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Ms. Elizabeth O'Donnell  
Executive Director  
Public Service Commission of Kentucky  
211 Sower Boulevard  
Frankfort, Kentucky 40602

**Kentucky Utilities Company**  
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November 16, 2006

RE: *In the Matter of: The Application of Kentucky Utilities Company for an Order Authorizing the Issuance of Securities and the Assumption of Obligations, Case No. 2006-00390*

Dear Ms. O'Donnell:

I am writing to advise that, on November 13, 2006, the Virginia State Corporation Commission approved the application of Kentucky Utilities Company d/b/a Old Dominion Power Company to eliminate its secured debt. A copy of the Virginia State Corporation Commission's Order is attached. Similarly, on November 6, 2006, the Tennessee Regulatory Authority voted to approve the contemplated transaction, contingent upon approvals from the Kentucky Public Service Commission and the Virginia State Corporation Commission.

Kentucky Utilities Company respectfully requests that the Commission enter an Order in the above-captioned proceeding, simultaneously with its Order in LG&E's companion proceeding (Case No. 2006-00445), on or before December 12, 2006.

Should you have any questions concerning the enclosed, please do not hesitate to contact me.

Sincerely,

Allyson K. Sturgeon

Enclosures

COMMONWEALTH OF VIRGINIA  
STATE CORPORATION COMMISSION

AT RICHMOND, NOVEMBER 13, 2006

APPLICATION OF

KENTUCKY UTILITIES COMPANY  
d/b/a OLD DOMINION POWER COMPANY

CASE NO. PUE-2006-00098

For authority to issue securities under Chapter 3 of Title 56 of the Code of Virginia and to engage in an affiliate transaction under Chapter 4 of Title 56 of the Code of Virginia

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STATE CONTROL

ORDER GRANTING AUTHORITY

On September 14, 2006, Kentucky Utilities Company, d/b/a/ Old Dominion Power Company ("Applicant" or the "Company"), filed an application with the State Corporation Commission ("Commission") requesting authority to issue securities under Chapter 3 of Title 56 of the Code of Virginia ("Code") and to engage in an affiliate transaction under Chapter 4 of Title 56 ("Affiliates Act") of the Code. Applicant paid the requisite fee of \$250.

Applicant is a wholly owned subsidiary of E.ON U.S. LLC ("E.ON US"). E.ON US is an indirect subsidiary of the multinational holding company, E.ON AG ("E.ON"). Fidelity Corporation ("Fidelity") is a finance company subsidiary of E.ON US Holding GmbH, another subsidiary of E.ON. Applicant requests authority to issue up to \$53,000,000 of unsecured notes to Fidelity, which lends money to companies in the E.ON holding company system.

The Company intends to use the proceeds from the unsecured loan from Fidelity ("Fidelity Notes") to defease and discharge the \$53,000,000 outstanding principal amount of the Company's 7.92% First Mortgage Bonds, Series P, due May 15, 2007 ("Series P Bonds"). The Series P Bonds are not redeemable, therefore defeasance is required for the Company to be released from obligations concomitant to the Series P Bonds. To defease the Series P Bonds, the Company will be required to deposit an amount of cash or U.S. Treasury securities with a bond

trustee that will be sufficient to cover both the principal and accrued interest on the Series P Bonds when they mature. Applicant estimates the cost to defease the Series P Bonds will be approximately \$100,000 inclusive of incremental interest charges, trustee and legal fees.

Applicant states that the interest rate, maturity, and other terms on the Fidelity Notes will be based on market conditions at the time of issuance. The interest rate will depend on the maturity of the Fidelity Notes, which will not exceed a period of 30 years. In addition, the interest rate on the Fidelity Notes will be at the lowest of: i) the effective cost of capital for E.ON; ii) the effective cost of capital for Fidelity; and iii) the Company's effective cost of capital as determined by reference to the Company's cost of a direct borrowing from an independent third party for a comparable term loan (the "Best Rate Method"), as described in the application. Applicant further requests authority to enter into one or more interest rate hedging agreements (T-Bill lock, swap or similar agreement, collectively the "Intercompany Loan Hedging Facility") either with an affiliate within the E.ON system or with a bank or financial institution. Applicant states that the Intercompany Loan Hedging Facility will be an interest rate agreement designed to lock in the underlying interest rate on the Fidelity Notes in advance of closing on the loan.

Applicant also requests authority to assume obligations under various agreements necessary for the issuance one or more series of new County of Carroll, Kentucky, Environmental Facilities Revenue Bonds (the "Refunding Bonds") up to the aggregate principal amount of \$54,000,000. Proceeds from the Refunding Bonds will be used to redeem the \$54,000,000 principal amount of County of Carroll, Kentucky, Solid Waste Disposal Facilities Revenue Bonds ("Kentucky Utilities Project") 1994 Series A Bonds, due November 1, 2024 ("Series A Bonds").

To obtain the most advantageous financing based on market conditions at the time of issuance, Applicant requests broad authority to negotiate terms and conditions of the Refunding Bonds. The Refunding Bonds would be issued pursuant to one or more indentures ("Indentures") between Carroll County and one or more trustees ("Trustees"). Proceeds from the sale of the Refunding Bonds would be loaned to the Company pursuant to one or more loan agreements

with Carroll County (the "Loan Agreements"). Upon issuance of the Refunding Bonds, the Company may enter into one or more guaranties (the "Guaranties") in favor of the Trustees to guarantee the Company's payment of all or any part of the obligations under the Refunding Bonds.

The Refunding Bonds will be sold in one or more underwritten public offerings, negotiated sales, or private placement transactions. The maturity of the Refunding Bonds will at a minimum extend through 2024, and may be extended further as permitted under current tax laws. The Refunding Bonds may be issued as fixed rate or variable rate debt, to be determined based on negotiations between the Company, Carroll County, and the purchasers of the bonds. If a variable rate option is chosen, the Refunding Bonds may include provisions to convert to other interest rate modes. In addition, the Refunding Bonds may include a tender purchase provision that would require entering into remarketing agreements with one or more remarketing agents. Applicant may also need to enter into one or more liquidity facilities to provide immediate funding to pay for bonds tendered for purchase and not remarketed. Such facilities would require entering into one or more credit agreements and possibly a promissory note to each facility provider to secure repayments by Applicant.

In connection with the issuance of the Refunding Bonds, Applicant further requests authority to enter into one or more interest rate hedging agreements that may be in the form of an interest rate cap, swap, collar, or similar agreement (collectively the "Hedging Facility") with a bank or financial institution. Applicant states that the Hedging Facility will be an interest rate agreement designed to allow the Company to actively manage and to limit its exposure to variable interest rates or to lower its overall borrowing costs on any fixed rate Refunding Bond.

Applicant states that the purpose for issuing the Fidelity Notes and the Refunding Bonds is to reduce the existing and prospective administrative costs and burdens associated with the Company's last two issues of debt secured under the Indenture of Mortgage or Deed of Trust dated May 1, 1974, as Amended (the "Company Indenture"). Applicant states that some of the documentation and procedures required for Security and Exchange Commission ("SEC")

compliance or to obtain lien releases whenever property covered by the Company Indenture is to be sold are antiquated, inefficient, and no longer necessary. Applicant notes that it has a total of \$108 million of secured intercompany debt that remains outstanding from authority previously granted in Case Nos. PUE-2003-00065, PUE-2003-00404, and PUE-2005-00023. Applicant states that Fidelia Corporation will release its lien on the Company's assets to prevent the \$108 million of secured Fidelia debt from having seniority to the Company's other debt.

Applicant expects the authority requested will generate some cost increases on non-insured floating rate debt due to a one notch ratings decline for the change from secured to unsecured debt and an expected 7 basis point increase in the bond insurance premium on one series of debt. However, Applicant's analysis supports that such increases in costs will be more than offset by administrative savings and interest savings related to maturity extensions. After consideration of all related costs and savings, the Company's analysis indicates the authority requested will result in a net present value savings of \$942,964.

THE COMMISSION, upon consideration of the application and having been advised by Staff, is of the opinion and finds that approval of the application will not be detrimental to the public interest. Accordingly,

IT IS ORDERED THAT:

- 1) Applicant is hereby authorized to issue and deliver unsecured Fidelia Notes in an aggregate principal amount not to exceed \$53,000,000 in the manner and for the purposes as set forth in its application, through the period ending December 31, 2007.
- 2) To the extent required under the Affiliates Act, the Company and Fidelia are authorized to modify the existing intercompany debt to allow Fidelia to release its lien on the Company.
- 3) Applicant is authorized to execute and deliver and perform the obligations of the Company under *inter alia*, the Loan Agreements with Fidelia, the Fidelia Notes authorized in Ordering Paragraph (1), and such other agreements and documents as set out in its Application, and to perform the transactions contemplated by such agreements.

4) Applicant is authorized, with regard to the Refunding Bonds, to execute, deliver and perform the obligations of the Company under *inter alia*, the Loan Agreements with Carroll County, Kentucky and under any Guarantees, remarketing agreements, hedging agreements, auction agreements, bond issuance agreements, Credit Agreements, Facilities and such other agreements and documents as set forth in the Application and to perform the transactions contemplated by such agreements up to the underlying \$54,000,000 aggregate balance of Refunding Bonds.

5) Applicant shall submit a Preliminary Report of Action within ten (10) days after the issuance of any securities pursuant to Ordering Paragraphs (1) and (4) (collectively referenced as "Proposed Debt"), to include the type of security, the issuance date, amount of the issue, the interest rate, the maturity date, and a brief explanation of reasons for the term of maturity chosen.

6) Within sixty (60) days after the end of each calendar quarter in which any of the Proposed Debt is issued pursuant to Ordering Paragraphs (1) and (4), Applicant shall file with the Commission a detailed Report of Action with respect to all Proposed Debt issued during the calendar quarter to include:

- (a) The issuance date, type of security, amount issued, interest rate, date of maturity, issuance expenses realized to date, net proceeds to Applicant, and an updated cost/benefit analysis that reflects the impact of any hedging facility for any Proposed Debt issued to defease or refund other outstanding debt prior to maturity, if an update is applicable;
- (b) A summary of the specific terms and conditions of each hedging facility and an explanation of how it functions to lock in or manage the interest rate on the underlying portion of Proposed Debt; and
- (c) The cumulative principal amount of Proposed Debt issued under the authority granted herein and the amount remaining to be issued;
- (d) A copy of all agreements related to the issuance of Refunding Bond; and

- (e) A copy of the document(s) that verify the release of Fidelia's lien on the Company from all previously authorized issues of secured intercompany debt.

7) Applicant shall file a final Report of Action on or before March 31, 2008, to include all information required in Ordering Paragraph (6) along with a balance sheet that reflects the capital structure following the issuance of the Proposed Debt. Applicant's final Report of Action shall further provide a detailed account of all the actual expenses and fees paid to date for the Proposed Debt with an explanation of any variances from the estimated expenses contained in the Financing Summary attached to the application.

8) *Approval of the application shall have no implications for ratemaking purposes.*

9) This matter shall be continued, subject to the continuing review, audit, and appropriate directive of the Commission.

AN ATTESTED COPY hereof shall be sent by the Clerk of the Commission to: Kendrick R. Riggs, Esquire, Stoll, Keenon, Ogden, PLLLC, 1700 PNC Plaza, 500 West Jefferson Street, Louisville, Kentucky 40202; and to the Commission's Division of Economics and Finance.