



Ernie Fletcher
Governor

LaJuana S. Wilcher, Secretary
Environmental and Public
Protection Cabinet

Christopher L. Lilly
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Commonwealth of Kentucky
Public Service Commission
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Mark David Goss
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Teresa J. Hill
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Gregory Coker
Commissioner

April 12, 2006

Mr. John J. Finnigan, Jr.
Senior Counsel
The Union Light, Heat and Power Company
P.O. Box 960
Room 250, Atrium II
139 East Fourth Street
Cincinnati, Ohio 45201-0960

RE: March 30, 2006
Informal Conference
Case No. 2003-00252

Dear Sir:

Enclosed please find a memorandum that has been filed in the record of the above-referenced case. Any comments regarding the contents of the memorandum should be submitted to the Commission within seven days of receipt of this letter. Any questions regarding this memorandum should be directed to Mr. Jeff Shaw of the Commission Staff at 502-564-3940, Extension 237.

Sincerely,

A handwritten signature in cursive script, appearing to read "Beth O'Donnell".

Beth O'Donnell
Executive Director

CC: Parties of Record

Attachment

Honorable Elizabeth E. Blackford
Assistant Attorney General
Office of the Attorney General
Utility & Rate Intervention Division
1024 Capital Center Drive
Suite 200
Frankfort, KY 40601-8204

Honorable John J. Finnigan, Jr.
Senior Counsel
The Union Light, Heat and Power
Company
139 East Fourth Street
Cincinnati, OH 45202

Honorable Michael J. Pahutski
Attorney at Law
The Union Light, Heat and Power
Company
139 East Fourth Street
Cincinnati, OH 45202

INTRA-AGENCY MEMORANDUM

KENTUCKY PUBLIC SERVICE COMMISSION

TO: Main Case File - Case Nos. 2003-00252

FROM:  Jeff Shaw, Division of Financial Analysis

DATE: April 12, 2006

SUBJECT: March 30, 2006 Informal Conference

An informal conference held March 30, 2006 at the Commission's offices was attended by representatives of The Union Light, Heat and Power Company ("ULH&P"), the Attorney General of the Commonwealth of Kentucky ("AG"), and Commission Staff ("Staff"). An attendance list for the conference and the letter and related information provided by ULH&P prior to the conference are attached hereto.¹ The purpose of the conference was to discuss how changes in electric markets and changes implemented by the Federal Energy Regulatory Commission ("FERC") impacted ULH&P's need for, and ability to enter into, a back-up power supply agreement with either its parent, Cincinnati Gas and Electric Company ("CG&E"), or some other electric generator.

ULH&P stated that, due to changes in FERC's code of conduct rules, it could not implement the back-up power supply contract with CG&E, which the Commission had previously approved in this case. It also indicated that, based on its experience under the Midwest Independent System Operator's ("MISO") Day 2 energy markets, it did not believe that putting its back-up power supply requirements out for bid would be beneficial (this was what ULH&P had planned approximately one year ago). ULH&P stated its belief that MISO's energy market could adequately serve its back-up power needs and indicated that it planned to rely on MISO for its back-up power supply.

Staff and the AG indicated that, as this represented a change from what the Commission had approved, they believed ULH&P would need Commission approval to depart from the type of back-up power arrangement previously authorized. ULH&P stated that it would make a formal proposal as part of the general rate application it expects to file later this year, supported by testimony and additional evidence.

Attachment

¹ This was a joint conference for this case and another ULH&P case, Case No. 2005-00228. A representative of the Kroger Company identified on the attendance list was in attendance for the discussion pertaining to that case.

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF THE UNION LIGHT, HEAT AND POWER COMPANY)
 FOR A CERTIFICATE OF PUBLIC CONVENIENCE AND NECESSITY TO)
 ACQUIRE CERTAIN GENERATION RESOURCES AND RELATED) CASE NO. 2003-00252
 PROPERTY; FOR APPROVAL OF CERTAIN PURCHASE POWER)
 AGREEMENTS; FOR APPROVAL OF CERTAIN ACCOUNTING TREATMENT;)
 AND FOR APPROVAL OF DEVIATION FROM REQUIREMENTS OF)
 KRS 278.2207 AND 278.2213(6))

JOINT APPLICATION OF DUKE ENERGY CORPORATION, DUKE)
 ENERGY HOLDING CORP., DEER ACQUISITION CORP., COUGAR)
 ACQUISITION CORP., CINERGY CORP., THE CINCINNATI GAS &) CASE NO. 2005-00228
 ELECTRIC COMPANY AND THE UNION LIGHT, HEAT AND POWER)
 COMPANY FOR APPROVAL OF A TRANSFER AND ACQUISITION)
 OF CONTROL)

=====

March 30, 2006 Informal Conference

=====

Please sign in:

NAME

REPRESENTING

RICHARD RAFF

PSC-LEGAL

Isaac Scott

PSC - Financial Analysis

JEFF SHAW

PSC - FINANCIAL ANALYSIS

David Edward Speward

Office of the Attorney General

Bobby Blaylock

OAG

Chris Vogt

CINERGY - ULH&P

NACK STEFFEN

CINERGY - ULH&P

ELIE RUSSELL

PSC

Brett Ritchie

Cinergy - ULH&P

Mike Gribler

Cinergy ULH&P

DOUG ESAMANN

CINERGY - ULH&P

JOHN FINNIGAN

CINERGY - ULH&P

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF THE UNION LIGHT, HEAT AND POWER COMPANY)
FOR A CERTIFICATE OF PUBLIC CONVENIENCE AND NECESSITY TO)
ACQUIRE CERTAIN GENERATION RESOURCES AND RELATED) CASE NO. 2003-00252
PROPERTY; FOR APPROVAL OF CERTAIN PURCHASE POWER)
AGREEMENTS; FOR APPROVAL OF CERTAIN ACCOUNTING TREATMENT;)
AND FOR APPROVAL OF DEVIATION FROM REQUIREMENTS OF)
KRS 278.2207 AND 278.2213(6))

JOINT APPLICATION OF DUKE ENERGY CORPORATION, DUKE)
ENERGY HOLDING CORP., DEER ACQUISITION CORP., COUGAR)
ACQUISITION CORP., CINERGY CORP., THE CINCINNATI GAS &) CASE NO. 2005-00228
ELECTRIC COMPANY AND THE UNION LIGHT, HEAT AND POWER)
COMPANY FOR APPROVAL OF A TRANSFER AND ACQUISITION)
OF CONTROL)

=====
March 30, 2006 Informal Conference
=====

Please sign in:

NAME

REPRESENTING

Mike Kurtz

Kroger

Dawn McGee

PSC Financial Analysis



Cinergy Corp.
139 East Fourth Street
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P.O. Box 960
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fax 513.287.3810
jfinnigan@cinergy.com

John J. Finnigan, Jr.
Senior Counsel

VIA E-MAIL AND OVERNIGHT MAIL

March 28, 2006

Ms. Elizabeth O'Donnell
Executive Director
Kentucky Public Service Commission
211 Sower Boulevard
P.O. Box 615
Frankfort, Kentucky 40602-0615

RECEIVED

MAR 29 2006

PUBLIC SERVICE
COMMISSION

Re: In the Matter of The Application of The Union Light, Heat and Power Company for a Certificate of Public Convenience and Necessity to Acquire Certain Generation Resources and Related Property; for Approval of Certain Purchase Power Agreements; for Approval of Certain Accounting Treatment; and for Approval of Deviation from Requirements of KRS 278.2207 and 278.2213(6), Case No. 2003-00252

Dear Ms. O'Donnell:

We write this letter to explain a substitute proposal for the back-up power supply contract between The Union Light, Heat and Power Company ("ULH&P") and its parent company, The Cincinnati Gas & Electric Company ("CG&E"), approved by the Commission in this case.

Background

ULH&P has always intended, as its central purpose in this case, to attain a long-term supply of power for its customers while attempting to insulate customers from the impacts of volatile wholesale power prices. The centerpiece of this plan was CG&E's transfer of three power plants to ULH&P – East Bend No. 2, Miami Fort No. 6 and the Woodsdale Generating Station ("the Plants") – at CG&E's net book value, which the Commission's December 5, 2003 and June 17, 2005 Orders approved. Although this Commission granted preliminary approval for the Plant transfer on December 5, 2003, the parties were unable to obtain the other necessary regulatory approvals until late 2005. CG&E and ULH&P closed the transaction on January 25, 2006, with an effective date of January 1, 2006, so ULH&P now owns the Plants, subject to The Dayton Power and Light Company's 31% ownership of East Bend No. 2.

Prior to the Plant transfer, ULH&P received power through full requirements wholesale power contracts with CG&E. Under traditional FERC ratemaking principles, these contracts were priced at CG&E's cost. In 1996, however, FERC issued Order 888

to promote competition in the wholesale power market by requiring transmission providers to grant open access transmission service. In Order 888, FERC stated that wholesale power suppliers would not be required to serve full requirements customers after their current contracts expired. As a result, full requirements customers would need to either build or buy their own generation, or enter into a contract with a wholesale power supplier at market-based rates.

ULH&P's then-current wholesale power contract was scheduled to expire on January 1, 2002. CG&E notified this Commission in November 1999 that CG&E would no longer supply wholesale power to ULH&P at cost-based rates after the contract expired. ULH&P and CG&E resolved this matter, and other pending ULH&P regulatory matters, in 2002 by entering into a new wholesale power contract, scheduled to expire December 31, 2006. This was a market-based, fixed price contract under which ULH&P received a monthly demand charge of \$7,200 per megawatt ("MW") based on its peak demand for the month, and an energy charge of \$24 per megawatt-hour ("MWH").

The Commission's May 11, 2001 Order in Case No. 2001-00058 approved ULH&P's new retail rates to recover the costs of this contract. This contract provided wholesale power for ULH&P's customers at an around-the-clock ("ATC") price of \$36.60/MWH, while the market-based price in May 2001 was estimated at \$41.29/MWH.¹ The Commission's Order also required ULH&P to analyze the cost of building new power plants in its next integrated resource plan, so that ULH&P's customers would be assured a long-term power supply at the lowest reasonable cost.

ULH&P addressed these Commission concerns by obtaining the Plants from CG&E. The parties proposed for CG&E to transfer the Plants to ULH&P at CG&E's net book value. CG&E also committed to provide back-up power for East Bend No. 2 and Miami Fort No. 6 through 2009.

Terms of the Back-up Supply Contract

ULH&P witness Robert C. McCarthy explained the proposed back-up supply contract in his testimony, which Mr. M. Stephen Harkness adopted at the hearing. A copy of the contract, as filed with Mr. McCarthy's 2003 testimony, is enclosed with this letter. The contract provided the following terms:

- Back-up capacity and firm energy for East Bend No. 2 and Miami Fort No. 6 for scheduled and non-scheduled outages. The contract contemplated that CG&E and ULH&P would jointly plan their scheduled outages such that CG&E could supply back-up power in an economical manner.

¹ *In the Matter of the Application of The Union Light, Heat and Power Company for Certain Findings Under 15 U.S.C. §79Z (Order at 3)(May 11, 2001).*

- Back-up power was intended to be priced at market rates.² The contract provided for an energy charge and monthly capacity charges of \$359,729 for East Bend No. 2 and \$61,866 for Miami Fort No. 6. The energy charge was priced at the average variable cost per MWH of energy produced during the prior calendar month at the Plant for which back-up power is required. The capacity charge was based on the market price and an estimate of how often ULH&P would require back-up power for East Bend and Miami Fort 6. The market price was estimated by using the forward market prices quoted from the Megawatt Daily and off-peak prices quoted from the North American Power 10x Report.³
- The contract was an “Into Cinergy” product, providing for CG&E to deliver the back-up energy at the busbars of the Plants and at interconnection points between the Cinergy transmission system and generating or transmission facilities owned by third parties.
- The term of the contract was through December 31, 2009.

The Commission’s December 5, 2003 Order noted that the contract was ultimately subject to FERC approval.⁴ The Commission stated that the contract was reasonable and stated that the contract’s monthly capacity charges should be recoverable through rates in ULH&P’s next retail electric base rate case.⁵ The Commission noted that the contract’s energy charges should be recoverable under ULH&P’s fuel adjustment clause.⁶

The Two-Year Period After the Commission’s December 2003 Interim Approval of Back-up Supply Contract

The following material changes occurred after the Commission granted interim approval of the Plant transfer and the back-up supply contract:

- The U.S. Securities and Exchange Commission (“SEC”) did not approve the transaction until November 29, 2005, nearly two years after this Commission’s interim approval.⁷
- FERC clarified its rules for approval of affiliate wholesale power contracts in 2004, indicating that it would be difficult to obtain FERC approval for such a contract without a competitive bidding process.⁸

² *In the Matter of The Application of The Union Light, Heat and Power Company for a Certificate of Public Convenience and Necessity to Acquire Certain Generation Resources and Related Property; for Approval of Certain Purchase Power Agreements; for Approval of Certain Accounting Treatment; and for Approval of Deviation from Requirements of KRS 278.2207 and 278.2213(6), Case No. 2005-00228* (Testimony of Robert C. McCarthy at page 3, line 22 through page 4, line 1)(July 21, 2003).

³ *Id.* at page 4, lines 10-17.

⁴ *Id.* (Order at 22)(December 5, 2003).

⁵ *Id.* (Order at 31-32)(December 5, 2003).

⁶ *Id.* (Order at 32)(December 5, 2003).

⁷ *Id.* (Notice of Filing of SEC Approval)(December 6, 2005).

- The Midwest Independent Transmission System Operator, Inc. (“MISO”) commenced its Day 2 electric energy markets on April 1, 2005, providing a market clearing price and joint dispatch of all generating resources participating in the MISO’s markets. Additionally, the MISO Day 2 markets provide for commercial delivery nodes and congestion costs applicable to each delivery node.
- In 2005, CG&E terminated its Joint Generation Dispatch Agreement with PSI Energy, Inc., its Indiana affiliated operating company, effective January 1, 2006. Additionally, CG&E, PSI and ULH&P, among other Cinergy affiliates, implemented market-based wholesale power tariffs with codes of conduct. The codes of conduct effectively prevent ULH&P and CG&E from sharing information on scheduled outages or events which might result in unscheduled outages.⁹

CG&E committed during the January 11, 2005 Informal Conference to stand by the terms of the back-up power supply contract, yet these last two events, which occurred later in 2005, materially changed the circumstances existing in January 2005.

For example, CG&E and ULH&P can no longer share information on scheduled outages, and events which could cause unscheduled outages, as contemplated in the proposed 2003 contract. This prevents CG&E and ULH&P from jointly planning their outage schedules. This substantially impacts CG&E’s ability to provide back-up power in an economical manner.

As another example, the original contract as drafted in 2003 was an “Into Cinergy” product, which would allow a seller to deliver power to any point within Cinergy’s control area. This product no longer exists. Under MISO Day 2, there are many commercial pricing nodes as delivery points, which would allow a winning bidder, in a competitive bidding process, to deliver to any commercial pricing node within the Cinergy control area, and ULH&P’s customers would bear the resulting congestion costs, which could be substantial. ULH&P’s original proposal for the back-up supply contract did not address this issue.

Proposed Alternative to the Back-up Supply Contract

The original intent of the back-up supply contract was to obtain a back-up supply of power for East Bend No. 2 and Miami Fort No. 6 at market-based prices. ULH&P has considered various alternatives to the back-up power contract, such as putting this

⁸ See *Allegheny Energy Supply Company, LLC*, Docket No. ER04-730-000, 108 F.E.R.C. ¶ 61,082, 2004 FERC LEXIS 1569 (Order Granting Authorization to Make Affiliate Sales)(July 29, 2004).

⁹ *In the Matter of The Application of The Union Light, Heat and Power Company for a Certificate of Public Convenience and Necessity to Acquire Certain Generation Resources and Related Property; for Approval of Certain Purchase Power Agreements; for Approval of Certain Accounting Treatment; and for Approval of Deviation from Requirements of KRS 278.2207 and 278.2213(6)*, Case No. 2005-00228 (September 2005 Compliance Filing of The Union Light, Heat and Power Company, attaching copy of ULH&P’s FERC market-based tariff, including code of conduct)(September 16, 2005).

proposed contract out to bid; drafting a new contract adapted to the MISO Day 2 markets and soliciting bids; entering into a bilateral contract with a third party for capacity and/or energy under various pricing terms; or relying on the MISO Day 2 energy markets for back-up power.

ULH&P believes that the best alternative is to obtain back-up power from the MISO Day 2 energy markets and that is what we propose to do. ULH&P believes that the MISO Day 2 energy markets have improved liquidity and, even though the electric commodity continues to exhibit inherent volatility, the MISO Day 2 markets have helped to dampen the volatility of energy prices. These energy purchases in the marketplace will be made primarily for outage purposes and only when they represent the most economic alternative for our customers, all things considered. As a result, ULH&P proposes to recover the costs of this economic energy from customers via the fuel adjustment clause, similar to ULH&P's 2003 proposal to recover the energy costs under the back-up power supply contract through the fuel adjustment clause.

Recognizing the need to provide customers with some insulation from volatility in the market, ULH&P further proposes to cap the price of back-up energy purchased in the marketplace at the dispatch cost of the Woodsdale Generating Station, presently \$116/MWH. This cap would remain in effect through December 31, 2009, the term of the proposed back-up supply contract. Furthermore, to reflect that the back-up need for ULH&P is primarily an energy need and not a capacity need, ULH&P proposes to eliminate the approximate \$5 million annual demand payment that was included in the terms of the earlier draft back-up agreement.

ULH&P recognizes that the cap on energy costs is significantly higher than the cost contained in ULH&P's former wholesale power contract with CG&E, or the cost reflected in the back-up power contract as proposed in 2003. Yet ULH&P was unable to execute that contract in 2003, for lack of full regulatory approval, and is unable to execute the contract now, because FERC would not approve such a contract between affiliates, one of which is deregulated, and the attendant information sharing contemplated by the original contract. ULH&P's new proposal benefits customers by providing a cap on the market price for back-up power – even though the parties intended in the 2003 proposal to provide a market price with no cap.


This approach has the following benefits:

- obtains the needed energy for customers through the MISO Day 2 markets, which have been very liquid and have seen low levels of volatility.
- while giving customers the benefits of access to the marketplace for energy, protects customers against the impacts of extreme spikes in the cost for wholesale power during periods when East Bend or Miami Fort have outages.
- by eliminating the demand payments, ensures that customers pay only the actual cost of replacement power or, at most, the cap amount which, in any given year, could be less than the demand payment structure contained in the draft back-up agreement.

- avoids the need for FERC approval of a wholesale power contract with CG&E, if ULH&P put the contract out for bid and CG&E won the bid.
- avoids any performance risk and credit risk related to contracting with an unaffiliated third party.
- avoids unnecessary congestion costs.

We appreciate your consideration of the matters raised in this letter. We look forward to discussing all of these matters at the upcoming informal conference.

Sincerely,


John J. Finnigan, Jr.
Senior Counsel

JJF/sew

cc: Hon. Richard G. Raff (with enclosure)
Hon. Dennis G. Howard, II (with enclosure)
Hon. Elizabeth E. Blackford (with enclosure)
Hon. Michael L. Kurtz (with enclosure)

BACK-UP POWER SALE AGREEMENT

This Back-up Power Sale Agreement (the "Agreement") is entered into as of this _____ day of _____ 2003 ("Effective Date") by and between The Cincinnati Gas & Electric Company, an Ohio corporation, ("CG&E" or "Seller") and its affiliate The Union Light, Heat and Power Company, a Kentucky corporation ("ULH&P") (each individually a "Party" or collectively the "Parties").

RECITALS

WHEREAS, ULH&P is an affiliate of Seller and an existing entity purchasing Energy from Seller; and

WHEREAS, ULH&P owns generating units located in Rabbit Hash, KY ("East Bend 2") and North Bend, Ohio ("Miami Fort 6") that are used to serve ULH&P's native load;

WHEREAS, ULH&P desires to purchase Back-up Capacity and Energy from Seller and Seller desires to sell Back-up Capacity and Energy to ULH&P pursuant to the Cinergy Operating Companies' FERC Electric Tariff, Original Volume No. 9;

NOW, THEREFORE, for and in consideration of the mutual covenants contained herein, the Parties agree as follows:

ARTICLE I DEFINITIONS

1.1 The following definitions and any terms defined in this Agreement shall apply hereunder.

"Back-up Capacity" means Seller's obligation to provide and ULH&P's right to receive Firm Capacity when East Bend 2 and/or Miami Fort 6 are partially or fully unavailable to generate Energy for non-economic reasons, such as a plant outage for maintenance or an unscheduled outage due to equipment failure.

"Back-up Energy" means Firm Energy sold by Seller to ULH&P when East Bend 2 and/or Miami Fort 6 would otherwise actually be generating electric power pursuant to economic dispatch but are partially or fully unavailable to generate Energy for non-economic reasons, such as a plant outage for maintenance or an unscheduled outage due to equipment failure.

"Business Day" means a day on which Federal Reserve member banks in New York City are open for business; and a Business Day shall open at 8:00 a.m. and close at 5:00 p.m. eastern prevailing time, unless otherwise agreed to by the Parties in writing.

“Capacity” means Seller’s obligation to hold generating capability and/or purchased power in reserve to meet the needs of ULH&P when East Bend 2 and/or Miami Fort 6 are partially or fully unavailable to generate Energy for non-economic reasons, subject to the terms and conditions of this Agreement.

“Energy” means electric energy of the character commonly known as three-phase, sixty-hertz electric energy that is delivered at the nominal voltage of the Points of Receipt, expressed in megawatt hours (MWh).

“Firm” means that the only excuse for the failure to deliver Energy by Seller or the failure to receive Energy by ULH&P is Force Majeure or the other Party’s failure to perform.

“Force Majeure” means an event or circumstance which prevents one Party from performing its obligations under this Agreement, which event or circumstance was not anticipated as of the Effective Date, which is not within the reasonable control of, or the result of the negligence of, the Party (or in the case of third party obligations or facilities, the third party) claiming suspension (the “Claiming Party”), and which, by the exercise of due diligence, the Claiming Party, or third party, is unable to overcome or avoid or cause to be avoided. Force Majeure shall not be based on (a) Seller’s ability to sell Energy to another market at a more advantageous price; or (b) Seller’s inability to buy Energy for ULH&P at an advantageous market price. Interruption by a Transmission Provider shall not be deemed to be an event of Force Majeure unless (i) the Party contracting with such Transmission Provider shall have made arrangements with such Transmission Provider for firm transmission, as defined under the Transmission Provider’s tariff, of Energy to be delivered or received hereunder and (ii) such interruption is due to force majeure as defined under the Transmission Provider’s tariff.

“Interest Rate” means, for any date the lesser of (a) two (2) percent over the per annum rate of interest equal to the prime lending rate (“Prime Rate”) as may be published from time to time in the Federal Reserve Statistical Release H.15; or (b) the maximum lawful interest rate.

“Liquidated Damages” has the meaning attributed to such term in Section 6.1.1.

“Nonperforming Party” has the meaning attributed to such term in Section 6.1.

“Performing Party” has the meaning attributed to such term in Section 6.1.

“Points of Delivery” means the agreed points of delivery of Energy as set forth in Attachment A and incorporated herein by reference.

“Points of Receipt” means the agreed points of receipt of Energy as set forth in Attachment A and incorporated herein by reference.

“Quantity” means that quantity of Energy that Seller agrees to make available to sell and deliver, or cause to be delivered, to ULH&P, and that ULH&P agrees to purchase and receive, or cause to be received, from Seller pursuant to the terms of this Agreement.

“Replacement Price” means the price at which ULH&P, acting in a commercially reasonable manner, purchases substitute Energy for that not delivered by Seller, plus any additional transmission charges incurred by ULH&P to the Points of Delivery; or, absent any such purchase, the market price for such Quantity at such Points of Delivery, as determined by ULH&P in a commercially reasonable manner; *provided, however*, in no event shall the Replacement Price include any Penalties, ratcheted demand or similar charges or any stranded costs.

“Term” has the meaning attributed to such term in Section 2.6.

ARTICLE II SERVICES TO BE RENDERED

- 2.1 Back-up Capacity and Energy. Seller hereby agrees to sell and deliver to ULH&P at the designated Points of Receipt, and ULH&P agrees to purchase and receive from Seller a Quantity of ULH&P’s requirements for Back-up Capacity and Energy. Resale by ULH&P of Back-up Energy provided by Seller pursuant to this Agreement except to ULH&P’s end use retail customers is neither contemplated nor permitted. The Energy provided under this Agreement is intended to be available to ULH&P only during such times as East Bend and/or Miami Fort 6 would actually be generating electric power (not including ramp-up time) because it is economic to operate the plant and is intended to allow ULH&P to replace the exact amount of lost capacity from East Bend 2 and/or Miami Fort 6 if either or both plants are partially or fully unavailable for non-economic reasons.
- 2.2 Point of Receipt. Seller will sell and deliver to ULH&P at the designated and applicable Points of Receipt, specified in Attachment A. Seller will be responsible for transmission and ancillary services to the designated Points of Receipt. As more fully set forth below, ULH&P will be responsible for all distribution, transmission and ancillary services in order to transmit the Energy from the Points of Receipt.
- 2.3 Energy Charge. For Back-up Energy sold and delivered by Seller due to an outage at East Bend 2, ULH&P shall pay Seller per MWh scheduled and delivered, a fee equal to East Bend 2’s variable operating costs per MWh (including fuel, operating and maintenance expense, and emission allowances) of energy produced during the previous calendar month.

For Back-up Energy sold and delivered by Seller due to an outage at Miami Fort 6, ULH&P shall pay Seller per MWh scheduled and delivered, a fee equal to Miami Fort 6's average variable operating costs per MWh (including fuel, operating and maintenance expense, and emission allowances) of energy produced during the previous calendar month.

- 2.4 Capacity Charge. For the right to receive Back-up Energy from Seller for an outage at East Bend 2, ULH&P shall pay Seller a fixed monthly capacity charge of three hundred fifty-nine thousand seven hundred and twenty-nine dollars (\$359,729) for each calendar month during the Term of this Agreement.

For the right to receive Backup Energy for Seller for an outage at Miami Fort 6, ULH&P shall pay Seller a fixed monthly capacity charge of sixty-one thousand eight hundred and sixty-six dollars (\$61,866) for each calendar month during the Term of this Agreement.

- 2.5 Quantity/Product. When an outage occurs at East Bend 2, Seller shall be obligated to sell and deliver up to an amount of Firm Energy with Liquidated Damages to ULH&P such that the amount of Energy available to ULH&P from East Bend 2 during the outage plus the amount of Firm Energy supplied by Seller equals 414 MW.

When an outage occurs at Miami Fort 6, Seller shall be obligated to sell and deliver up to an amount of Firm Energy with Liquidated Damages to ULH&P such that the amount of Energy available to ULH&P from Miami Fort 6 during the outage plus the amount of Firm Energy supplied by Seller equals 163 MW.

- 2.6 Term. This Agreement shall, subject to approval of the FERC, become effective when the Plants are transferred to ULH&P and shall continue in full force and effect until December 31, 2009.

ARTICLE III TRANSMISSION, SCHEDULING AND DELIVERIES

- 3.1 Transmission. ULH&P is responsible for purchasing network integration transmission service and ancillary services for delivery from the Points of Receipt to ULH&P's transmission system interconnection and for executing an Interconnect Agreement with Cinergy Services, Inc. on behalf of CG&E and PSI Energy, Inc. or succeeding RTO/ISO or equivalent. The network integration transmission service and ancillary charges will be the rates set forth in the applicable Open Access Transmission Tariff (OATT), and includes those charges required to deliver Energy from the Point of Receipt to the Point of Delivery. This transmission service charge payable by ULH&P includes all charges for ancillary services under tariff schedules (Schedules 1, 2, 3, 4, 5 & 6) and includes loss factors for transmission service. This transmission service charge is consistent with, and subject to, any revisions to the applicable OATT.

ULH&P has the right to designate Seller as agent to coordinate all transmission services. If ULH&P elects this right, it will provide Seller with 30 days advance written notice.

- 3.2 Scheduling and Notice. The Parties acknowledge that East Bend 2 and Miami Fort 6 will be economically dispatched along with Seller's generating assets, and that the determination of the Quantity of Energy taken by ULH&P under this Agreement will be performed on an after-the-fact basis in accordance with the terms of that Purchase, Sales and Operation Agreement entered into between ULH&P and Seller to be executed concurrently with this Agreement. Thus, ULH&P shall not be required to schedule for the delivery of any Back-up Energy taken under this Agreement.
- 3.3 Seller's and ULH&P's Obligations. With respect to the Agreement, Seller shall sell and deliver, or cause to be delivered, and ULH&P shall purchase and receive, or cause to be received, at the Points of Receipt, the Quantity, and ULH&P shall pay Seller the Energy Charge and the Capacity Charge set forth herein. Seller shall be responsible for any taxes, costs, losses or charges imposed on or associated with the delivery of the Quantity up to the Points of Receipt. ULH&P shall be responsible for any taxes, costs, losses or charges imposed on or associated with the Quantity at and from the Points of Receipt. Each Party shall indemnify, defend and hold harmless the other Party for and against any taxes for which such Party is responsible under this Section 3.3.
- 3.4 Title, Risk of Loss and Indemnity. As between the Parties, Seller shall be deemed to be in exclusive control and possession of the Quantity prior to the Points of Receipt, and ULH&P shall be deemed to be in exclusive control and possession of the Quantity at and from the Points of Receipt. Seller warrants that it will deliver the Quantity to ULH&P at the Points of Receipt free and clear of all liens, claims and encumbrances arising or attaching prior to the Points of Receipt. Title to and risk of loss related to the Quantity shall transfer from Seller to ULH&P at the Points of Receipt. Seller and ULH&P shall each indemnify, defend and hold harmless the other Party from claims, damages or injuries arising from an occurrence when title to the Energy is held by the indemnifying Party.
- 3.4 Relative Responsibilities. Neither Party assumes any responsibility with respect to the construction, installation, maintenance or operation of the system of the other Party. In no event shall one Party be liable to the other party for damage or injury to any person or property, whatsoever, arising, occurring or resulting from, in any manner, the receiving, transmission, control, use, application or distribution of said Energy. Each party shall use reasonable diligence to maintain its facilities in proper and serviceable condition, and shall take reasonable steps and precautions for maintaining the services agreed to be provided and received under this Agreement.

ARTICLE IV METERING, BILLING AND PAYMENT

- 4.1 Metering. The Energy delivered to ULH&P shall be measured by suitable recording instruments. ULH&P will provide dial-up access to the meters at all of ULH&P's Points of Delivery as specified in Attachment A. This load data will provided to Seller on a monthly basis by the 10th day of the following calendar month. If ULH&P fails to provide this dial-up access, Seller may terminate this Agreement. Seller has the right to audit ULH&P's metering records and tapes to ensure that ULH&P is complying with the terms of this Agreement.
- 4.2 Billing Period. Unless otherwise agreed upon, the calendar month shall be the standard billing period for all settlements under this Agreement.
- 4.3 Payment of Bills. The net monthly bill, which shall consist of a period of approximately thirty (30) days between meter readings, as established by Seller, shall be paid on or before the twentieth (20th) day of the month following the calendar month of the service.
- 4.4 Payment Method – All such payments shall be made by electronic transfer in immediately available funds to an account designated in writing by Seller.
- 4.5 Late Payment. Overdue payments shall accrue interest at the Interest Rate from, and including, the due date to, but excluding, the date of payment.
- 4.6 Billing Disputes. If ULH&P, in good faith, disputes an invoice, ULH&P shall immediately notify Seller of the basis for the dispute and pay the portion of such statement not in dispute no later than the due date. If any amount withheld under dispute by ULH&P is ultimately determined to be due to Seller, it shall be paid within one (1) Business Day after such determination, along with interest accrued at the Interest Rate from the original due date until the date paid. Inadvertent overpayments shall be returned by the receiving Party upon request or deducted by the receiving Party from subsequent payments.

ARTICLE V FORCE MAJEURE

- 5.1 Performance Excused. If either Party is rendered unable to carry out, in whole or part, its obligations under this Agreement due to Force Majeure then, during the pendency of such Force Majeure but for no longer period, the Party affected by the Force Majeure shall be relieved of its obligations insofar as they are affected by Force Majeure (other than any obligation to make payments then due or becoming due with respect to performance which occurred prior to the Force Majeure); *provided, however,* ULH&P shall be obligated to pay Capacity charges with respect to this Agreement notwithstanding the existence of a Force Majeure. The Party affected by the Force Majeure shall provide the

other Party with written notice setting forth the full details thereof, including the anticipated duration of the Force Majeure event, as soon as practicable after the occurrence of such event and shall take all reasonable measures to mitigate or minimize the effects of such Force Majeure; *provided, however*, that this provision shall not require Seller to deliver, or ULH&P to receive, Energy at points other than the Points of Receipt.

ARTICLE VI DEFAULTS AND REMEDIES

- 6.1 Unless excused by Force Majeure or ULH&P's failure to perform, if Seller fails to deliver the Quantity, ULH&P shall give notice of such failure as promptly as reasonably practicable. ULH&P shall be entitled to receive from Seller an amount calculated as follows ("Liquidated Damages"): (Seller shall pay ULH&P, on the date payment would otherwise be due to Seller, an amount for each MWh of such deficiency equal to the positive difference, if any, obtained by subtracting the per unit Price from the per unit Replacement Price.
- 6.2 Events of Default. An "Event of Default" shall mean, with respect to a Party ("Defaulting Party"), the occurrence of any of the following:
- (a) the failure to make when due, any payment required pursuant to this Agreement if such failure is not remedied within two (2) Business Days after written notice of such failure is given by the other Party, and provided the payment is not the subject of a good faith dispute as described in Section 4.6.
 - (b) the failure of the Defaulting Party to perform any covenant set forth in this Agreement and such failure is not excused by Force Majeure or cured within two (2) Business Days after written notice thereof to the Defaulting Party;
 - (c) any representation or warranty made by the Defaulting Party herein shall at the time prove to be false or misleading in any material respect;
 - (d) the Defaulting Party (i) files a petition or otherwise commences or acquiesces in a proceeding under any bankruptcy, insolvency, reorganization or similar law, or has any such petition filed against it (ii) makes an assignment or any general arrangement for the benefit of creditors, (iii) otherwise becomes bankrupt or insolvent (however evidenced); or (iv) is unable to pay its debts as they fall due.
- 6.3 Remedies upon an Event of Default. Upon the occurrence of an Event of Default with respect to a Defaulting Party, the Non-Defaulting Party shall have the right, without prior notice, to liquidate and terminate this Agreement at any time, and shall calculate, in a commercially reasonable manner, any remaining amounts due under the Agreement.

- 6.4 Notwithstanding any other provision of this Agreement, upon the occurrence of an Event of Default, or an event that, with the giving of notice or the passage of time or both, would constitute an Event of Default with respect to a Party, the other Party shall have the right to suspend performance of this Agreement.

ARTICLE VII LIMITATIONS; DUTY TO MITIGATE

- 7.1 Limitation of Remedies, Liability and Damages. The Parties confirm that the express remedies and measures of damages provided in this agreement satisfy the essential purposes hereof. For breach of any provision of this agreement for which an express remedy or measure of damages is provided, such express remedy or measure of damages shall be the sole and exclusive remedy, the obligor's liability shall be limited as set forth in such provision and all other remedies or damages at law or in equity are waived.

If no remedy or measure of damages is expressly provided herein, the obligor's liability shall be limited to direct actual damages only, such direct actual damages shall be the sole and exclusive remedy and all other remedies or damages at law or in equity are waived. Unless expressly provided herein, neither Party shall be liable for any consequential, incidental, punitive, exemplary or indirect damages, lost profits or other business interruption damages, by statute, in tort or contract, under any indemnity provision or otherwise. It is the intent of the Parties that the limitations herein imposed on remedies and the measure of damages be without regard to the cause or causes related thereto, including the negligence of any Party, whether such negligence is sole, joint or concurrent, or active or passive. To the extent any damages required to be paid hereunder are liquidated, the Parties acknowledge that the damages are difficult or impossible to determine, otherwise obtaining an adequate remedy is inconvenient and the liquidated damages constitute a reasonable approximation of the harm or loss.

- 7.2 Duty to Mitigate. Each Party agrees that it has a duty to mitigate damages and covenants that it will use commercially reasonable efforts to minimize any damages it may incur as a result of the other Party's performance or non-performance of this Agreement.

ARTICLE VIII GOVERNING LAW - DISPUTE RESOLUTION

- 8.1 Governing Law and Jurisdiction. THIS AGREEMENT AND THE RIGHTS AND DUTIES OF THE PARTIES HEREUNDER SHALL BE GOVERNED BY AND CONSTRUED, ENFORCED AND PERFORMED IN ACCORDANCE WITH THE LAWS OF THE STATE OF OHIO, WITHOUT REGARD TO PRINCIPLES OF CONFLICTS OF LAW. All disputes hereunder or relating hereto shall be resolved in the Federal or State courts of Ohio located in the County of Hamilton and each Party hereby irrevocably submits to the *in personam* jurisdiction of such courts. Each Party hereby

waives its respective right to any jury trial with respect to any litigation arising under or in connection with this Agreement.

ARTICLE IX MISCELLANEOUS

- 9.1 Assignment. Any assignment of this Agreement or any rights or obligations hereunder by Seller shall be made only with the written consent of ULH&P, except that such written consent shall not be required by Seller for any such assignments to an affiliate. Any assignment of this Agreement or any rights or obligations hereunder by ULH&P shall be made only with the written consent of Seller.
- 9.2 Corporate Guaranty. Prior to the Effective Date of this Agreement, Seller will obtain a corporate guaranty from Cinergy Corp., guaranteeing Seller's obligations under this contract to ULH&P.
- 9.3 Notices. All notices, requests, statements or payments shall be made as specified below. Notices required to be in writing shall be delivered by letter, facsimile or other documentary form. Notice by regular mail shall be deemed to have been received three (3) Business Days after it has been sent. Notice by facsimile or hand delivery shall be deemed to have been received by the close of the Business Day on which it was transmitted or hand delivered (unless transmitted or hand delivered after close of normal business hours, in which case it shall be deemed to have been received at the close of the next Business Day). Notice by overnight mail or courier shall be deemed to have been received two (2) Business Days after it has been sent. A Party may change its addresses by providing notice of the same in accordance with this Section 9.3.

To Seller:

NOTICES & CORRESPONDENCE:

Regular Mail: CG&E.

Mail Code EA503

139 East Fourth Street

Cincinnati, Ohio 45202

Attn: Contract Administrator

Overnight Mail

CG&E

Mail Code EA503

221 East Fourth Street

Cincinnati, OH 45202

Attn: Contract Administrator

PAYMENTS:

Check: Cinergy Services Inc.

Cinergy Bulk Power

1415 Solutions Center

Chicago, IL 60677-1004

Electronic Transfer

PNC Bank, Ohio

ABA# 042000398

Acc# 4000600813

Account Name: Cinergy

INVOICES:

Attention: Billing Department
Mail Code: EA402
Fax Number: 513-419-5790
Phone Number: 513-419-5165

SCHEDULING:

Attention: Scheduling
Phone Number: 513-419-5112

To ULH&P:

NOTICES & CORRESPONDENCE:

ULH&P
EA 503
139 East Fourth Street
Attention: Contract Administrator

INVOICES:

Attention: Billing Dept.
Fax Number: 513-419-5790
Phone Number: 513-419-5165

SCHEDULING:

Attention: Scheduling
Phone Number: 513-419-5112

- 9.4 General. This Agreement constitutes the entire agreement between the Parties relating to the subject matter contemplated by this Agreement. No amendment or modification to this Agreement shall be enforceable unless set forth in writing and executed by both Parties. This Agreement shall not impart any rights enforceable by any third party (other than a permitted successor or assignee bound to this Agreement). No waiver by a Party of any default by the other Party shall be construed as a waiver of any other default. Any provision declared or rendered unlawful by any applicable court of law or regulatory agency or deemed unlawful because of a statutory change will not otherwise affect the remaining lawful obligations that arise under this Agreement. The headings used herein are for convenience and reference purposes only. All indemnity and audit rights contained herein shall survive the termination or expiration of this Agreement for three (3) years.
- 9.5 Audit. Each Party has the right, at its sole expense, during normal business hours, and upon reasonable notice, to examine the records of the other Party to the extent reasonably necessary to verify the accuracy of any statement, charge or computation made pursuant to this Agreement. If any such examination reveals any inaccuracy in any statement, the necessary adjustments in such statement and any payments related thereto shall be made promptly. Any interest due with respect to underpayment or overpayment shall be calculated as set forth in Sections 4.5 and 4.6 as applicable; *provided, however*, that no adjustment for any statement or payment will be made unless objected to within two (2) years from the rendition thereof.

The Parties have caused this Agreement to be executed by their duly authorized representatives in multiple counterparts as of the Effective Date.

**The Union Light, Heat and Power Company
Company**

The Cincinnati Gas & Electric

By: _____

By: _____

Title: _____

Title: _____

Date: _____

Date: _____

ATTACHMENT A

A.1 Points of Receipt. At the Effective Date of the Agreement, Seller hereby agrees to sell and deliver Energy to ULH&P at the busbars of the generating units owned by the Seller and at the points of interconnection between the Cinergy transmission system and the generating facilities or transmission system of others ("Points of Receipt").

A.2 Points of Delivery. This Agreement is subject to ULH&P executing an Interconnect Agreement with Cinergy Services, Inc. or succeeding RTO/ISO equivalent specifying the Points of Delivery as set forth below.

Points of Delivery:

Name of Substation	Voltage
Augustine	<ul style="list-style-type: none"> • At 138 kV Air Break No. 857 (supply to 132-13.2 kV TB1) • At 138 kV Air Break No. 864 (supply to 132-13.2 kV TB5)
Bellevue	<ul style="list-style-type: none"> • At 138 kV Air Break No. 925 (supply to 132-13.2 kV TB1) • At 138 kV Air Break No. 936 (supply to 132-13.2 kV TB2)
Buffington	<ul style="list-style-type: none"> • At 138 kV Air Break No. 931 (supply to 132-66 kV TB1) • At 138 kV Circuit Breaker No. 941 (supply to 132-66 kV TB2) • At 138 kV Circuit Breaker No. 935 (supply to 138-13.09 kV TB3) • At 138 kV Circuit Breaker No. 942 (supply to 138-13.09 kV TB4) • At 138 kV Circuit Breaker No. 946 (supply to 138-13.09 kV TB7)
Cold Spring	<ul style="list-style-type: none"> • At 138 kV Air Break No. 867 (supply to 132-13.2 kV TB1)
Constance	<ul style="list-style-type: none"> • At 138 kV Air Break No. 976 (supply to 132-13.2 kV TB2)
Crescent	<ul style="list-style-type: none"> • At 138 kV Air Break No. 837 (supply to 132-13.2 kV TB1) • At 138 kV Air Break No. 854 (supply to 132-13.2 kV TB2)
Donaldson	<ul style="list-style-type: none"> • At 138 kV Air Break No. 977 (supply to 132-13.2 kV TB1) • At 138 kV Air Break No. 984 (supply to 132-13.2 kV TB2)

Florence	<ul style="list-style-type: none"> At 138 kV Air Break No. 857 (supply to 132-13.2 kV TB1) At 138 kV Air Break No. 863 (supply to 132-13.2 kV TB4) At 138 kV Air Break No. 864 (supply to 132-13.2 kV TB2)
Hands	<ul style="list-style-type: none"> At 138 kV Air Break No. 837 (supply to 132-13.2 kV TB1)
Hebron	<ul style="list-style-type: none"> At 138 kV Circuit Switcher No. 886 (supply to 138-13.09 kV TB1)
Kenton	<ul style="list-style-type: none"> At 138 kV Circuit Breaker No. 981 (supply to 132-66 kV TB4)
Kentucky University	<ul style="list-style-type: none"> At 138 kV Air Break No. 963 (supply to 132-13.2 kV TB4)
LaFarge	<ul style="list-style-type: none"> At 138 kV Air Break No. 872 (Feeder 5983 supply to 138kV customer)
Newport Steel 138Kv Station No. 1	<ul style="list-style-type: none"> At 138 kV Air Break No. 959 (Feeder 5986 supply to 138kV customer)
Newport Steel 138Kv Station No. 2	<ul style="list-style-type: none"> At 138 kV Air Break No. 975 (Feeder 5986 supply to 138kV customer)
Newport Steel 69Kv Station	<ul style="list-style-type: none"> At 66kV Air Break Nos. 1008 and 1040 (Feeder 2166 to 69kV customer)
Wilder	<ul style="list-style-type: none"> At 138 kV Circuit Breaker No. 831 (supply to 132-66 kV TB2) On 69kV Bus 2 between Circuit Breaker Nos. 646 & 650 At 138 kV Circuit Breaker No. 835 (supply to 138-13.09 kV TB3)
Feeder 2862A	<ul style="list-style-type: none"> At 69 kV Air Break No. 539 (supply to Feeder 2862B) At Tower 29 (supply to Feeder 2862C)
Feeder 1524	<ul style="list-style-type: none"> 12.47 kV feed from West End Substation to Kentucky
West End 41	<ul style="list-style-type: none"> 12.47 kV feed from West End Substation to Kentucky
West End 46	<ul style="list-style-type: none"> 12.47 kV feed from West End Substation to Kentucky
West End 48	<ul style="list-style-type: none"> 12.47 kV feed from West End Substation to Kentucky

Modifications or additions to Points of Delivery shall be made only with the written consent of Seller.