COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF LOUISVILLE GAS AND ELECTRIC COMPANY FOR AN ORDER APPROVING AN ACCOUNTING ADJUSTMENT TO BE INCLUDED IN EARNINGS SHARING MECHANISM CALCULATIONS FOR 2003	)	CASE NO: 2003-00426

AND

APPLICATION OF KENTUCKY UTILITIES COMPANY FOR AN ORDER APPROVING AN ACCOUNTING ADJUSTMENT TO BE INCLUDED IN EARNINGS SHARING MECHANISM CALCULATIONS FOR 2003	)	CASE NO: 2003-00427

STIPULATION

WHEREAS, Louisville Gas and Electric Company ("LG&E") filed an application for an order approving an accounting adjustment with the Kentucky Public Service Commission ("Commission") on November 14, 2003 in Case No. 2003-00426;

WHEREAS, Kentucky Utilities Company ("KU") filed an application for an order approving an accounting adjustment with the Commission on November 14, 2003 in Case No. 2003-00427;

WHEREAS, the Kentucky Industrial Utility Customers, Inc. ("KIUC") was granted intervention by the Commission on December 4, 2003;

WHEREAS, the parties wish to facilitate the disposition of these two proceedings through the submission of a joint stipulation on the accounting issues; and, NOW; THEREFORE, pursuant to 807 KAR 5:001 Section 4(6)the parties stipulate as follows:

1. SFAS No. 143, *Accounting for Asset Retirement Obligations*, and FERC Order 631, *Accounting, Financial Reporting, and Rate Filing Requirements for Asset Retirement Obligations*, specify the accounting LG&E and KU must follow relative to legal obligations for the ultimate disposal of assets effective January 1, 2003. The companies have proposed accounting for these asset retirement obligations ("AROs") using a method which both complies with the required accounting literature and is consistent with the current ratemaking treatment.

2. The purpose of this stipulation is to state the accounting treatment which will negate, on a net basis, the income statement effects of implementing SFAS No. 143, so that there is no effect from SFAS No. 143 on LG&E's or KU's operating income for accounting or ratemaking purposes.

3. Effective January 1, 2003, the Companies recorded the entries as summarized on Exhibit 1. Upon implementation of SFAS No. 143 and FERC Order 631, LG&E and KU were required to remove the cost of removal ("COR") component from accumulated depreciation for assets with a legal obligation at retirement (Exhibit 1, Entry 4). The Companies were also required to record the expected future cost of the AROs discounted back to the date the assets were placed in service as ARO liabilities in FERC Account 230 (Exhibit 1, Entry 1). Offsetting ARO assets, equal to the ARO liabilities at the assets' original in-service dates, were recorded in FERC Accounts 317, 347 or 359.1, to represent the additional cost of the assets, due to the ultimate removal cost (Exhibit 1, Entry 1). Each of the ARO assets and ARO liabilities was then incremented to 2003 values by recording depreciation expense and accumulated depreciation from the in-service date of the underlying asset for the ARO asset (Exhibit 1, Entry 2) and by

recording accretion expense incrementing the ARO liability from the in-service date of the underlying asset (Exhibit 1, Entry 3). The net of the previously recorded COR, depreciation on the ARO assets, and the accreted ARO liabilities from the in-service date to January 1, 2003 (the amounts that would have been recorded in prior periods had the standard always been in effect) was recorded as a cumulative effect charge to the income statement using FERC Account 435 (Exhibit 1, Entries 4, 2 and 3, respectively). In order to remove the effect of adopting SFAS No. 143 and retain the ratemaking accounting approved by the Commission, the Companies recorded an offsetting regulatory credit in the income statement in FERC account 407 to counter the impact of the cumulative effect charges (Exhibit 1, Entry 5). The regulatory credit was offset against a regulatory asset in FERC Account 182.3 (Exhibit 1, Entry 5).

4. LG&E and KU made applications to the Commission on November 14, 2003 requesting that they be allowed to offset the amount recorded in the cumulative effect with the amount recorded in the regulatory credit since the cumulative effect was recorded below the line and the regulatory credit was recorded above the line, resulting in inconsistent treatment of these amounts for ratemaking purposes.

5. Exhibit 2 illustrates the entries that will be recorded beginning in 2003. LG&E and KU will continue recording depreciation expense and accumulated depreciation on the ARO asset and will continue incrementing the value of the ARO liability through accretion expense (Exhibit 2, Entries 1 and 3). In order to continue removing the effect of adopting SFAS No. 143 and retain the ratemaking accounting approved by the Commission, the Companies will offset all depreciation expense and accretion expense related to ARO assets and liabilities through a credit to the regulatory credit account (FERC account 407) and a charge to a regulatory asset account (FERC account 182.3) (Entries 2 and 4). LG&E and KU will continue to record the COR

component of depreciation on the underlying assets, by charging depreciation expense (Exhibit 2, Entry 5). The COR depreciation will be offset by a credit to the regulatory liability in FERC Account 254 (Exhibit 2, Entry 5). Non-COR depreciation on the underlying assets will continue to be charged to depreciation expense and credited to accumulated depreciation (Exhibit 2, Entry 5).

6. For ratemaking purposes, the regulatory liability associated with the COR depreciation expense, including the portion netted against regulatory assets in the cumulative effect at adoption of SFAS No. 143, will be included in the calculation of rate base since this amount represents the accumulated depreciation for the COR under Commission approved depreciation rates. The ARO assets, related ARO asset accumulated depreciation, ARO liabilities, and remaining regulatory assets associated with the adoption of SFAS No. 143 will be excluded from rate base.

7. KU and LG&E stipulate to the accounting described above, given that Commission approval is received both for the offset of the cumulative effect against the regulatory credit for the initial adoption of SFAS 143 effective January 1, 2003, and for recording the associated regulatory assets and regulatory liabilities, at initial adoption and on an on-going basis.

8. KIUC's consent and agreement to the terms of this Stipulation is without prejudice to any position KIUC may take on the merits of the issues discussed herein in future ratemaking proceedings before the Commission, except and excluding LG&E's and KU's annual Earning Sharing Mechanism filings for the 2003 operating periods and thereafter.

The parties request the Commission issue an order which:

(1) approves the regulatory assets and liabilities associated with adopting SFAS No. 143 and going forward,

(2) eliminates the impact on net operating income in the 2003 ESM annual filing caused by adopting SFAS No. 143,

(3) to the extent accumulated depreciation related to the cost of removal is recorded in regulatory assets or regulatory liabilities, such amounts will be reclassified to accumulated depreciation for ratemaking purposes of calculating rate base, and

(4) the ARO assets, related ARO asset accumulated depreciation, ARO liabilities, and remaining regulatory assets associated with the adoption of SFAS No. 143 will be excluded from rate base.

The parties recommend the Commission issue an order granting the applications of LG&E and KU subject to the accounting procedures described herein.

Dated: December 19, 2003

Respectfully submitted,

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