when he or she (or a company in which he or she has an interest) contracts or deals, other than on arms' length terms, with the company of which he or she is a director. Misappropriation of corporate property occurs when a director takes a corporate opportunity originally available to or related to the business of the company, or when a director otherwise misuses corporate property. A director has a duty to the corporation to serve its best interests, and any lapse of this duty will result in liability to the extent the company was damaged or the director benefited.

Duty of Obedience. The "Duty of Obedience" in North Carolina requires simply that directors perform their duties in accordance with the relevant statutes and the corporate charter. A director of a corporation will be held personally liable when he or she acts beyond the scope of those powers.

It is anticipated that the AEC Board will expeditiously adopt the additional safeguards and recommendations set forth herein. Also, although Mr. Koger has taken all actions necessary to avoid any conflict of interest, the AEC Board will be advised by its counsel to remain cognizant of Mr. Koger's investment in Microcell and any possible potential conflict of interest arising from it.

AEC believes that (i) it is extremely unlikely that any plan (such as the one followed by MCNC) will be adopted under which shares or "units of ownership" in any future spinoffs or investments by AEC would be distributed in any manner; (ii) in the event that acquisition of a financial interest in an Affiliated Entity is contemplated by an individual employee, AEC will be timely notified; and (iii) the AEC Board will act accordingly to review and approve any proposed acquisition of a financial interest or requiring the disposal of any such interest as a condition of continued employment. Please feel free to call me with any questions or comments 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