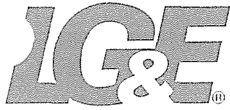

a PPL company

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PUBLIC SERVICE
COMMISSION

Louisville Gas and Electric Company
State Regulation and Rates
220 West Main Street
PO Box 32010
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Mr. Jeff DeRouen
Executive Director
Public Service Commission of Kentucky
211 Sower Boulevard
Frankfort, Kentucky 40602-0615

July 9, 2012

RE: ***Application of Louisville Gas and Electric Company for an Order Authorizing the Issuance of Securities and the Assumption of Obligations***
Case No. 2012-00233

Dear Mr. DeRouen:

Enclosed please find an original and eight (8) copies of Louisville Gas and Electric Company's response to the Commission Staff's First Information Request dated June 28, 2012, in the above-referenced matter.

Should you have any questions regarding the enclosed, please contact me at your convenience.

Sincerely,

Rick E. Lovekamp /DJH

Rick E. Lovekamp

COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF LOUISVILLE GAS AND ELECTRIC	)	
COMPANY FOR AN ORDER AUTHORIZING THE	)	CASE NO.
ISSUANCE OF SECURITIES AND ASSUMPTION OF	)	2012-00233
OBLIGATIONS	)	

RESPONSE OF
LOUISVILLE GAS AND ELECTRIC COMPANY
TO THE COMMISSION STAFF'S
INITIAL REQUEST FOR INFORMATION
DATED JUNE 28, 2012

FILED: July 9, 2012

VERIFICATION

COMMONWEALTH OF KENTUCKY)
) SS:
COUNTY OF JEFFERSON)

The undersigned, **Daniel K. Arbough**, being duly sworn, deposes and says that he is Treasurer of Louisville Gas and Electric Company and an employee of LG&E and KU Services Company, and that he has personal knowledge of the matters set forth in the foregoing responses, and that the answers contained therein are true and correct to the best of his information, knowledge and belief.

Daniel K. Arbough

Subscribed and sworn to before me, a Notary Public in and before said County and State, this 2nd day of July, 2012.

Notary Public

My Commission Expires:

April 10, 2016

LOUISVILLE GAS AND ELECTRIC COMPANY

CASE NO. 2012-00233

Response to Commission Staff's Initial Request for Information
Dated June 28, 2012

Question No. 1

Witness: Daniel K. Arbough

Q-1. Refer to LG&E's application, page 3, paragraph 7. Describe LG&E's options for First Mortgage Bond prices, maturity dates, and fixed and variable interest rates under current market conditions.

A-1. Current indicative interest rates for First Mortgage Bonds are as follows:

30 year fixed rate = 3.95%
10 year fixed rate = 2.70%
5 year fixed rate = 1.44%
5 year variable rate = 3 month LIBOR + 52 bps
3 year variable rate = 3 month LIBOR + 28 bps
2 year variable rate = 3 month LIBOR + 18 bps

These rates are exclusive of underwriting fees. The 3 month LIBOR rate as of June 29, 2012 was 0.4606%.

LOUISVILLE GAS AND ELECTRIC COMPANY
CASE NO. 2012-00233

Response to Commission Staff's Initial Request for Information
Dated June 28, 2012

Question No. 2

Witness: Daniel K. Arbough

Q-2. Refer to LG&E's application, pages 5 and 6, paragraph 14, and Exhibit 3. Describe any communication between LG&E and current lenders regarding increasing the limit under the existing Revolving Line of Credit, and the likelihood that LG&E will have to incur the additional credit facility cost shown on Exhibit 3, page 2.

A-2. In discussions at the end of June, 2012, the agent bank of the existing Revolving Line of Credit continued to express confidence in the ability to increase the size of the existing Revolving Line of Credit. The bank did indicate that the up-front fee necessary to complete the increase may need to be increased to $75,000 or $100,000 from the $50,000 shown in Exhibit 3, page 1.

LOUISVILLE GAS AND ELECTRIC COMPANY

CASE NO. 2012-00233

Response to Commission Staff's Initial Request for Information Dated June 28, 2012

Question No. 3

Witness: Daniel K. Arbough

Q-3. Refer to LG&E's application, Exhibit 2.

a. Provide any changes to projected expenditures due to LG&E's and Kentucky Utilities Company's recent decision not to purchase the gas-fired generating facility of Bluegrass Generation Company, L.LC.

b. Explain whether LG&E has an estimated timetable for future financing related to the projected construction expenditures.

A-3.

a. LG&E's anticipated capital expenditures for 2012 will be decreased by $75.9 million due to the decision not to purchase Bluegrass Generation Company, LLC.

b. LG&E currently expects to finance projected construction expenditures with short-term debt until short-term debt accumulates to the point where it can be replaced by index eligible First Mortgage Bonds. At this time, LG&E expects to issue First Mortgage Bonds in early 2013. However, LG&E will continue to evaluate the possibility of issuing First Mortgage Bonds earlier in the event an increase in interest rates is anticipated.

LG&E monitors capital market conditions via numerous daily and weekly publications received from commercial banks, investment banks, and investment management firms. The consensus among market participants is that interest rates will remain at very low levels for an extended period of time. On June 20 the Federal Reserve indicated that a subdued inflation outlook and current economic conditions warrant maintaining short-term Federal Funds rates at exceptionally low levels at least through late 2014, and the market has confidence in these statements. The June employment report released on July 6 was weak and bolsters the Federal Reserve's view that continued low interest rates are necessary to improve the employment environment. The economic turmoil in Europe also has reinforced the safe haven status of the U.S. dollar which has kept U.S. interest rates very low. Perhaps the best indication of the market's view of future interest rate movements is the pricing for a

six month forward starting swap that was referenced in paragraph 9 on page 4 of the financing application. The indication suggests that the market's view of where long-term interest rates will be six months in the future is only .15% above the current levels.

Question No. 4

Witness: Daniel K. Arbough

Q-4. Refer to LG&E's application, Exhibit 5, pages 2 and 3, item (5). Explain when the 2003 Series A and the 2007 Series B bonds must be remarketed or bought back by LG&E, the anticipated interest rate at the end of the intermediate term, and the relative advantage of remarketing the bonds at intermediate terms as opposed to some other arrangement.

A-4. The 2003 Series A bonds are fixed at a rate of 1.65% for a period of five years ending on April 3, 2017 ("Mandatory Purchase Date"). The 2007 Series B bonds are fixed at a rate of 1.60% for a period of five years ending on June 1, 2017 ("Mandatory Purchase Date"). At the Mandatory Purchase Date, LG&E will be required to remarket the bonds or repurchase them. Interest rates remain at historical lows at the short-end of the tax-exempt yield curve, but the curve becomes quite steep beyond five years with tax-exempt yields exceeding taxable yields beyond 5 years. LG&E elected a five year term for the remarketing of both bonds in order to extend to the longest tenor where tax-exempt rates were comparable to taxable yields while retaining the tax-exempt status of the bonds. Although taxable and tax-exempt rates are very close today, the Company believes there will be value in the tax-exempt status of the bonds in the future. It is not possible to predict the interest rate at the end of the 5-year intermediate term.

LOUISVILLE GAS AND ELECTRIC COMPANY

CASE NO. 2012-00233

Response to Commission Staff's Initial Request for Information
Dated June 28, 2012

Question No. 5

Witness: Daniel K. Arbough

Q-5. Explain whether proceeds of the First Mortgage Bond debt or the increase in the Revolving Line of Credit will be used to retire short-term debt. The explanation should specifically address whether LG&E has considered rolling short-term debt into lower interest fixed or variable rate mortgage bonds considering the relatively low interest rates currently available for long-term financing.

A-5. LG&E currently has no short-term debt outstanding. LG&E expects to finance projected construction expenditures with short-term debt until short-term debt accumulates to the point where it can be replaced by index eligible First Mortgage Bonds ($250 million minimum required). Issuing index eligible bonds will enable LG&E to obtain a more attractive rate on its long-term financing. Index eligible bonds can be issued at lower rates because many investment funds are limited to purchasing only index eligible bonds thereby increasing the number of potential investors and demand for the bonds. The reason for the limitation by some investors is a view that bonds of larger series are more liquid and can be sold at fair value more easily than bonds in a smaller series.

Issuing index eligible bonds today when there is no short-term debt outstanding would result in the Company incurring interest expense per the rates quoted in the response to question number 1 on the entire amount. The proceeds would be used to pay off any amount of short-term debt outstanding at the time of issuance with the remainder invested short-term until the capital costs are incurred. The short-term investments would earn very low interest rates and much less interest income than the interest expense incurred. The same outcome would result (although in a smaller magnitude) if the Company elected to issue a smaller sized bond. LG&E will continue to evaluate the possibility of issuing First Mortgage Bonds earlier in the event an increase in interest rates is anticipated.

LOUISVILLE GAS AND ELECTRIC COMPANY

CASE NO. 2012-00233

Response to Commission Staff's Initial Request for Information
Dated June 28, 2012

Question No. 6

Witness: Daniel K. Arbough

Q-6. Explain in detail LG&E's procedures for monitoring its variable rate debt and determining when and how much of that debt should be converted to a fixed rate. Provide any written procedures that address the use, monitoring and conversion of variable rate debt.

A-6. The Company has two types of variable rate debt.

The first is variable rate long-term bonds. Variable rate long-term bonds have been utilized for tax-exempt bonds because of the steep yield curve for tax-exempt bonds. Additionally, short-term tax-exempt bond rates are generally less volatile than taxable variable rate bonds. Theoretically, if taxable rates move by 1%, tax-exempt rates should move by (1-tax rate)*1%. Consequently, the interest rate risk of a dollar of variable rate tax-exempt bonds is less than the risk of a dollar of variable taxable bonds. As noted in the response to question 1, long tenors are not available in the variable rate taxable market. There are no plans to alter the amount of variable rate long-term debt in the future.

The second type of variable rate debt is short-term debt. The debt is typically related to bank loans, commercial paper, or short-term intercompany loans and is incurred to fund working capital needs or to fund capital expenditures on an interim basis. The Company will generally keep this type of debt at or below $250 million unless there is a known short-term need that will result in the debt being paid down shortly. Once the balance approaches $250 million, the Company will look to term this debt out into long-term, fixed rate bonds. However, it is prudent to have facilities in place to allow the level of short-term debt to increase should market events prevent the conversion of short-term debt. Likewise, the Company's Treasury Department continuously monitors capital market conditions for attractive opportunities to issue long-term bonds in advance of its needs.

There is no written procedure that governs the use of variable rate debt, but the level of variable rate debt is continually monitored by LG&E's Treasury Department and reported to the chief financial officer monthly as a standard business practice.

LG&E uses short term debt as the first form of financing for capital projects. LG&E evaluates the cost-effectiveness, reasonableness, and feasibility of issuing the type of variable rate debt and determining when and how much of that debt should be converted to a fixed rate connection with the ongoing management of its debt balances and debt financings. LG&E expects to allow its short-term debt balance to accumulate to approximately $250 million, at which time first mortgage bonds would be issued in a minimum size of $250 million. Market conditions may accelerate or delay the timing of the long-term debt issuances or increase the size of such issuances.