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PUBLIC SERVICE
COMMISSION

DUKE ENERGY CORPORATION

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Kristen Cocanougher
Sr. Paralegal
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VIA HAND DELIVERY

December 17, 2012

Mr. Jeff Derouen
Executive Director
Kentucky Public Service Commission
211 Sower Blvd
Frankfort, KY 40601

Re: In the Matter of the Application of Duke Energy Kentucky, Inc. for an Order Authorizing the Issuance of Unsecured Debt and Long-Term Notes, Execution and Delivery of Long-Term Loan Agreements, and Use of Interest Rate Management Instruments
Case No. 2012-

And

In the Matter of the Application of Duke Energy Kentucky, Inc. for an Order to Enter into up to \$25,000,000 Principal Amount of Capital Lease Obligations
Case No. 2012-

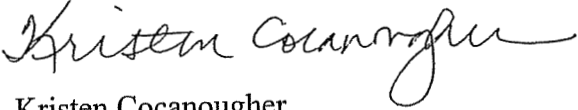
Dear Mr. Derouen:

Enclosed please find an original and twelve copies of the above-referenced Applications.

Please assign a separate case number for each enclosed Application and file-stamp and return two extra copies of each in the enclosed overnight envelope.

Feel free to contact me should you have any questions.

Sincerely,

A handwritten signature in cursive script that reads "Kristen Cocanougher". The signature is fluid and connected, with a prominent loop at the end of the last name.

Kristen Cocanougher

cc: Dennis Howard II.

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of the Application of Duke Energy)
Kentucky, Inc. for an Order to Enter into up to)
\$25,000,000 Principal Amount of Capital Lease) Case No. 2012-_____
Obligations)

**APPLICATION FOR CAPITAL LEASE AUTHORITY AND REQUEST FOR INTERIM
EXTENSION OF CURRENT AUTHORITY**

Pursuant to KRS 278.300 and 807 KAR 5:001 Sections 8 and 11, Duke Energy Kentucky, Inc. (“Duke Energy Kentucky”) respectfully requests that the Commission authorize Duke Energy Kentucky to issue capital leases, and enter into all necessary agreements and other documents relating thereto, as more fully described herein. In addition, Duke Energy Kentucky respectfully requests the Commission issue an order granting an extension of the Company’s existing leasing authority approved in Case No. 2010-00370 but set to expire December 31, 2012, until the Commission issues an order approving the new authority requested in this case. Duke Energy Kentucky does not anticipate a need, nor does it intend to enter into any new transactions during this interim period, but out of an abundance of caution wishes to maintain such flexibility should the need suddenly arise. The Company agrees to abide by all reporting requirements contained under the current authority during this interim period.

In support of this Application, Duke Energy Kentucky states as follows:

1. **Address:** Duke Energy Kentucky is a Kentucky corporation with its principal place of business at 4580 Olympic Street, Erlanger, Kentucky 41018. Duke Energy Kentucky's principal executive office is 139 East Fourth Street, Cincinnati, Ohio 45202.

2. **Articles of Incorporation:** Pursuant to 807 KAR 5:001, Section 8(3), Duke Energy Kentucky states that a certified copy of its Articles of Incorporation, as amended, on file with this Commission in Case No. 2009-202 and is hereby incorporated by reference.

3. **Statement of Business:** Duke Energy Kentucky is a utility as defined in KRS 278.010(3)(a) and (b), engaged in providing retail gas and electric services to its customers in Northern Kentucky in various municipalities and unincorporated areas of Kenton, Campbell, Boone, Gallatin, Grant, and Pendleton Counties. Duke Energy Kentucky is thus subject to the Commission's jurisdiction.

4. **807 KAR 5:001 Section 11(1)(a).** As of September 30, 2012, the original cost of Duke Energy Kentucky's property was \$1,713,956,000. The Company's principal properties consist of electric generating plants, and gas and electric distribution facilities.

5. **807 KAR 5:001 Section 11(1)(b).** Duke Energy Kentucky proposes, with the necessary consent and authority of this Commission, to enter into from time to time over a period ending December 31, 2014, up to \$25 million principal amount of capital lease obligations ("Capital Leases"). Duke Energy Kentucky proposes to utilize Capital Leases purely as another form of financing its capital requirements. The Capital Leases will have structures and terms similar to other forms of debt financing, but with the potential, in certain instances, to lower the overall cost associated with financing property acquisitions.

Capital Leases will be used to finance new property, including construction, or re-finance existing property, in order to optimize the cost of financing commensurate with such property's

expected life (such property being more fully described in “Property Expected to be Leased” below).

Advantages of Leasing. Leasing can allow Duke Energy Kentucky to access lower cost funds. One reason for this is because lessors often have a higher credit rating than Duke Energy Kentucky, and therefore, can secure capital at a lower cost. Capital leasing may also deliver lower cost funds because the lessor may be better able to use the tax depreciation benefits than the lessee, thus lowering the cost of financing. Some portion of this lower cost may be passed on to Duke Energy Kentucky, along with a spread for profit to the lessor, which usually is at a cost below what Duke Energy Kentucky could have obtained otherwise.

Established financing practices are employed to determine whether ownership or lease (including sale/leaseback) of certain assets is the appropriate method of financing. The impact on earnings and cash flow for available financing alternatives are analyzed.

Capital lease financing is similar to debt except that for certain acquisitions it can be more easily tailored to match the useful life of the acquisition. It is often more effective to enter into a capital lease whose maturity is concurrent with an asset’s useful life than to issue a large amount of bonds for a basket of assets having various useful lives. When compared to bonds, the effective cost of capital lease financing may be lower due to reduced transaction costs. And, in the case of variable rate leases, small interest spreads over short-term borrowing indexes such as London Interbank Offered Rate (“LIBOR”) may be negotiated, thus making Capital Leases a cost-effective source of financing which may lower overall utility costs.

Property Expected to be Leased. The property expected to be leased will consist of equipment used in Duke Energy Kentucky’s operations including, but not limited to, meters, computers and office equipment, and intangible property such as software and site licenses

(collectively, the "Property"). The Property may also include land, plant or equipment in service, plant under construction or land, plant or equipment to be acquired or constructed.

Accounting. Duke Energy Kentucky proposes to account for the Capital Leases as prescribed by the Federal Energy Regulatory Commission Uniform System of Accounts as currently in effect.

The amount financed under each Capital Lease, excluding transaction costs, is not expected to be more than the net capitalized cost of the Property or the appraised value of the Property (in the event more than the capitalized cost is financed).

In accordance with generally accepted accounting principles, the net capitalized cost of property usually includes installation, training, allowance for funds, administrative overhead and other costs capitalized in connection with acquiring and placing the property in service. Such costs are expected to be included in the Property cost financed under a Capital Lease.

Method of Transacting Capital Leases. To effectuate the lease transactions, Duke Energy Kentucky will: (1) obtain third-party lease financing for Property acquisitions; or (2) in the case of existing Property, sell the Property to a third-party finance lessor ("Lessor"), and simultaneously therewith Duke Energy Kentucky will lease the Property back from the Lessor. In connection therewith, the terms of each Capital Lease will be approved by Duke Energy Kentucky's Board of Directors, or by such persons authorized by the Board, and it is anticipated that an agreement setting forth the terms of each Capital Lease will be executed.

In the case of new Property that is acquired or constructed, the Lessor will either: (a) pay the vendor and Duke Energy Kentucky for their respective costs associated with the acquisition; or (b) reimburse Duke Energy Kentucky for the capitalized cost of the property, with Duke

Energy Kentucky concurrently paying the vendor the invoice cost; this latter option being undertaken solely to allow for administrative efficiencies.

Related Agreements. Duke Energy Kentucky may enter into one or more participation agreements with its affiliates and the Lessor in connection with the Capital Leases, with such agreements defining Duke Energy Kentucky's role as principal and, as applicable, agent on behalf of its affiliates for billing and payment remittance purposes. Such arrangements will be undertaken solely for administrative efficiencies and convenience of the parties involved.

End of Term Options. At the end of each initial or renewal lease term, it is anticipated that Duke Energy Kentucky will have an option to either: (a) renew each Capital Lease pursuant to arm's length negotiation with the then existing Lessor or other lessors; (b) purchase the Property; or (c) terminate the Capital Lease.

Pricing Parameters. Duke Energy Kentucky has parameters within which the final negotiated Capital Leases, including sale and leasebacks, and rental obligations will fall, and requests authority to execute Capital Leases of the Property within such parameters. The parameters, as set forth in Exhibit A, would allow Duke Energy Kentucky to consummate transactions when it believes it is prudent to do so provided the terms are within the parameters.

Commission Authorization. Duke Energy Kentucky requests that the Commission issue its order authorizing the Capital Leases now, prior to the time Duke Energy Kentucky reaches specific agreement with respect to the terms of such lease transactions, to provide the Company flexibility in entering into the leases. Such Commission approval will not relieve Duke Energy Kentucky of its responsibility to obtain the best terms available for the structure selected and, therefore, it is appropriate and reasonable for this Commission to authorize Duke Energy Kentucky to agree to such terms and prices consistent with said parameters.

6. **807 KAR 5:001 Section 11(1)(c).** The proceeds from the Capital Lease obligations are expected to be used: (a) for necessary acquisitions of property, and estimated capital expenditures of approximately \$41.4 million in 2012 and \$51.3 million in 2013 and \$99.6 million in 2014; (b) for re-financing existing property; (c) for such additional expenditures as contemplated by KRS 278.300; or (d) for other lawful corporate purposes. Therefore, Capital Lease transactions are necessary and appropriate for and consistent with the proper performance by Duke Energy Kentucky of its services to the public, will not impair its ability to perform those services, and are reasonably necessary and appropriate for such purposes.

7. **807 KAR 5:001 Section 11(1)(d).** See Exhibit B concerning estimated capital expenditures, attached hereto, and made a part hereof. Duke Energy Kentucky does not currently have any specific agreements other than those entered into under the existing authority and as reported to the Commission in 2010-00370. Duke Energy Kentucky requests that the Commission issue its order authorizing the Capital Leases now, prior to the time Duke Energy Kentucky reaches specific agreement with respect to the terms of such lease transactions, to provide the Company flexibility in entering into the leases. Duke Energy Kentucky will notify the Commission of the terms of any such agreements if and when the Company enters in to a Capital Lease.

8. **807 KAR 5:001 Section 11(1)(e).** This section is not applicable, since no specific discharge of obligations is contemplated at this time from transacting the Capital Leases.

9. **807 KAR 5:001 Section 11(1)(f).** In Case No. 2010-00370, the Commission approved up to \$25 million in principal amount of Capital Lease obligations for the period ending December 31, 2012. As of September 30, 2012, there remained approximately \$25 million of available authority.

10. **807 KAR 5:001 Section 6 and Section 11(2)(a).** Duke Energy Kentucky is filing the following information in Exhibit C, which is incorporated herein and made a part of this application:

<u>Exhibit C</u> <u>Page</u>	<u>Description</u>	<u>807 KAR 5:001</u> <u>Section Reference</u>
	Financial Exhibit	6 and 11 (2) (a)
1	Amount and kinds of stock authorized	6 (1)
1	Amount and kinds of stock issued and outstanding	6 (2)
1	Terms of preference or preferred stock	6 (3)
1	Brief description of each mortgage on property of Duke Energy Kentucky	6 (4)
1-2	Amount of bonds authorized and issued and related information	6 (5)
3	Notes outstanding and related information	6 (6)
2	Other indebtedness and related information	6 (7)
4	Dividend information	6 (8)
4-6	Detailed Income Statement and Balance Sheet	6 (9)

11. **807 KAR 5:001 Section 11(2)(b).** This section is not applicable, as there are no related deeds of trust or mortgage documents relevant to this application.

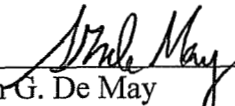
12. **807 KAR 5:001 Section 11(2)(c).** The proposed construction is primarily comprised of installations, improvements and extensions in the ordinary course of business as a utility. It is therefore impractical to submit maps and plans pertaining thereto.

13. As previously stated, Duke Energy Kentucky's current leasing authority, approved in Case No 2010-00370, is set to expire on December 31, 2012. As such, Duke Energy

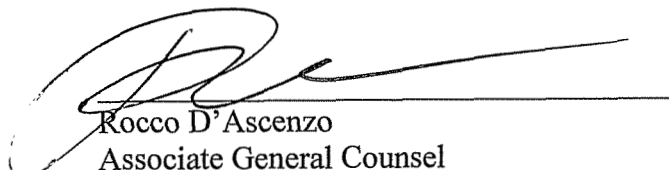
Kentucky respectfully requests the Commission issue an initial order, prior to the expiration of the current authority, extending such authority for an interim period until the Commission issues its decision on the above-captioned request. While Duke Energy Kentucky does not anticipate a need to enter into any new transactions during this interim period, the Company believes it is prudent and in the public interest to maintain such flexibility should a need suddenly arise.

WHEREFORE, Duke Energy Kentucky respectfully requests that the Commission issue an initial order granting an interim extension of its existing leasing authority for an interim period and issue an order authorizing Duke Energy Kentucky to enter into up to \$25 million principal amount of Capital Leases, including sale and leasebacks, for the purposes herein stated and in a manner as herein set forth, and authorizing Duke Energy Kentucky to account for such Capital Leases in the manner as herein set forth.

DUKE ENERGY KENTUCKY, INC.

By: 
Stephen G. De May
Vice President and Treasurer

Its Attorneys:

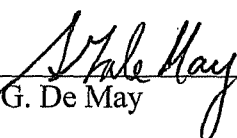


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VERIFICATION

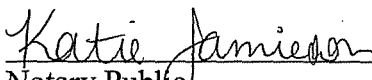
State of North Carolina)
) SS:
County of Mecklenburg)

Stephen G. De May, being first duly sworn, states that he is Vice President and Treasurer of Duke Energy Business Services LLC; that he has read the foregoing application; and that the contents are true to the best of his knowledge, information and belief.



Stephen G. De May

Subscribed and sworn to before me, this 12 day of December, 2012.



Katie Jamieson
Notary Public

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Duke Energy Kentucky, Inc.

Capital Lease Parameter Summary

- Property Description:** The property expected to be leased will consist of equipment used in Duke Energy Kentucky's operations including, but not limited to, meters, computers and office equipment, and intangible property such as software and site licenses (collectively, the "Property"). The Property may also include land, plant or equipment in service, plant under construction or land, plant or equipment to be acquired or constructed.
- Use of Proceeds:** To acquire property, fund construction expenditures, refinance existing property or for other general corporate purposes.
- Principal Amount:** Up to \$25 million, depending on the capitalized cost or appraised value of the property, plus transaction costs.
- Lessor:** One or more lessors to be named.
- Lease Term:** To be determined.
- Lease Cost:** Aggregate cost of rental payments, commitment fees and closing costs during each initial or renewal period that results in an interest rate (implicit or otherwise) that is equal to or less than those generally obtainable on capital lease financing having the same or reasonably similar terms offered to, or entered into, by utility companies or utility holding companies of the same or reasonably comparable credit quality.

Duke Energy Kentucky
Capital Expenditures
(\$ in thousands)

Expansion	2012	2013	2014
Smart Grid	\$ 800	\$ 1,300	\$ 17,800
Customer Adds	2,800	4,800	4,900
Other	2,300	2,800	3,800
Total Expansion	\$ 5,900	\$ 8,900	\$ 26,500

Maintenance	2012	2013	2014
Regulated Operations	\$ 13,800	\$ 15,500	\$ 18,300
Power Delivery	8,600	12,500	14,100
Gas Delivery	4,300	11,300	7,900
Customer Service	200	-	-
Other FE&G	(100)	1,600	900
Total Maintenance	\$ 26,800	\$ 40,900	\$ 41,200

Environmental	2012	2013	2014
Environmental Control	\$ 8,700	\$ 1,500	\$ 31,900
Total Environmental	\$ 8,700	\$ 1,500	\$ 31,900

Total Forecast Capital Expenditures	\$ 41,400	\$ 51,300	\$ 99,600
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Notes:

Includes all additions (account 107000) and retirements (account 108000), including all AFUDC



FINANCIAL EXHIBIT

(1) **Amount and kinds of stock authorized**

1,000,000 shares of Capital Stock \$15 par value amounting to \$15,000,000 par value.

(2) **Amount and kinds of stock issued and outstanding**

585,333 shares of Capital Stock \$15 par value amounting to \$8,779,995 total par value. Total Capital Stock and Additional Paid-in Capital as of September 30, 2012:

Capital Stock and Additional Paid-in Capital
As of 9/30/2012
(\$ per 1,000)

Capital Stock	\$8,780
Premiums thereon	18,839
Total Capital Contributions from Parent (since 2006)	8,594
Contribution from Parent Company for Purchase of Generation Assets	<u>140,061</u>
Total Capital Stock and Additional Paid-in-Capital	<u>\$176,274</u>

(3) **Terms of preference or preferred stock whether cumulative or participating, or on dividends or assets or otherwise.**

There is no preferred stock authorized, issued or outstanding.

(4) **Brief description of each mortgage on property of applicant, giving date of execution, name of mortgagor, name or mortgagee, or trustee, amount of indebtedness authorized to be secured thereby, and the amount of indebtedness actually secured, together with any sinking fund provision.**

Duke Energy Kentucky does not have any liabilities secured by a mortgage.

(5) **Amount of bonds authorized, and amount issued, giving the name of the public utility which issued the same, describing each class separately, and giving the date of issue, face value, rate of interest, date of maturity and how secured, together with the amount of interest paid thereon during the last fiscal year.**

The Company has three outstanding issues of unsecured senior debentures issued under an Indenture dated December 1, 2004, between itself and Deutsche Bank Trust Company Americas, as Trustee, as supplemented by one Supplemental Indenture. The Indenture allows the Company to issue debt securities in an unlimited amount from time to time. The Debentures issued under the Indenture are the following:

Supplemental Indenture	Date of Issue	Principal Amount Authorized and Issued	Principal Amount Outstanding	Rate of Interest	Date of Maturity	Interest Paid Year 2011
Not Applicable	12/9/2004	40,000,000	40,000,000	5.000%	12/15/2014	2,000,000
1 st Supplemental	3/10/2006	50,000,000	50,000,000	5.750%	3/10/2016	2,875,000
1 st Supplemental	3/10/2006	65,000,000	65,000,000	6.200%	3/10/2036	4,030,000
2 nd Supplemental	9/22/2009	100,000,000	<u>100,000,000</u>	4.650%	10/1/2019	<u>4,650,000</u>
			<u>255,000,000</u>			<u>13,555,000</u>

- (6) **Each note outstanding, giving date of issue, amount, date of maturity, rate of interest, in whose favor, together with amount of interest paid thereon during the last fiscal year.**

Not applicable.

- (7) **Other indebtedness, giving same by classes and describing security, if any, with a brief statement of the devolution or assumption of any portion of such indebtedness upon or by person or corporation if the original liability has been transferred, together with amount of interest paid thereon during the last fiscal year.**

The Company has two series of Pollution Control Revenue Refunding Bonds issued under a Trust Indenture dated as of August 1, 2006, and a Trust Indenture dated as of December 1, 2008, between the County of Boone, Kentucky and Deutsche Bank National Trust Company as Trustee. The Company's obligation to make payments equal to debt service on the Bonds is evidenced by a Loan Agreement dated as of August 1, 2006 and December 1, 2008 between the County of Boone, Kentucky and Duke Energy Kentucky. The Bonds issued under the Indentures are as follows:

**Duke Energy Kentucky
Exhibit C
Page 3 of 6**

Indenture	Date of Issue	Principal Amount Authorized and Issued	Principal Amount Outstanding	Rate of Interest	Date of Maturity	Interest Paid Year 2011
Series 2008A	12/01/2011	50,000,000	50,000,000	0.17% ⁽¹⁾	8/1/2027	86,417
Series 2010	11/24/2010	26,720,000	<u>26,720,000</u>	3.90% ⁽²⁾	8/1/2027	<u>1,042,507</u>
			<u>76,720,000</u>			<u>1,128,924</u>

(1) The interest rate represents the average floating-rate of interest on the bonds for 2011. The interest rate on the bonds resets every 35 days through an auction process.

(2) The variable-rate debt was swapped to a fixed rate of 3.86% for the life of the debt.

The Company has issued and has outstanding as of September 30, 2012 the following capital leases:

Series	Date of Issue	Principal Amount Authorized and Issued	Principal Amount Outstanding	Rate of Interest	Date of Maturity
2004	12/25/2004	2,017,084	628,815	5.010	09/25/2013
2005	12/30/2005	2,079,031	856,836	4.893	12/30/2014
2006	12/28/2006	2,406,336	1,236,647	5.000	12/30/2015
Erlanger	12/30/2006	2,100,000	1,453,022	8.634	09/30/2020
2007	12/31/2007	3,066,955	1,872,285	5.115	12/31/2016
2009	04/21/2009	3,429,432	2,442,650	4.821	04/21/2018
2010	06/18/2010	<u>955,061</u>	<u>768,016</u>	3.330	06/18/2019
		<u>16,053,899</u>	<u>9,258,271</u>		

The Company also has outstanding as of September 30, 2012, long term debt in the amount of \$851,494 associated with the July 31, 2007 sale of a gas storage cavern carrying an interest rate of 4.77% and a maturity date of July 31, 2027.

(8) Rate and amount of dividends paid during the last five (5) previous fiscal years, and the amount of capital stock on which dividends were paid each year.

DIVIDENDS PER SHARE

Year Ending*	Per Share	Total	No. of Shares	Par Value of Stock
December 31, 2007	0.00	0	585,333	8,779,995
December 31, 2008	51.25	30,000,000	585,333	8,779,995
December 31, 2009	0.00	0	585,333	8,779,995
December 31, 2010	0.00	0	585,333	8,779,995
December 31, 2011	230.64	135,000,000	585,333	8,779,995

* The Company paid a dividend per share of \$17.08 on 585,333 shares for a total dividend of \$10,000,000 during the nine months ended September 30, 2012.

(9) Detailed Income Statement and Balance Sheet

See the attached pages for the detailed Income Statement for the twelve months ended September 30, 2012 and the detailed Balance Sheet as of September 30, 2012 and December 31, 2011.

	Twelve Months Ended	
	<u>September, 30</u>	
	2012	
Operating Revenues		
Electric	\$	335,486
Gas		92,008
Total operating revenues		<u>427,494</u>
Operating Expenses		
Fuel used in electric generation and purchased power		132,446
Natural gas purchased		39,127
Operation, maintenance and other		145,293
Depreciation and amortization		45,277
Property and other taxes		12,257
Goodwill and other impairment charges		928
Total operating expenses		<u>375,328</u>
Gains on Sales of Other Assets and Other, net		447
Operating Income		<u>52,613</u>
Other Income and Expenses, net		1,896
Interest Expense		17,432
Income Before Income Taxes		37,077
Income Tax Expense		16,663
Income From Continuing Operations		20,414
Income From Discontinued Operations, net of tax		-
Net Income	\$	<u>20,414</u>

See Notes to Unaudited Condensed Financial Statements

DUKE ENERGY KENTUCKY, INC.
CONDENSED BALANCE SHEETS
(Unaudited)

(in thousands)	September 30, 2012	December 31, 2011
ASSETS		
Current Assets		
Cash and cash equivalents	\$ 7,649	\$ 9,874
Receivables (net of allowance for doubtful accounts of \$169 at September 30, 2012 and \$243 at December 31, 2011)	2,460	5,388
Receivables from affiliated companies	18,908	27,313
Notes receivable from affiliated companies	—	4,235
Inventory	41,454	36,817
Other	24,969	18,077
Total current assets	95,440	101,704
Investments and Other Assets		
Intangibles, net	551	1,301
Other	3,871	3,427
Total investments and other assets	4,422	4,728
Property, Plant and Equipment		
Cost	1,713,956	1,681,364
Less accumulated depreciation and amortization	(706,005)	(698,977)
Net property, plant and equipment	1,007,951	982,387
Regulatory Assets and Deferred Debits		
Regulatory Assets	48,838	49,973
Other	2,551	2,803
Total regulatory assets and deferred debits	51,389	52,776
Total Assets	\$ 1,159,202	\$ 1,141,595
LIABILITIES AND COMMON STOCKHOLDER'S EQUITY		
Current Liabilities		
Accounts payable	\$ 16,261	\$ 27,558
Accounts payable to affiliated companies	17,721	25,546
Notes payable to affiliated companies	2,264	—
Taxes accrued	18,683	12,195
Interest accrued	3,704	3,552
Current maturities of long-term debt	1,836	1,956
Other	25,143	19,023
Total current liabilities	85,612	89,830
Long-term Debt	339,352	340,830
Deferred Credits and Other Liabilities		
Deferred income taxes	242,528	231,102
Investment tax credits	1,201	1,776
Accrued pension and other post-retirement benefit costs	16,692	17,417
Asset retirement obligations	6,115	5,859
Regulatory liabilities	66,905	70,459
Other	29,095	29,658
Total deferred credits and other liabilities	362,536	356,271
Commitments and Contingencies		
Common Stockholder's Equity		
Common Stock, \$15.00 par value, 1,000,000 shares authorized and 585,333 shares outstanding at September 30, 2012 and December 31, 2011	8,780	8,780
Additional paid-in-capital	167,494	167,494
Retained earnings	195,428	178,390
Total common stockholder's equity	371,702	354,664
Total Liabilities and Common Stockholder's Equity	\$ 1,159,202	\$ 1,141,595